

**FINAL DECISION OF
THE COMMUNICATIONS AUTHORITY**

**PROLONGED DELAY OF
HONG KONG TELECOMMUNICATIONS (HKT) LIMITED
IN SUBMITTING ITS REGULATORY ACCOUNTING REPORTS
UNDER UNIFIED CARRIER LICENCE NO. 008**

Telecommunications Licensee Investigated:	Hong Kong Telecommunications (HKT) Limited (“HKT”)
Issue:	Prolonged delay in submitting regulatory accounting reports by HKT
Relevant Instruments:	Special Condition (“SC”) 5.6 of HKT’s Unified Carrier Licence No. 008 (the “Licence”); and Direction issued by the Communications Authority (“CA”) pursuant thereto (the “CA Direction”)
Decision:	Breach by HKT of SC 5.6 of the Licence and the CA Direction
Sanction	Issue of warning
Case Reference:	OFCA/S/R/186/5/3 Pt.3 C

BACKGROUND

Under the Licence, HKT is required to maintain and submit appropriate accounting records to enable the CA or the Office of Communications Authority (“OFCA”) to perform their respective functions including financial monitoring of the licensee’s operation and determining the Network Turnover and actual amount of royalty-based Spectrum Utilization Fees (“SUF”) HKT needs to pay. For this purpose, an Accounting Manual for mobile carrier licensees was issued by the former

Telecommunications Authority in 2005, setting out the guidelines and requirements which each reporting party as directed by the CA shall follow in maintaining its accounting records. The Accounting Manual was revised in 2012. At present, all mobile network operators are required to implement the same accounting practices in accordance with the Accounting Manual.

2. Since March 2015, OFCA has been urging HKT via letters and emails to submit the Regulatory Reports for the financial years ending on 31 December 2014 and 31 December 2015. Not until OFCA's formal letter in January 2017 to HKT reminding it of its obligation to comply with the relevant licence conditions did HKT ultimately submit on 15 February 2017 the audited Regulatory Reports for the year ending on 31 December 2014 (viz. nearly 20 months past the stipulated deadline) and on 23 February 2017 the unaudited Regulatory Reports for the year ending on 31 December 2015 (viz. nearly 10 months past the stipulated deadline). On 14 March 2017, HKT submitted the audited Regulatory Reports for the year ending 31 December 2015 with a delay of more than 9 months, after the expiry of the period of 150 days for their submission.

OFCA'S INVESTIGATION

Contravention of Licence Condition

3. The Special Condition ("SC") 5 and the CA Direction are relevant for the CA's consideration in this case, with the particularly relevant part of the SC and CA Direction extracted as follows –

"SC 5.6 : "The licensee shall submit to the Authority in respect of the Accounts for each Business an audit report prepared by the auditor for the time being of the licensee within a specified period as determined by the Authority after the end of the Royalty Year to which they relate stating whether in the auditor's opinion the Accounts comply with the Accounting Manual." (emphasis added)

CA Direction: "Pursuant to Special Condition 5 of the Unified Carrier Licence (the "Licence") granted to Hong Kong Telecommunications (HKT) Limited (the "Licensee") on 22 October 2016, the Communications Authority (the "Authority") hereby directs the Licensee, until further notice is given in writing, to implement the accounting practices as specified in the Accounting Manual issued and as revised from time to time

by the Authority and to commence submitting as set out in Appendix E of the Accounting Manual.” (emphasis added)”

4. The frequency of the Regulatory Reports and the respective timing of submission are explicitly set out in Appendix E of the Accounting Manual, which is reproduced at **Annex**. In gist, all relevant licensees are required to submit:

- (a) a set of unaudited Regulatory Reports no later than 90 days following the end of their respective financial year; and
- (b) a set of audited Regulatory Reports no later than 150 days following the end of their respective financial year.

(The above timelines are hereinafter collectively referred to as the “stipulated deadline(s)”)

5. Based on the facts of the case and the available information, OFCA considers that there is prima facie evidence that HKT has not complied with SC 5.6 of the Licence and the CA Direction, due to the prolonged delay in the submission of its unaudited and audited Regulatory Reports for the financial years 2014 and 2015 well past the stipulated deadlines. OFCA decided to investigate the matter and sought HKT’s representations on the suspected breach of SC 5.6 and the CA Direction.

The Representations of HKT

6. OFCA invited HKT to make representations during the course of the investigation. HKT made its representations on, inter alia, the suspected breach of the concerned licence condition to OFCA on 21 February 2017. The salient points of its submission are –

- (a) HKT did not dispute the late submission of the unaudited and audited Regulatory Reports for the financial years ending on 31 December 2014 and 31 December 2015. The delay had been the result of exceptional circumstances which had been fully explained to OFCA as the Regulatory Reports were being prepared;
- (b) The prolonged lead time required for preparation of the Regulatory Reports was due to the integration of CSL and the resulting job rotation and consolidation of duties taking place

within the engineering team. As a result, it had taken around nine to twelve months for the HKT mobile engineering team to familiarize itself with the network traffic management system adopted by CSL, and then to align with the assumptions used by HKT in order to produce a set of figures which would make sense for regulatory reporting purposes. The delayed availability of the CSL network traffic usage data also interrupted the entire preparation process;

- (c) HKT staff had been in regular contact with OFCA staff regarding the status of preparation of the outstanding Regulatory Reports, and thus OFCA was kept informed of the progress. HKT had been responsive to queries raised by OFCA in the past regarding the figures contained in its Regulatory Reports and its expected timeline for submission of the outstanding reports;
- (d) HKT had experienced practical difficulties in adhering to the stipulated deadlines for submission of the Regulatory Reports. HKT noted from statements made by OFCA to the press that the other operators had also been late in submitting their Regulatory Reports. HKT therefore suggested that OFCA should review the practicality of the deadlines specified in Appendix E of the Accounting Manual; and
- (e) HKT would endeavor to submit all the outstanding Regulatory Reports (i.e. the audited Regulatory Reports for the financial years 2015 and 2016) before end of May 2017.

7. HKT made further representations on 22 March 2017 in response to the CA's Provisional Decision on the case. The salient points of its submission are as follows –

- (a) HKT considered the decision to issue a warning not unreasonable under the circumstances;
- (b) the fact that HKT managed to submit the outstanding Regulatory Reports soon after OFCA had invoked formal regulatory procedures should not in any way indicate that HKT was able to submit the 2014 and 2015 Regulatory Reports on time all along, and that it was deliberately delaying matters, or that HKT only chose to submit the reports upon threat of regulatory action being taken;

- (c) HKT had already submitted the unaudited Regulatory Reports for 2014 in October 2016 and was already targeting to submit the audited Regulatory Reports for 2014 by the middle of February before OFCA's letter of 17 February 2017. With the 2014 figures confirmed, HKT was able to submit the Regulatory Reports for 2015 soon thereafter; and
- (d) HKT expressed its apology again for the delay in submitting its Regulatory Reports and would make every effort to comply with the submission deadlines in future.

OFCA'S ASSESSMENT

8. HKT did not dispute in its representations that it had failed to submit the relevant Regulatory Reports by the stipulated deadlines. As regards the explanation in the representations that there were exceptional circumstances in this case, due to the merger of the former CSL's business, OFCA considers that the prolonged delay does not seem to be the result of deliberate acts on the part of HKT, and it was more likely to be due, as per HKT's submission, to difficulties caused by some of these extraordinary circumstances. OFCA however finds the lengthy delays, in particular the 20 months in excess of the required time period of 150 days in submitting the audited Regulatory Report for 2014 and 18 months in excess of the required time period of 90 days in submitting the unaudited Regulatory Reports for 2014, to be hardly justifiable even with allowance given for the exceptional circumstances. As for the submission of the Regulatory Reports for 2015, although the delays appear to be less severe (10 months for the unaudited report and more than 9 months for the audited report), attributing the late submission to difficulties arising from the merger, which was completed back in late 2014 is even less convincing and justifiable.

9. As for HKT's representations that OFCA had been constantly kept informed of the issues it was facing and its expected timeline for submission of the outstanding reports, this does not excuse HKT's persistent breach of the relevant licence condition nor should it be treated in any way as acceptance by OFCA or the CA of HKT's delay in submitting the outstanding reports well past the stipulated deadlines. Indeed, OFCA has made it clear to HKT that such delay was unacceptable.

10. When considering a case of delay of this kind, OFCA will take into account the extent of the delay, whether there are acceptable reasons for the delay, and the consequences of such delay before it considers whether

there is a justifiable case for recommending to the CA that it should consider taking regulatory action. As far as the Regulatory Reports for the financial years 2014 and 2015 are concerned, there are no acceptable reasons to justify the prolonged delay by HKT in submitting them. Also, it is worth noting that while OFCA's repeated requests to HKT for its submission of the outstanding Regulatory Reports had been to no avail, once OFCA invoked the formal regulatory procedure by inviting representations from HKT as to a suspected breach of licence conditions in relation to this matter, vide its letter of 17 February 2017, HKT managed to submit the outstanding audited Regulatory Reports for the financial year 2014 on 15 February 2017 followed by the unaudited and audited Regulatory Reports for the financial year 2015 on 23 February 2017 and 14 March 2017 respectively. In OFCA's opinion, it showed that HKT was able to submit the outstanding Regulatory Reports in a more timely manner had it put sufficient resources and attention to them.

11. Further, as pointed out in OFCA's letter of 17 February 2017 to HKT, the prompt submission of the Regulatory Reports is essential to facilitate the proper performance of the CA's regulatory functions including the financial monitoring and calculation of SUF payable by individual licensees. In the current case, the significant delay in submission of the Regulatory Reports for the financial years 2014 and 2015, meant that the effective performance by the CA and OFCA of their regulatory functions, including the calculation and finalization of the royalty-based SUF to be paid by HKT for the concerned periods, has been impaired. Although HKT has already paid all the Appropriate Fee to the Government and the SUF calculated for the previous royalty years, and it is not likely that HKT will need to pay additional SUF above the Appropriate Fee, and so there should be no actual financial impact on the Government, this does not excuse or lessen the seriousness of the contravention of HKT of SC 5.6 and the CA Direction in the first place.

THE CA'S CONSIDERATION AND DECISION

12. After examining the evidence of the case, the representations made by HKT and the assessment of OFCA, the CA is of the view that HKT failed to comply with SC 5.6 of the Licence and the CA Direction by its prolonged and undue delay in submitting the Regulatory Reports for the financial years 2014 and 2015.

13. In considering the sanction that it should impose, the CA has had regard to all circumstances of the case and the following mitigating factors –

- (a) the delay in submitting the unaudited and audited Regulatory Reports for the financial years 2014 and, to a lesser extent for the financial year 2015 appears to have been mainly attributable to the extraordinary circumstances arising from the merger between HKT and CSL;
- (b) in response to OFCA's investigation, HKT has taken immediate action in submitting the audited Regulatory Report for the financial years 2014 and 2015 on 15 February 2017 and 14 March 2017 respectively;
- (c) HKT has promised to comply with its licence obligation to provide the other upcoming Regulatory Reports required pursuant to SC 5.6 and the CA Direction promptly and in accordance with the deadlines which are set by its licence;
- (d) this is the first occasion that HKT has been found in breach of the relevant licence condition; and
- (e) although HKT's late submission of the unaudited and audited Regulatory Reports has impaired OFCA's work by, for example, delaying the calculation and finalisation of the royalty-based SUF payable by HKT for 2014 and 2015, given that it has already paid the Appropriate Fee to the Government, and the SUF calculated for the previous royalty years did not exceed the Appropriate Fee, it is not likely that HKT will need to pay further royalties and so there should be no actual financial impact to the Government.

14. Taking into account the nature of the breach, and the mitigating factors mentioned in paragraph 13 above, the CA considers that the issue of a warning to HKT cautioning it to strictly comply with SC 5.6 and the CA Direction in the remaining term of its Licence is, in all the circumstances of the case, proportionate and reasonable. The CA would not hesitate to direct a more severe regulatory sanction against HKT, including but not limited to a financial penalty, if it commits a similar breach in the future.

The Communications Authority
March 2017

APPENDIX E: REPORT FORMATS

- 1. Objectives**
 - The reports prescribed in the AM are illustrated in this Appendix. The intent of the report formats set out on the following pages is to provide Reporting Parties with illustrative examples of the content and format of each report described.

- 2. Frequency of reports**
 - The frequency of the reports and their respective timing are outlined on the on the following page. Reports that are to be submitted on a semi-annual basis are to include financial information for the preceding period. Reports that are to be submitted on an annual basis are to include financial information in total for the year. Information is not required by month within any report.

APPENDIX E: REPORT FORMATS

REPORT NAME	FREQUENCY	TIMING
Entity Reports		
Unconsolidated Financial Statements	Unaudited: Semi Annually	90 days after mid year / year end
1.1 Unconsolidated Balance Sheet		
1.2 Unconsolidated Profit and Loss Account		
1.3 Unconsolidated Fixed Asset Schedule		
1.4 Summary of Affiliate Transactions	Audited: Annually	150 days after year end
Reconciliation Report		
2.1 Reconciliation Statement – Audited Regulatory Reports to Audited Statutory Accounts	Audited: Annually	150 days after year end
Segment Reports under HCA		
3.1 Segment Profit and Loss Account	Unaudited: Semi Annually	90 days after mid year / year end
3.2 Net Investment by Segment		
3.3A Network Service Cost Report (3G)(*)		
3.3B Network Service Cost Report (2G) (*)		
3.3C Network Service Cost Report (2.5/2.6 GHz Frequency) (#)		
3.4 Cost of Capital Report	Audited: Annually	150 days after year end
Segment Reports under CCA		
4.1 Segment Profit and Loss Account	Unaudited: Semi Annually	90 days after mid year / year end
4.2 Net Investment by Segment		
4.3A Network Services Cost Report (3G) (*)		
4.3B Network Services Cost Report (2G) (*)		
4.3C Network Services Cost Report (2.5/2.6 GHz Frequency) (#)		
4.4 Cost of Capital Report	Audited: Annually	150 days after year end
Statement of Network Turnover		
5.1A Statement of Network Turnover and SUF (3G) (*)	Unaudited: Semi Annually	90 days after mid year / year end
5.1B Statement of Network Turnover and SUF (2G) (*)		
5.2 Statement of Network Tariff (*)	Audited: Annually	150 days after year end
Administrative Reports		
6.1 Audit Reports	Audited: Annually	150 days after year end
6.2 Audit Statutory Accounts		

(*) The report is only applicable to Reporting Parties which make use of the 2G Frequency and/or 3G Frequency for provision of Licensed Telecommunications Services.

(#) The report is only applicable to Reporting Parties which make use of the 2G Frequency in the 2.5/2.6 GHz Frequency network for provision of Licensed Telecommunications Services.