



Commission for
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DotEcon Report:

Assessment of responses to Consultation 13/88

Consultants Report

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An Coimisiún um Rialáil Cumarsáide
Commission for Communications Regulation

Abbey Court Irish Life Centre Lower Abbey Street Dublin 1 Ireland

Telephone +353 1 804 9600 Fax +353 1 804 9680 Email info@comreg.ie Web www.comreg.ie

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Prepared for ComReg

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1 Introduction

1. ComReg is preparing an award process for the release of usage rights for 2x15MHz of 1800MHz spectrum over the period 1 February 2014 to 12 July 2015. The proposals for this award were set out in ComReg's Consultation 13/88, giving interested parties an opportunity to express their views on the proposals.
2. Two operators submitted a response to Consultation 13/88: Telefónica and Vodafone. We have been asked by ComReg to assess the issues raised in these submissions.
3. This report is structured as follows:
 - Section 2 provides a summary of the responses;
 - Section 3 provides our assessment on the arguments raised; and
 - Section 4 provides an overall summary of our assessment of the consultation.

2 Summary of responses

Response submitted by Telefónica

4. Telefónica agrees with the overall approach proposed for the award, including regulatory issues associated with the award, licence conditions and proposed auction format (including the exemption from any coverage obligations and the absence of spectrum caps for this award). It also highlights the need for a rapid award to allow the available spectrum to be brought into use without delay (although they agree that in practice 1 February 2014 is likely to be the earliest possible start date for usage rights).

5. However, Telefónica disagrees with the minimum fees set for the lots available, arguing that:
 - the split of fees into an up-front payment and a Spectrum Usage Fee is unnecessary due to the short licence duration, and suggests that the fee structure be simplified by using a single one-off up-front payment;
 - the minimum fees should only be aimed at deterring frivolous participation, and set an order of magnitude smaller than the proposed minimum fees;
 - there is no basis for setting minimum fees with reference to the minimum fees used in the MBSA; and
 - minimum fees in the MBSA were too high and choked-off demand, thus basing minimum fees with reference to those in the MBSA would increase the risk that the spectrum is not allocated in this award.
6. Telefónica proposes that any spectrum that may remain unsold after this auction should be made available upon request on a first-come, first-served basis, exempt from any upfront fees, and subject to a Spectrum Usage Fee adjusted on a pro-rata basis for the licence duration.
7. Telefónica also suggests that ComReg should retain maximum flexibility to issue and amend licences with the agreement of licensees when drafting the Regulations, so that short-term assignments and amendments are possible during transition periods.

Response submitted by Vodafone

8. Vodafone welcomes the similarities between the proposals for this award and the MBSA process, and requests that the award be conducted at the earliest possible date to allow for any technical planning and preparations to take place before the proposed commencement date of 1 February 2014, with particular emphasis on the need for sufficient time between the completion of the award process and the start date for any usage rights. Vodafone agrees with the proposed auction format, the exemption from any coverage obligations for these licences and the general approach

of setting minimum fees on the basis of those used in the MBSA in order not to offer licences on more favourable terms relative to the MBSA.

9. However, Vodafone objects to the proposal that spectrum caps are not used for this award. Instead, it proposes a cap of 2x30MHz on the spectrum that any single operator may hold in the 1800MHz band in Time Slice 1.
10. Vodafone also asserts that, as the rights of use of the spectrum offered have been assigned to H3GI from 13 July 2015, any operator except H3GI would need to transition out of these lots in advance of this date. Vodafone argues that due to the short duration of the licences offered the transition period might have a material impact on the value of licences, putting H3GI at an advantage relative to other operators. To mitigate the disadvantage for operators who would have to transition out of the blocks before 13 July 2015, Vodafone proposes the Spectrum Usage Fees applicable to any operator other than H3GI is reduced by the amount corresponding to two months to reflect a shorter practical licence duration.

3 Our assessment on the arguments raised in the responses

Timing of the Award Process

11. Both Telefónica and Vodafone support a quick award process held at the earliest possible date to facilitate use of the licences from the earliest possible date. We agree that it would be beneficial to conclude the award well ahead of the start date of usage rights. However, ComReg should also provide sufficient time for interested parties to prepare for the award once the Information Memorandum is published. Therefore, ComReg's current proposal that the deadline for submission of Applications be set approximately 5-6 weeks following the date of publication of the Information Memorandum is reasonable, and we would suggest that in any case the deadline be set no earlier than 4 weeks after the date of publication of the Information Memorandum to ensure that there is no potential for unfairness towards potential bidders who

may have insufficient time to assess the opportunity. Accordingly, it may be preferable to frontload any efforts to accelerate the process and focus on an early publication of the Information Memorandum rather than on shortening the length of the award process.

Fee Structure

12. According to Telefónica, any benefits from splitting the minimum fee into an upfront payment and an on-going fee are limited in terms of making long-term strategic decisions easier for bidders. Equally, we consider that there is no clear disadvantage in splitting the minimum fee. However, using a different fee structure would be inconsistent with offering the spectrum available on similar terms as in the MBSA. In addition, requiring the full minimum fee as a single upfront payment may put some bidders at a disadvantage. Therefore, in the absence of any compelling reason to take a different approach, we consider that adopting the same fee structure as in the MBSA is preferable in order to meet ComReg's objectives.

Level of minimum fees

13. Telefónica suggests that the proposed minimum fees are too high, and that the outcome of the MBSA suggests that the minimum fees used in the MBSA choked-off demand. However, we also note that Vodafone considers that there is benefit in ensuring that licences cannot be obtained on more favourable terms than the MBSA.
14. Telefónica's suggestion that the fact that the MBSA resulted in unassigned spectrum (which is the subject of the current award) can be taken as evidence that reserve prices in the MBSA were set too high cannot be verified with the data available. There may be a number of reasons why some lots remained unsold, especially given that this was a combinatorial auction in which bids were made for packages of lots. The fact that these lots remained unsold simply indicates that none of the bidders submitted a bid for a package that included these lots along with their winning package, and does not provide any information about the level of demand

at reserve prices. Therefore, Telefónica's interpretation of the outcome of the MBSA cannot be verified. Conversely, the final prices reached in the MBSA (and also other comparable awards across Europe) suggest that the minimum fees in the MBSA were set well below the value of the rights of use of spectrum that were sold. Overall, there is no evidence that minimum prices in the MBSA were set too high and that lower prices would be necessary to ensure an efficient use of the spectrum available in the current award.

15. Deviating from the approach used for setting minimum prices in the MBSA also risks raising concerns about regulatory uncertainty. There could be undesirable long-term consequences from setting minimum prices significantly below the level used in the MBSA if this encourages parties to defer bidding for rights of use of spectrum in the hope of obtaining similar unsold rights of use of spectrum at a lower price later.

Transition Issues

16. Vodafone highlights that any possible user other than H3GI would need to transition its use out of the frequencies ahead of the end date of the licence. For this reason, it proposes that any operator other than H3GI be exempted from paying the Spectrum Usage Fees for two months, in order to reflect the shorter usable duration of the licence. Vodafone argues that this would avoid favouring H3GI.
17. Although we agree that any possible user would need to manage its use of the frequencies carefully to ensure a smooth transition at the end of the licence period, we consider that Vodafone's proposal has little merit. Attempting to mitigate any possible value differences between H3GI and any other operator through discriminatory fees might effectively rely on arbitrary administrative decisions and it is not certain that this would necessarily lead to more efficient allocation of the spectrum.
18. An efficient outcome for society requires assigning the available lots in a way that maximises the overall value of the spectrum. However, there may be a number of reasons why operators may place different value on

rights of use of spectrum of which avoiding transition costs is just one.

19. For instance, other factors that may affect the value different operators attribute to the spectrum, might include existing customer base, network topology or synergy values from complementary spectrum already held by an operator (which can be expected to be greater for those operators who hold usage rights on contiguous frequencies). Trying to in some manner correct for such differences across operators would not be efficient, impartial or reflective of actual opportunity costs. Therefore, focussing only on this aspect of value difference and implementing Vodafone's proposal would be difficult to justify.
20. Telefónica, in its response, suggests that ComReg should retain flexibility to make short-term assignments and amendments during transition periods with agreement of the licensees. We consider that ComReg should be as clear as possible about the terms of the licence in the Information Memorandum given the short duration of these licences and the limited possibility of unforeseen circumstances arising. The terms and conditions proposed by ComReg for these licences already clearly provide a certain degree of flexibility to trade or amend licences. Any further ambiguities could create uncertainty about the value of the licences, which may discourage some bidders and increase the risk of an inefficient allocation. In addition, opening the door to negotiations and amendments after the award could undermine the award if those negotiations fail; in the worst case, it could lead to strategic behaviour, as a bidder might be able to acquire the spectrum simply to deny it to its competitors, but then stall the process for issuing the corresponding licence to avoid paying the fees.

Unsold lots following the award process

21. Telefónica suggests that any lots that still remain unsold after the proposed award should be made available on first-come, first-served basis exempt from the upfront minimum fee and subject to Spectrum Usage Fees adjusted on a pro-rata basis for the licence duration, on the grounds that those lots would have remained unsold

as a result of minimum prices being too high. Telefónica does not specify if any Spectrum Usage Fees would be applicable, given that it also proposes a simple fee structure consisting of a single up-front payment and no Spectrum Usage Fees.

22. Telefónica argues that its proposal would promote an efficient use of the spectrum if demand were choked-off by excessive minimum fees. However, Telefónica's proposal could materially distort bidding incentives, by creating an incentive to suppress demand in the auction process in the hope of acquiring unsold lots cheaper afterwards. This would seriously undermine the integrity of the proposed award process, not least as it could lead to rights of use of spectrum being awarded on discriminatory terms (where some users pay the minimum fee and others do not).
23. In addition, given the proximity of the start date of Time Slice 2, there is very little scope for demand to evolve further after this award and before the start date of H3GI's licence in Time Slice 2. Consequently, any benefits from releasing spectrum that might be unassigned in this award at a later date would necessarily be small, and would need to be offset against the possible inefficiencies that could result from distorting bidding incentives in this award, and any issues that could arise from offering licences on different terms. In contrast, offering the lots in this award under the provision that any unsold lots in Time Slice 1 will not be offered at a later stage provides the correct incentives for bidders to bid truthfully in the auction.

Spectrum Caps

24. The use of spectrum caps is justified when the allocation of spectrum in the award affects the structure of the downstream market and, in particular, the intensity of downstream competition. This situation may occur if the number of operators in the market, and their spectrum endowments, is flexibly determined within the award process. This was clearly the situation in the MBSA where spectrum caps were used to avoid the possibility of asymmetric outcomes.

25. The MBSA already determined a minimum number of operators in the downstream market,¹ yielding four operators and a balanced distribution of the available spectrum. Therefore, the outcome of the current award, where only three 2x5MHz lots of short duration are offered, cannot have a material impact on the structure of the downstream market. Therefore, the use of spectrum caps in this award would constitute an unnecessary restriction on the possible outcomes that cannot be justified by any concerns about downstream competition.
26. In practice, the spectrum cap proposed by Vodafone would only be binding for Meteor, who would be able to bid for two lots, but not all three. Therefore, such a spectrum cap would only affect Meteor (who is otherwise a likely candidate to bid for the spectrum given that it holds usage rights for frequencies contiguous to those available) without any clear benefits in terms of downstream competition.

4 Summary of our views

27. The responses to the consultation broadly support the proposals for the award, and indicate a desire for the award to be concluded at the earliest possible date to facilitate efficient and timely use of the spectrum available.
28. Both Telefónica and Vodafone raised objections that are limited in scope. The counter-proposals they offered would have an effect on the price they may expect to pay for the spectrum offered, either by means of a reduction of minimum fees or by introducing measures that may suppress competition for the spectrum available to some degree. However, the arguments in support of these proposals are unconvincing. More concerning, the proposals involve offering the available spectrum on different terms than those set in the MBSA, and in some cases could result in differential treatment

¹ Without ruling out the possibility that a new operator may win lots in the award process, or acquire rights of use of spectrum in the secondary market.

of the lots available in this award. Adopting the proposals from Telefónica and Vodafone could distort bidding incentives, and create unhelpful precedent that could have undesirable consequences in the long term.

29. Having carefully considered the submissions, we are not persuaded to change the recommendations set out in our previous report for ComReg in relation to the award process, published as ComReg Document 11/89. Overall, we consider that ComReg's proposals in relation to the award and minimum fees are better suited to meet its objectives than the counter-proposals, and see no justification to make material adjustments before publishing a final Information Memorandum.

Annex: Adjustments to minimum fees following publication of CPI data for October

30. The inflation adjustment to reserve prices and SUFs presented in our previous report for ComReg in relation to the award process, published as ComReg Document 11/89, can be updated on the basis of data published in October. According to the CSO, prices rose by 0.4% between June 2012 and October 2013, as shown in Table 1.

Table 1: CSO CPI between June 2012 and October 2013²

June 2012 CPI	101.2
October 2013 CPI	101.6
Inflation between June 2012 and October 2013	0.4%

31. The reserve price of €0.791m in June 2012 prices is therefore equivalent to **€0.794m in October 2013 prices**. The updated proposed fees for the 1800MHz licences are summarised in Table 2.³

Table 2: Proposed minimum licence fees

Reserve Price	€0.794m
Annual SUF*	€0.54m

* In 2012 prices. In line with the MBSA process, the CPI adjustment to this SUF will use 1 February 2013 (i.e. the commencement date of the Liberalised Use Licences) as the starting date for the calculation of the CPI.

² See CPI index based in Dec 2011 from CSO's website: <http://www.cso.ie/en/releasesandpublications/er/cpi/consumerpriceindexoctober2013/#.Unuo9aX7X8s>

³ See ComReg Document 11/89 for details on the adjustment of fees.