



Response to consultation: Notice of Ofcom's proposal to make regulations in connection with the award of 2500-2690MHz and 2010-2025MHz

Auction information policy

In the draft Wireless Telegraphy (Licence Award) (No.2) Regulations 2008 (the 'draft Award Regulations') Ofcom has retreated from its earlier position, set out in the December 2007 consultation (which Ofcom terms the 'Auction Rules Consultation'), under which it would publish at the end of each Primary Round the aggregate demand for paired and unpaired lots, the number of remaining bidders and the packages bid for. Ofcom now proposes to publish only the aggregate demand for each category of lot. We are unclear why this change of position has occurred, and believe it would be detrimental in its effect, for two reasons:

- (1) If a bidder has a standalone valuation of spectrum (ie one which would apply whatever the distribution of spectrum at the end of auction), Ofcom's new position would act to prevent that bidder from being able to compare its own valuation with other bidders' emerging valuations. This increases the risk of the bidder overpaying for any spectrum won – the "winner's curse" – which would undermine the auction objective of arriving at an efficient allocation of spectrum in line with bidders' true valuations.
- (2) If a bidder's valuation is contingent at least in part on the number of other successful bidders, Ofcom's new position again risks leading to an inefficient outcome by preventing the bidder from seeing how many other bidders remain in the auction at any given time. In this situation, it is quite likely that a bidder could overpay in winning spectrum, or drop out of the auction too early.

For these reasons, Vodafone much prefers the earlier information disclosure regime, and strongly urges Ofcom to reconsider.

Disclosure of all primary and supplementary bids after the auction

Regulation 71 states that "*Ofcom shall complete the award process by publishing on their internet website –*

(a) details of all valid principal stage bids and all valid assignment stage bids made by each bidder".

Vodafone finds this provision troubling, given that the UK auction is relatively early in the anticipated round of auctions for largely the same spectrum bands across Europe. Although the disclosure of all bids after an auction finishes could have no impact on an isolated auction, it could yield information of potentially great significance to parties intending to bid in subsequent similar auctions.

The key area of difficulty lies in the supplementary bids round, in which a bidder might choose to enter supplementary bids for a very wide range of spectrum packages. Most of these will end up having no bearing on the result of the UK auction, but collectively they could reveal information about that bidder's general valuation approach to competing bidders in later auctions. This risk could serve to constrain the bidding behaviour of some UK auction participants, but

not others (if they expect to have little or no interest in subsequent auctions), leading to an unfair distortion in the UK auction process and possibly the outcome.

Vodafone entirely understands the desire to publish all relevant information after the auction finishes, but we would urge Ofcom to reconsider whether this really necessitates the disclosure of the precise level of all bids in the supplementary round. We think it should be possible to publish sufficient information about bids in this round so as to demonstrate that the auction outcome was in line with the draft Auction Regulations, without publishing the precise amount of all bids.

Calculation of base prices

Ofcom has described the second price rule as being the minimum price needed to ensure that no alternative bidder or combination of bidders is prepared to pay more than any winning bidder or group of bidders. However, there is a material inconsistency between the description of this second price rule as given in the Information Memorandum and the criteria as given in the draft Award Regulations:

- In similar language to previous consultations, Section 4.151 of the Information Memorandum states that:

"the total amount of the Base Prices for all Winning Principal Stage Bids will be minimised" such that

"no losing Bidder or combination of Bidders (including combinations of losing and winning Bidders), on the basis of their Bids, would be prepared to pay more than the Base Prices;" [emphasis added]

- Regulation 3 of Schedule 8 of the draft Award Regulations states that the Base Prices ("reduced winning principal stage bids") should satisfy the following test:

"the combination of the reduced winning principal stage bids submitted by the winning bidders would have been the valid combination of principal stage bids or one of the valid combinations of principal stage bids (as the case may be) having the highest total value of amounts bid." [emphasis added]

The appendix provides a brief example which illustrates the inconsistency.

The issue is material, as it concerns the actual amount that a winning bidder may pay for a licence. Of the two formulations, Vodafone prefers the former (ie the version in the Information Memorandum), not least because this is the way that we have understood Ofcom to have been describing its intention throughout the development and consultation stages of this auction. We know of no reason why the second price rule should be changed at this late stage.

Above all, however, it is essential that Ofcom should arrive at one definitive formulation of this central provision and ensure that all potential bidders are fully informed of the impact of the chosen formulation in practice.

The relevance of 'confidential information' to bidder qualification

The draft Award Regulations include a provision under which a potential applicant could be disqualified if it has obtained confidential information relating to another applicant¹. 'Confidential information' is defined as *"any information which is not in the public domain and which, if it were made public, or disclosed to another applicant (or potential applicant) or bidder or a member of their prospective bidder groups, would be likely to affect decisions that such other applicant (or potential applicant) or bidder may make in relation to the award process;"*.

¹ Regulation 8(3)(h) of the draft Award Regulations; "In making their determination under paragraph (1) OFCOM shall take into account whether ... any member of the applicant's bidder group has obtained or is obtaining or attempting to obtain confidential information relating to another applicant;"

This definition of confidential information seems very broad, especially when the potential range of applicants is so wide. Vodafone thinks Ofcom should take a fresh look at this definition to see whether it could be tightened up without undermining its core intent. At the least, the provision should include a start date (ie clarifying that any exchange of information prior to that date would not be caught). It is in no-one's interest for disputes about the possible exchange of confidential information, however ill-justified, to risk excluding genuinely independent bidders from the auction.

Number of primary bid rounds

Regulation 21(2)(d) states that the primary stage of the auction should continue if the number of individual lots exceeds nine. This seems inappropriate: if the demand for paired and unpaired lots combined is equal to or less than the spectrum available (ie the test in 21(2)(c)), the primary stage should conclude regardless of whether the valid bids include more than nine unpaired lots.

Bids for the 2010-2025 lot

Regulation 15(4) suggests a bid can include unpaired lots plus the 2010-2025 lot, but Regulation 18(3) suggests that the 2010-2025 lot cannot be included with a basic supplementary bid for the other unpaired lots. This appears to be simply an administrative inconsistency, but an important one to tidy up.

Requirements for determining base prices

The approach to calculating base prices set out in Schedule 8, paragraphs 4 and 5, of the draft Auction Regulations is not clear. Could Ofcom recheck the formulation and algorithm here, and clarify its conclusions for potential bidders?

Appendix – Illustration of the possible inconsistency between IM 4.151 and Schedule 8

Consider 5 bidders.

Alan, Bill and Chas are interested in unpaired spectrum; Kate and Lisa are interested in paired spectrum.

The following bidder behaviour is observed in the primary bid rounds:

Round	Unpaired price	Alan	Bill	Chas	Paired price	Kate	Lisa
1	£50,000	8 lots	8 lots	4 lots	£100,000	8 lots	8 lots
2	£100,000	4 lots	4 lots	-	£200,000	8 lots	8 lots
3					£400,000	7 lots	7 lots

The following (basic) supplementary bids are made in addition to primary round bids:

Alan bids £790,000 for 8 lots of unpaired spectrum

Bill bids £790,000 for 8 lots of unpaired spectrum

The unpaired winners are determined to be Alan and Bill, who both win 4 lots of unpaired spectrum, and the paired winners are Kate and Lisa, who both win 7 lots of paired spectrum.

The bid combinations allow the auction for unpaired to be examined separately from the auction for paired.

The unpaired winners' opportunity costs are calculated as follows:

- Using the rule expressed in Schedule 8 of the Award Regulations, the base prices are calculated to be the same as the bidders' opportunity costs.

Alan: $£400,000 - (£800,000 - £790,000) = £390,000$

Bill: $£400,000 - (£800,000 - £790,000) = £390,000$

This is because if Alan's and Bill's bids are reduced by (slightly less than) £10,000 then the adjusted winning bids just beat the next highest adjusted bid combination ($£390,000 + £390,000 = £780,000$; next highest adjusted combination is $£790,000 - £10,000 = £780,000$).

- However, using the rule expressed in section 4.151 of the Information Memorandum, the base prices should be the minimum to ensure that no *losing* bidder, or combination of bidders, would be prepared to pay more than the calculated base prices.

In particular: Alan must pay **£200,000** and Bill must pay **£200,000**.

This is because if Alan's and Bill's bids are reduced by (slightly less than) £200,000 then the combination of Alan (£200,000) plus Bill (£200,000) just beats any combination of Alan or Bill with a *losing* bidder (for example Alan £200,000 + Chas £200,000).