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CC: Charles Jenne, Selene Rosso, Alan McNaboe, Ofcom

13 November 2014

Dear Geoffrey,

Re: Responses to Ofcom's August 2014 consultation on Annual Licence Fees ("Further Consultation")

In your letter dated October 28 2014, you requested EE Limited ("EE") to provide its views on the suggestions made by other mobile network operators in their responses to the Further Consultation that EE's bids in the UK 4G auction reflected an element of "strategic value", for the purpose of informing Ofcom's approach to estimating the UK market value of 800 MHz and 2.6 GHz spectrum.

Ofcom has not defined what it means by "strategic value", however the relevant suggestions made by the other mobile operators which we are requested to respond to are broadly as follows:

- **Vodafone** – EE's bids for packages of spectrum approaching the spectrum cap were above EE's valuations for the spectrum comprised in those packages (Section 1.3 and Annex 1 of Vodafone's response to the Further Consultation).
- **Telefonica** – because EE did not bid for 2x15 MHz of 800 MHz spectrum this suggests that EE's bids for 2x20 MHz of 800 MHz were driven by strategic factors beyond its perception of what the spectrum was intrinsically worth (paragraphs 50 to 57 of Telefonica's response to the Further Consultation).
- **Three** - EE could anchor its bid around the (2,0,5) package and this permitted it to overstate its true valuation of (4,0,4) without a chance of winning it, in order to attempt to increase its opponents' costs (Page 10 and Annex A (Power Auctions Report), section 4).

We are both surprised and concerned that Ofcom has felt the need to request our views on these submissions. EE's bids were accepted by Ofcom for the purposes of determining prices in the auction, and we



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would expect Ofcom to have sufficient confidence in its auction results to be able to refute these allegations without needing to request highly confidential information from EE regarding our auction valuations and bidding strategy.

In its pre-auction Statement Ofcom clearly expressed a view that its auction design would be sufficient to discourage any strategic bidding. For example, in relation to concerns that bidders may bid with a motivation to increase their competitors' prices, Ofcom stated:

*"In our view a bidding strategy aimed at raising the prices paid by rival bidders, carries significant risks for a bidder pursuing it. Any bid made during the auction can potentially win and the strategy described would involve placing bids that are above the value the bidder places on the package. Unlike in the potential scenarios that led us to remove the Final Price Cap we had proposed in an earlier consultation, the bidder cannot be sure that its inflated bids will not win. Events since the publication of the Auction Statement do not change this fact."*¹

We see no reason for Ofcom to have changed this position on the basis of the submissions made in response to the Further Consultation.

Furthermore, whilst the various interpretations of our auction strategy – produced after months of analysis by auction experts and other operators – certainly make interesting reading, Ofcom must appreciate the reality, which is that EE had only one set of auction experts and a very limited period in which to draw up its list of supplementary bids that is now being dissected in such great detail in an attempt to demonstrate there was an element of strategic value in our bids. In particular, following the conclusion of the primary bid rounds in the auction on 7 February 2013, we had just three working days before the supplementary round to produce our supplementary bids, as well as to complete a formal approval process with our Board of Directors.

Given these factors we do not consider it to be either necessary nor appropriate for Ofcom to rely on information provided by us in relation



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¹ Ofcom, *Statement on the making of regulations in connection with the award of the 800 MHz and 2.6 GHz spectrum bands*, 12 November 2012, paragraph 4.12.

to our bidding strategy in order to respond to the submissions of the other mobile network operators. However, should it now be the case that Ofcom has reason to doubt the reliability of certain bids made in the auction for the purpose of determining UK market values, we note that this would weigh against Ofcom's current proposed approach (i.e. using a "marginal bidder analysis") under which its market value estimates would be based on a small subset of the auction bids. As set out in our response to the Further Consultation, we believe that Ofcom should revert to the linear reference price methodology, with revenue constraint, which takes into account all bids made in the auction in an objective manner, i.e. without requiring any subjective choices as to which are the "most relevant" bids to focus upon.

Nevertheless, for the avoidance of doubt (and as discussed in our meeting on 4 November 2014 as well as previous confidential conversations), we can confirm that all of EE's bids made in the auction were within our valuations for the relevant spectrum, i.e. within what Ofcom refers to as "intrinsic value". Furthermore, our valuations did not incorporate any elements relating to the value of depriving other parties usage of the spectrum concerned (e.g. by weakening a competitor) nor to increasing the costs of our competitors.

None of our bids would therefore, for example, fall within the definition of "Strategic Bid" set out in Vodafone's response:

*"Any bid placed in auction which departs from a bidder's private value in an attempt at reducing the price paid by the bidder or increasing the price paid by other bidders."*²

As we explained in our meeting, our valuations were not the only constraint on our bids – a number of other factors were also taken into account. For example, we explained that we had a budget cap (as we would expect all bidders to have had) and that the application of the reserve price in the auction formed a further constraint on our supplementary bids.



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² Vodafone response to Further Consultation, Annex 1.4.

Finally, we can confirm that, contrary to the suggestion in your letter, the submissions made by other mobile operators regarding the inclusion of strategic value in EE's bids are not related to our arguments regarding the need to account for the "complementarity premiums" inherent in EE's bids for packages of 800 MHz and 2.6 GHz spectrum in the auction (see section 3.2.2 of EE's response to the Further Consultation), and our comments above are without prejudice to those arguments. It is entirely rational to expect that bidders may value complementarities between spectrum bands for technical and commercial reasons. Indeed we understand that the potential existence of such complementarities, as well as substitutability, was one of the main reasons for Ofcom's decision to adopt a combinatorial auction format.

Please do not hesitate to contact me should you have any questions.

Yours sincerely



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