

HUTCHISON TELEPHONE COMPANY LIMITED

**COMMENTS ON
OFTA'S CONSULTATION PAPER
AUCTIONING OF SPECTRUM FOR
THIRD GENERATION MOBILE SERVICES (3G) –
PROPOSED RULES ON "CONNECTED BIDDERS"**

9 APRIL 2001

1. GENERAL

- 1.1 Hutchison Telephone Company Limited (HTCL) welcomes the opportunity to express its views on the consultation paper issued by the Office of Telecommunications Authority (OFTA) on 23 March 2001 on the proposed rules on “Connected Bidders” and the overall licence allocation framework.
- 1.2 3G will be an important milestone for Hong Kong’s future as a leading telecommunication hub in Asia Pacific and around the world. The process by which the licences are to be allocated and the framework under which the 3G businesses and operations are to be regulated thus will have far reaching implications on the viability of future 3G business and standing of Hong Kong in the international telecommunications market.

2. PRINCIPLES OF AUCTION

- 2.1 The stated aim of the Information Technology and Broadcasting Bureau and the Telecommunications Authority (TA) to ensure a speedy auction process to maintain competitiveness of Hong Kong in the new 3G era is noted and generally supported. However, in HTCL’s view, it is paramount to the success of the process that the auction be transparent, fair, objective and economically efficient.
- 2.2 Auction by its nature should be an open and transparent process comprising rounds of interactive bidding whereby the bids made by the bidders would eliminate the bidders in excess of the number of successful bidders intended to be achieved and eventually determine who shall be the successful bidder(s).
- 2.3 Another inherent feature of an auction is the knowledge of the bidders of the bids made by other bidders. A bidder, fully aware of the identity of the other bidders participating at the same auction and fully abreast of the bids made by the other bidders, shall by reference to such information and its commercial circumstances make its own informed decision on the bid to be made in each round of bidding.
- 2.4 The TA has contended that open auctions can be vulnerable to manipulation and the Austrian auction was quoted as an example where the auction ended very early due to the “signalling” by the strong bidders. HTCL however notes that in an investigation conducted after the Austrian auction a firm finding was made that no collusion existed at such auction. In fact independent of the “signalling” the bidding went on for another two days. The same thing happened in the German auction. Again the “signalling” had no effect on the bidding which went on for three weeks.
- 2.5 HTCL also notes that the 3G auction in the United Kingdom is the most open and transparent auction whereat the number and identity of, and the bids made by, the bidders were fully disclosed and known to all bidders and it is the one auction at which no suggestion of collusion was ever made.

- 2.6 Drawing from the experiences from other auctions, HTCL believes that the withholding of information from the bidders, thereby disabling the bidders from making an informed assessment and decision, at an auction would serve little purpose other than to drive up the auction price unnecessarily.
- 2.7 HTCL is also concerned that withholding of information at any auction may subject such auction to possible disputes and contentions.
- 2.8 Based on the above principles, HTCL has the following comments and views on the auction design and process proposed by the TA.

3. HYBRID ALLOCATION METHOD

- 3.1 HTCL welcomes the TA's decision to issue four 3G licences.
- 3.2 The assessment of the pre-qualification criteria has to be based on a set of transparent, objective and quantifiable measures and a set of thresholds and commitments, which should be publicly available prior to submission of applications and applied equally to all licence bidders. HTCL understands that the TA is adopting such approach.

4. LICENCE ALLOCATION FRAMEWORK

4.1 Information

- 4.1.1 On 3G general licensing and regulatory framework, although two rounds of public consultation and an industry workshop have been conducted by the TA, details on a number of important issues, for instance the obligations of MVNO, the rate of return which may be charged to the MVNOs/NSPs in wholesale pricing, the calculation method of open network, the security required and the detailed pre-qualification requirements etc. remain undisclosed. These issues are complicated and unprecedented, and yet are fundamental to the 3G business and success of the auction.
- 4.1.2 HTCL urges that reasonable time should be allowed between the disclosure and publication of the details on these important aspects and the commencement of the auction process to allow the interested parties to fully analyse such details. HTCL suggests that the Information Memorandum mentioned by the TA could be published as soon as it is available even before the Bill and the Subsidiary Legislation are passed.

4.2 Powers of the SITB and the TA

- 4.2.1 HTCL believes that the auction process and indeed the whole telecommunications industry will be most economically efficient if they are left to the market forces moderated with light regulatory framework. The TA's role should therefore be to facilitate the market functioning as opposed

to create rules which would impose limits to the natural process of growth and evolution of this new 3G era.

4.2.2 HTCL also urges that the SITB and the TA in the exercise of their respective powers under the Telecommunications Ordinance should uphold the following principles and policy objectives:

- (a) protection of consumers' interest;
- (b) protection of industry interest; and
- (c) fair and equal treatment of all license bidders.

4.3 **Auction Process and Design**

4.3.1 *Reference*

Reference is made to the explanatory note on auction process and design and rules on connected bidders presented at the Bills Committee meeting held on 26 March 2001 and the further information on the overall licence allocation framework set out in the Consultation Paper.

4.3.2 *Transparent Process*

- (a) The TA suggests that the bidders' identities and numbers be kept confidential to achieve the overall objectives of promoting entry. This certainly contradicts with the principles of an auction and defeats the purpose of an open and transparent auction as discussed in paragraph 2 above. HTCL maintains its strong support for the principles of an open and transparent auction and contention that the auction process should be conducted in a manner which is highly transparent, fair, objective and economically efficient to the development of 3G market.
- (b) It is questionable as to how the above suggestion is justified. For example, land auctions which have been conducted in Hong Kong for many years and other auctions conducted by the Government do not seem to have deterred any players from participating.
- (c) At the 3G auctions in Italy and the United Kingdom, the bidders were fully aware of who the other bidders were, the number of bidders participating and the bids made. In Germany, information on the number of active bidders present at each round of the auction was available.
- (d) HTCL therefore contends that the bidders' identities and the number of active bidders participating at each stage of the auction should be fully disclosed to all bidders.

4.3.3 *Connected Bidders*

- (a) HTCL suggests that the resolution of connected bidders process should be moved forward to the pre-qualification stage to select out of connected bidders those bidders which shall go forward to the main auction stage.

- (b) That was in fact the way connected bidders were resolved at other auctions in Europe. For example, in Switzerland, the connected bidders resolved the connection by merging or withdrawing before they moved into the next stage of the main auction. In the United Kingdom, again the first phase of the auction was to determine who the connected bidders were at which such connected bidders would bid against each other to decide on those bidders who would move on to the main auction.
- (c) If the connected bidders were to be resolved after main auction, it is unclear as to how the provisional winners would be selected and the auction may run the risk of ending with 4 provisional winners, 2 of whom are connected, or comprising 2 sets of connected bidders.

4.3.4 *Bidding Process*

- (a) The SITB has previously stated that treasury benefit is not the priority or emphasis of the Government in the 3G auction. HTCL notes that the underlying principle and purpose of any auction is to eliminate the bidders in excess of the number of successful bidder(s) intended to be achieved and accordingly the process should stop at the point where that principle and purpose is achieved. However the auction as presently proposed is designed to continue beyond that point to where the fourth winner decides to leave, in order to determine the fair market price for 3G licences. In effect the suggested process would create an artificial auction whereat the successful bidders would be bidding against themselves with no purpose other than to drive the auction price up unnecessarily.
- (b) HTCL is of the view that the purpose of determining the fair market price can still be achieved, by using the price offered by the four remaining bidders immediately after the fifth bidder leaves the auction as the fair market price for the 3G licences.

4.3.5 *Tie Bids*

- (a) The TA has suggested the following options for resolution of tie bids:

Selection by drawing lots HTCL strongly objects to drawing lots as the mechanism to determine tie bids on the basis that such method is arbitrary and unfair and with no justification or reference to anything other than luck of the bidders. In the 3G auctions in foreign jurisdictions, drawing lots has never been used to exclude bidders from licence allocation.

Selection by time of withdrawal HTCL is of the view that such mechanism is again unfair as bidders may need time to consult their shareholders (which may well be overseas) and indeed their banks. Such mechanism is also vulnerable to manipulation (for instance bidders may choose to withdraw on the last minute allowed before moving onto the next step up the bidding schedule) and dispute and even litigation on the accuracy of the time recording.

In Italy for instance, the computer time broke down during the auction. It is therefore dangerous to rely on the time to make such a determination.

Tied bidders must bid again It is hereby proposed that the tie bidders would against each other bid again up to a single extra bidding increment however such extra bid would be used to determine the price which all successful licensees would be required to pay. In case of tie again, such tie bids would be determined by drawing lots. HTCL fails to see how and why the tie bidders would continue bidding up a single extra bidding increment when they have by reference to their respective business cases and circumstances decided to withdraw from the auction at that point. This mechanism in HTCL's view simply delays the tie situation but does not resolve it. HTCL reiterates its objection as set out above to using drawing lots at any one point in time in determining the allocation of licence.

All bidders continue to bid This mechanism again simply delays the tie situation which is bound to happen again. HTCL reiterates its objection as set out above to using drawing lots at any one point in time in determining the allocation of licence.

- (b) As the above proposals are not desirable, HTCL requests the TA to re-consider whether it is appropriate to issue the licences to all remaining bidders as and when the ascending auction process has decided on the number to be equal to or less than four. The public has previously been informed of the TA's intention to let the market forces decide on the number of licences to be issued, which may be less than four. In such circumstance, the TA may consider allocating the spare spectrum to the winners to fulfil the needs of the market for network capability and capacity.

4.4 **Network Turnover**

4.4.1 The term "network turnover" is defined in the draft Telecommunications (Method for Determining Spectrum Utilization Fees)(Third Generation) Mobile Services) Regulation to mean "in relation to a licensee, ... the revenue arising from or attributable to the provision of any telecommunications services over any telecommunications network using the frequency bands assigned to the licensee".

4.4.2 As it is proposed for 3G that the spectrum utilization fee be charged based on relevant minimum fee (for the first 5 years) and thereafter on the network turnover, HTCL contends that the following fees and items should not be charged in addition to such spectrum utilization fee, nor, as the case may be, included within the scope of network turnover:

- (a) Fees currently charged and proposed to be charged for the carrier (mobile) licence based on the number of base stations should not be levied in addition to the spectrum utilization fee as that would constitute double counting and penalization of performing mobile operators for maintaining and operating extensive mobile network coverage.

- (b) Fees currently charged and proposed to be charged for the carrier (mobile) licence based on the number of mobile stations should not be levied in addition to the spectrum utilization fee as that would constitute double counting and penalization of performing mobile operators with wide coverage and better service and thereby attracting large customer base.
- (c) Fees currently charged and proposed to be charged for the carrier (mobile licence) based on the frequency spectrum assigned should be excluded as that would certainly constitute a duplication of charges on the same subject.
- (d) At the moment the obligations of MVNOs/NSPs are unclear and undefined. If MVNOs/NSPs are not liable to pay any royalty/fee based on its turnover, network turnover in the case of 3G network operators should then exclude turnover arising from or attributable to content and/or service provisioning, otherwise it would create an unfair disadvantage prejudicing the business case of the 3G network operators as against those of the MVNOs/NSPs.

4.4.3 In the case of open network, the spectrum utilization fee including the royalty based on the network turnover should be included in determining the cost element for the purpose of calculating the wholesale pricing charged to the MVNOs/NSPs.

4.5 **Frequency Bands**

4.5.1 On the frequency bands designated in the Telecommunications (Designation of Frequency Bands Subject To Payment of Spectrum Utilization Fee) Order, HTCL has the following comments and recommendations:

- (a) HTCL recommends that the unpaired TDD band 1914.9 –1919.9 be moved to 2014.7 – 2019.7 due to the expected TDD high interference on the FDD uplink, which the 400KHz guard band may not be sufficient for safeguarding the spectrum purity.
- (b) The 1964.9 – 1979.7 spectrum is adjacent to the frequency allocated for the mobile satellite service. According to HTCL's measurements, there are evidences showing that interference from the mobile satellite service exists in the 1964.9 – 1979.7 frequency band. HTCL would be happy to provide information and data on such measurements. HTCL therefore strongly requests the TA to take actions prior to the commencement of the auction to control and free such frequency band from interference..
- (c) On the basis of the recommendation made in paragraph (a) above, HTCL recommends that the spectrum allocated to each of the four successful bidders should be of the same size of 14.8 MHz paired plus

5 MHz unpaired to ensure fairness and equal treatment to all successful licensees.

- 4.5.2 In the case that cash bids are to be made to determine the frequency band allocation, HTCL would like to clarify and stress the importance of availability of information to all winners for the purposes of making informed decisions therefor, particularly on identities of the final winners.

5. GENERAL

Should any further clarification or information in relation to the above or generally the subject of 3G licensing be required, HTCL would be happy to provide such clarification or information and further discuss with OFTA.