

RESPONSE TO DRAFT GUIDELINES FOR THE ALLOCATION OF 1.7GHZ AND 2.0GHZ SPECTRUM

EUROPEAN BUSINESS COUNCIL TELECOMS CARRIER COMMITTEE

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1. EXECUTIVE SUMMARY

The EBC Telecoms Carrier Committee (the EBC) welcomes the opportunity to comment on the draft guidelines for the allocation of 1.7Ghz and 2.0GHz spectrum (**Draft Guidelines**) released by the Ministry of Internal Affairs and Communications (**Soumusho**) on 3 June 2005.

Spectrum allocation is an extremely important policy issue, given the inevitable impact that allocation policies have on the competitive environment. Japanese consumers currently benefit from innovative services provided at competitive prices. These benefits have resulted from the careful balance between vigorous price competition and sustainable investment. Spectrum allocation proposals must ensure the maintenance of this balance.

The Draft Guidelines outline two objectives: the avoidance of the concentration of spectrum by a specific operator(s), and encouraging the efficient use of spectrum. These guideline objectives are said to be achieved by prioritising the entry of up to 3 new entrants and allocating growth spectrum based on the achievement of specified subscriber thresholds.

The EBC has serious concerns that, in their current form, the Draft Guidelines not only fail to achieve the intended objectives, but are likely to cause significant damage to the competitive environment. Specifically, the Draft Guidelines:

- Fail to distinguish between dominant and non-dominant operators thereby creating the likelihood that the dominant operator is likely to obtain all the available ToMeiHan 1.7GHz spectrum;
- Fail to establish robust and objective selection criteria for new entrants which would maximise the likelihood of spectrum being allocated efficiently and reduce risk of new operator failure;
- Fail to take into account existing allocations of spectrum that the dominant operator could use for 3G services;

- Fail to provide for the necessary network preparation period required prior to spectrum usage.

EBC's detailed comments on the Draft Guidelines are set out below.

2. SOUMUSHO'S OBJECTIVES

The EBC notes that the purpose of the TBL is to “secure the consistent provision of telecommunications service, to protect the users’ benefit, and thereby to ensure both the sound development of telecommunications and the convenience of people, and to promote the public welfare”.

In designing spectrum allocation guidelines, therefore, Soumusho should have regard to the extent to which its proposals will benefit users over the long term and ensure a healthy process of competition in accordance with legislative requirements.

The purpose of the TBL is unlikely to be met if Soumusho’s proposals pursue the objectives of preventing concentration and efficient use of spectrum without regard to the overall long term interest of end users.

3. PRIORITISATION OF NEW ENTRY

The Draft Guidelines make the following provisions for new entry:

- 15MHz x 2 of 1.7GHz Nationwide Spectrum to be allocated in blocks of 5MHz x 2 to up to 2 new entrants. Any remaining spectrum is to be reserved for new entrant’s growth needs once the utilisation criteria set out in the Draft Guidelines is met;
- 15MHz x 1 of 2.0GHz spectrum to be allocated in a single block to one new entrant; and
- Entry criteria based on the appropriateness of the deployment plan, certainty of implementation, interference prevention, contribution to the healthy development and facilitated operations of telecoms business.

The EBC notes that, contrary to experiences from other markets, in Japan, there has been little or no public discussion about the costs and benefits of new entry. The focus on new entrants on the part of the government appears also to be at odds with the experience of other mobile markets which are generally consolidating.

Whilst the intention behind the introduction of new entrants may be to prevent concentration of spectrum, the proposal actually produces the opposite effect, by ensuring that there is less spectrum available to each non-dominant operator. In order to sustain healthy competition, all operators including existing operators, must have the potential to access additional spectrum resources. Without access to sufficient spectrum resources, existing operators will have their business choices constrained, with flow through effects on both innovation and pricing.

The long term interests of end users will therefore be adversely affected if allocation proposals focus merely on increasing competitor numbers, without regard to the need to promote robust and sustainable competition.

Additionally, the new entrant selection process outlined in the Draft Guidelines lacks robustness and transparency. This is essential when dealing with a valuable resource such as spectrum. A public debate about the relevant criteria and applicable weightings to be applied in the selection process should be standard regulatory practice. This would enable all stakeholders to understand the objectives that new entry is designed to achieve and allow for greater transparency in terms of weighing the merits of comparative applications.

The EBC believes that current selection criteria are fundamentally inadequate. They fail to require applicants to provide details about such essential matters as:

- Proven technical and managerial experience and expertise;
- The technical standard to be adopted by the applicant in rolling out services;
- Evidence of a viable business plan;
- Evidence of access to sufficient capital; and
- Proposals for ensuring reliability, access, and quality of service.

Given the valuable nature of spectrum and the high costs of rolling out a network, it is vital that applicants are properly scrutinised. Without robust scrutiny, the likelihood of the spectrum being allocated in the most efficient way is minimised, and Japanese consumers are exposed to the risk of market failure of a new entrant.

4. METHODOLOGY FOR ALLOCATION OF SPECTRUM

The Draft Guidelines provide that applications for allocations of spectrum can be made when the number of subscribers per megahertz exceeds defined thresholds. These thresholds increase in

line with the volume of allocated 3G spectrum. Where applications compete, the applicant who has the highest number of subscribers per MHz will be preferred.

The EBC notes that, while the proposed criteria appear to apply equally to all operators, by merely focussing on raw subscriber numbers without making any distinction between dominant and non-dominant operators, the criteria ignore the unmatched advantages of revenues, volumes, and scale and scope enjoyed by the dominant operator. Providing that the operator with the highest number of users per megahertz will be prioritised in the spectrum allocation serves to further entrench these advantages. The almost inevitable outcome, therefore, is a concentration of spectrum in the hands of the dominant operator.

The EBC believes that likelihood of the dominant operator monopolising these spectrum allocations is also dramatically increased by the failure to require DoCoMo to take into account its 800MHz spectrum as 3G spectrum. This spectrum is currently allocated as 3G spectrum and some initial usage of it for 3G purposes has begun. Failing to require this spectrum to be factored into the relevant calculations means that there is no incentive for efficient use of this spectrum for 3G services. Instead, it creates the potential for this spectrum to be “mothballed” while applications for 1.7GHz spectrum are made. The design of the allocation process, therefore, rather than preventing concentration and encouraging efficient use, creates an environment where concentration of spectrum based on inefficient use is the likely outcome.

In addition the EBC notes the cost efficiencies that accrue to operators utilising lower bandwidths because of the extended propagation benefits. These cost efficiencies mean that operators are able to reach the threshold subscriber numbers at a lower cost than competitors who are utilising higher frequencies. Some recognition of the importance of these cost efficiencies should therefore be factored into the threshold criteria.

Finally, the EBC notes that applications for spectrum can only be made once the actual subscriber threshold has been met. In doing so, the Draft Guidelines create a delay which is both inefficient and damaging to the long term interests of consumers, given the lead in time required for efficient network and service planning by mobile operators. By failing to allow operators to apply for spectrum based on projections, the Draft Guidelines require them to make one of two choices: they can choose to formulate business plans, develop technology and networks, on the assumption that they will be successful in the application process; or, they can delay these decisions until such time as they are certain that they have been successful in their application. The first choice runs the risk of wasted resources while the second choice means that the benefits of developments and the efficient usage of spectrum will be delayed. The EBC firmly believes that neither of these outcomes is in the long term interests of end users.

The EBC has previously commented on its concerns about the impact of spectrum imbalances.¹ The Draft Guidelines not only fail to recognise our concern regarding the existing imbalance, but actually increase the distortionary effect on competing foreign operators who require growth spectrum. We are deeply concerned by the creation of an allocation mechanism that unduly prefers the dominant operator. Such action is likely to significantly erode the confidence of international investors and undermine the Government's ambitions to increase direct foreign investment in Japan. Investors require confidence that they can enter and compete on a level playing field.

Simple solutions which would redress the balance between efficient use and the long term interests of end users, by distinguishing between dominant and non-dominant operators, would be to reserve a specific amount of growth spectrum specifically for non-dominant operators or to place a cap of 10MHz on the total amount of spectrum that the dominant operator is able to obtain through the allocation process. Spectrum caps have previously been used in the United States to deal with concerns about the aggregation of spectrum in a way which might exclude efficient competitors or allow anticompetitive behaviour.

5. CONCLUSION

Under the Draft Guidelines, a focus on new entry and subscriber numbers as a proxy for spectrum efficiency means that existing non-dominant operators find themselves squeezed between the new entrants on the one hand and the dominant operator on the other. The failure to strike a balance between the objectives of efficiency and the long term interests of end users means that non-dominant operators are unlikely to obtain the growth spectrum that they need. This will inevitably lead to weaker competition and harm the long term interests of users.

It is therefore essential that the final guidelines for the allocation of spectrum are revised to take into account the points set out above. In particular, proposals for the allocation of spectrum must not entrench the position of the dominant operator. A balanced outcome between new entrants, existing non-dominant operators, and the dominant operator is essential if investment, innovation, and competition in the Japanese mobile industry are to be maintained.

To this end, the Committee encourages Soumusho to amend the draft guidelines in line with international best practice to:

- Establish robust and objective selection criteria for new entrants;

¹ European Business Council Business Dialogue Round Table Recommendations, June 2005

- Distinguish between dominant and non-dominant operators and prevent concentration of spectrum in the dominant operator either by imposing a cap of 10Mhz on the amount of spectrum that the dominant operator can obtain under the allocation process or by specifically reserving a similar amount of spectrum for non-dominant operators;
- Clarify that existing 800MHz spectrum is to be attributed to the dominant operator in calculating required subscriber numbers;
- Consider adjusting the subscriber criteria to take into account the cost efficiencies that accrue to operators utilising lower frequencies;
- Provide for the necessary network preparation period by allowing applications based on demand projections rather than actual subscriber numbers.