

**Statement of Preliminary Issues
700 MHz Spectrum Applications**

22 October 2013

Introduction

1. The Commerce Commission has received applications from Telecom New Zealand Limited (Telecom) and Vodafone New Zealand Limited (Vodafone) seeking clearance to acquire the management rights to 700 MHz radio spectrum. Telecom's application was received on 4 October 2013. Vodafone's application was received on 9 October 2013. Public versions of the applications can be access on our website at: <http://www.comcom.govt.nz/business-competition/mergers-and-acquisitions/clearances/clearances-register/>
2. This Statement of Preliminary Issues outlines the key competition issues we currently consider will be important in deciding whether or not to grant clearance. The issues highlighted in this statement are based on the information available at the time of publication, and may change as our assessment of the applications for clearance progresses.
3. We invite interested parties to make comment on the likely competitive effects of the proposed acquisitions and request that parties who wish to make a submission do so by 5 November 2013.

The auction and acquisitions

4. The applications from Telecom and Vodafone relate to an upcoming auction being conducted by the Ministry of Business, Innovation and Employment (MBIE) of radio spectrum in the 700 Mhz band.¹ The Crown is auctioning the management rights to radio spectrum freed up by the switchover to digital television. Spectrum in the 700 MHz band is expected to assist with the development of fourth generation (4G) mobile services. The auction comprises nine lots of 5 MHz paired spectrum in the 700 MHz band.
5. The parties that have been confirmed as registered bidders for the auction are Telecom, Vodafone and Two Degrees Mobile Limited (2degrees).
6. As part of the auction rules, there are limits on the amount of spectrum each bidder can acquire. In the first phase of the auction (the clock allocation phase), each bidder will be limited to acquiring up to 2 x 15 MHz (or three lots) of spectrum. If one or more lots remain unsold at the end of this phase of the auction, then the auction may proceed to a supplementary allocation phase. In any supplementary allocation phase, the acquisition limits will be increased to 2 x 20 MHz (or four lots) in an attempt to sell any unsold lot(s) of spectrum in the 700 MHz band.

¹ Further information on the upcoming auction is available at <http://www.rsm.govt.nz/cms/policy-and-planning/consultation/digital-dividend-auction>.

7. Whilst the wording of their applications differs, in essence, both Telecom and Vodafone seek clearance to acquire the management rights to 2 x 20 MHz (or four of the total nine lots) of spectrum in the 700 Mhz band, should the auction proceed to a supplementary allocation phase.
8. This Statement of Preliminary Issues has been prepared on the basis that there is a supplementary allocation phase. Whether or not a supplementary allocation phase is likely to occur should be more apparent once the clock allocation phase of the auction has concluded on 29 October 2013 and it is known whether there are unsold lots. Practically speaking, the Commission only needs to make decisions on Telecom and Vodafone's applications if the auction is to proceed to a supplementary allocation phase.² This would be likely only if 2degrees does not bid for three lots.

Our framework

9. Our approach to analysing the competition effects of the proposed acquisitions is based on the principles set out in our Mergers and Acquisitions Guidelines.³ As required by the Commerce Act 1986, we assess mergers using the substantial lessening of competition test.
10. This test asks whether an acquisition is likely to substantially lessen competition in a market by comparing the likely state of competition if the acquisition proceeds (the scenario with the acquisition, often referred to as the factual), with the likely state of competition if the acquisition does not proceed (the scenario without the acquisition, often referred to as the counterfactual).⁴
11. Determining the scope of the relevant market or markets can be an important tool in determining whether a substantial lessening of competition is likely. This is because the more closely substitutable two products are, the likely greater the competitive constraint between those products.
12. We define markets in the way that we consider best isolates the key competition issues that arise from the acquisition. In many cases this may not require us to precisely define the boundaries of a market. A relevant market is ultimately determined, in the words of the Act, as a matter of fact and commercial common sense.⁵
13. We analyse the extent of competition in each relevant market both with and without the acquisition in terms of the following.
 - 13.1 Existing competition – the degree to which existing competitors compete and their ability to expand in the event that the purchaser raises prices.

² If there are no unsold lots at the end of the clock allocation phase, then there will be no supplementary allocation phase and the proposed acquisitions cannot proceed. Pursuant to section 68(2), where the Commission is of the opinion that a proposed acquisition is unlikely to proceed, then it can decline to give clearance.

³ Commerce Commission, *Mergers and Acquisitions Guidelines*, July 2013.

⁴ *Commerce Commission v Woolworths Limited* (2008) 12 TCLR 194 (CA) at [63].

⁵ Section 3(1A). See also *Brambles v Commerce Commission* (2003) 10 TCLR 868 at [81].

- 13.2 Potential competition – the ability of businesses to readily enter the market on sufficient scale in order to provide competitive constraint.
 - 13.3 The countervailing market power of buyers – the potential for a business to be sufficiently constrained by purchaser’s ability to exert an influence on price, quality and/or terms of supply.
 - 13.4 Coordinated behaviour – conditions that make market participants likely to collude either tacitly or explicitly.
14. A comparison of the extent of competition both with and without the acquisition enables us to assess the degree by which the proposed acquisition might lessen competition. If the lessening is likely to be substantial, we may not give clearance to the proposed acquisition.

Preliminary issues

15. We are currently focusing our investigation on the following areas.

Market definition

16. We define markets in the way that we consider best isolates the key competition issues that arise from the acquisition.
17. In previous decisions, the Commission has considered the impact of spectrum acquisitions in the national markets for:
- 17.1 retail mobile services (for residential and business customers); and
 - 17.2 wireless spectrum management rights suitable for mobile services.
18. The applications presently before the Commission relate to the acquisition of the management rights to 700 MHz radio spectrum to be used in the development of 4G mobile services. We will consider, and are interested in parties’ views on, whether 4G mobile services are sufficiently distinctive to place them in a discrete market from second generation (2G) and/or third generation (3G) services.
19. Currently limited 4G mobile services are being provided and developed using spectrum in the 1.8 GHz and higher bands. However, spectrum in the 700 MHz band is expected to be a more efficient means of delivering 4G mobile services to rural areas as well as improving indoor coverage in metropolitan areas. We will consider, and are interested in parties’ views on, whether particular spectrum frequencies constitute individual product markets or form part of a broader differentiated market for wireless spectrum management rights.

Factual and counterfactual

20. Previously, the Commission has considered only applications relating to the acquisition of the management rights to radio spectrum after an auction has concluded (and the results of the auction were known). The current applications

from Telecom and Vodafone have been registered before the auction of radio spectrum in the 700 Mhz band has commenced.

21. Until the clock allocation phase has concluded, we are unlikely to know whether there might be a supplementary allocation phase and how many lots might be offered for sale in any such phase. This uncertainty means that, at this time, there are multiple possible factual and counterfactual scenarios.
22. In their applications for clearance, Telecom and Vodafone have both made submissions on what they consider to be the likely factual and counterfactual scenarios.
23. The Commission will assess the likely factual and counterfactual scenarios at the end of the clock allocation phase.
24. We invite the views of interested parties on the likely factual and counterfactual scenarios. We also invite interested parties' views on which likely counterfactual scenario is the most competitive and, therefore, should be used as the comparator in the Commission's competition analysis.

Competition analysis

25. Both Telecom and Vodafone have submitted that their acquisition of 2 x 20 MHz of spectrum in the 700 MHz band would not give rise to a substantial lessening of competition in any market. They have further submitted that significant efficiencies would arise from their acquisition of 2 x 20 MHz of spectrum, including higher quality 4G services in rural areas.
26. The submissions from Telecom and Vodafone as to why their acquisitions would not lessen competition include arguments that:
 - 26.1 retail mobile services market(s) are currently highly competitive;
 - 26.2 the acquisitions would not alter existing operators' abilities to compete, or the dynamics or intensity of competition in those markets;
 - 26.3 existing competitors would continue to provide constraint; and
 - 26.4 2degrees, in particular, is likely to have sufficient spectrum holdings to enable it to compete in the provision of 4G mobile services.
27. We will examine the extent to which Telecom and/or Vodafone's acquisition of 2 x 20 MHz of spectrum in the 700 MHz band might inhibit the ability of competitors to compete in providing retail mobile services, in particular, prevent or inhibit them from competing in the provision of 4G mobile services. We invite interested parties views on these points and on the degree by which the proposed acquisitions might lessen competition generally.

Next steps

28. In line with our Merger and Acquisitions Guidelines (available on our website at www.comcom.govt.nz), we have established a draft timeframe for consideration of the issues and the two applications for clearance. An extension of time was agreed to by both Telecom and Vodafone such that we should make our final decisions by 6 December 2013.
29. To keep up to date with changes in relation to timing and to find relevant documents, visit the Clearance Public Register on our website at:

<http://www.comcom.govt.nz/clearances-register/>
30. As part of our investigation, we will identify the parties we believe will provide the best information to help us assess the preliminary issues identified above. We will be contacting those parties over the next few weeks.
31. We also invite submissions from any other parties who consider they have information relevant to our consideration of this matter. If you wish to make a submission, please send it to the Registrar, at registrar@comcom.govt.nz with the reference 700 Mhz spectrum in the subject line of your email, or The Registrar, PO Box 2351, Wellington 6140 by close of business **5 November 2013**. Please clearly identify any confidential information contained in the submission and provide contact details.
32. Parties making submissions should note that, given the potential interest in the Commission's consideration of these applications, we intend to publish public versions of all submissions on our website. If we do not receive separate confidential and public versions of a submission, we will assume that nothing is confidential in that submission and place it on our website.