IN THE MATTER OF

THE WIRELESS TELEGRAPHY ACT 2006
(DIRECTIONS TO OFCOM) ORDER 2010

OPINION

Introduction

1. We have been asked by Vodafone Limited to provide a legal opinion addressing the question of the proper approach to be taken by Ofcom when performing its obligations under Article 6 of the Wireless Telegraphy Act 2006 (Directions to Ofcom) Order 2010 ("the Direction").

2. Article 9 of the Direction required Ofcom to organise an auction of licences for the use of frequencies in the 800MHz and 2600MHz bands. This auction took place in early 2013, and the licences were issued on 1 March 2013.

3. By Article 6(1) of the Direction, Ofcom is now required to revise the fees payable by operators for spectrum in the 900MHz and 1800MHz bands "so that they reflect the full market value of the frequencies in those bands". Article 6(2) then provides that, in revising the fees, Ofcom "must have particular regard to the sums bid for licences in the Auction". Ofcom is currently undertaking a consultation before deciding on a methodology for determining the revised fees. It is in this context that Vodafone has

sought our opinion as to the correct approach to Ofcom's obligations under the Direction as a matter of UK and (so far as relevant) EU law.

4. We have structured our analysis by reference to two questions. First, what is the relationship between the Direction and the various other legal instruments governing Ofcom's responsibilities in relation to radio spectrum? Secondly, how can Ofcom comply with the Direction while at the same time discharging those other responsibilities?

Summary of conclusions

5. We can summarise our conclusions in relation to these two questions as follows:

(1) The Direction is a piece of delegated legislation and, as such, is only valid and binding on Ofcom to the extent that it is consistent with Ofcom's duties under the applicable primary legislation. That legislation must be interpreted and applied in such a way as to give full effect to the provisions of the EU directives from which it derives.

(2) It is possible for Ofcom to interpret and implement the Direction consistently with its overriding statutory duties, but only if two points in particular are observed.

(3) First, the requirement to "have particular regard" to the amounts bid in the 800MHz and 2600MHz auctions does not mean that Ofcom has necessarily to make any – let alone any significant – use of these amounts in practice when it comes to assess the market value of the 900MHz and 1800MHz spectrum. Thus, if Ofcom considers the auction bids to be of little or no relevance for this purpose, it should give them a correspondingly small degree of weight, or no weight at all, in its eventual methodology.

(4) Secondly, it is essential from the point of view of Ofcom's overarching statutory and EU obligations that any fees which it imposes do not exceed the market value of the spectrum. (By contrast, Ofcom would not be in breach of those obligations if it set the fees below the market value.) Ofcom should therefore adopt a

conservative approach to the assessment of the market value. Such an approach is in no way precluded by the terms of the Direction.

The status of the Direction

6. Before considering the validity and effect of the Direction, it is first necessary to set it in context by outlining Ofcom's statutory powers and duties in relation to spectrum usage fees generally, and establishing the place of the Direction within that scheme.

7. Ofcom's power to impose usage fees derives from the Wireless Telegraphy Act 2006 ("the 2006 Act") which, together with the Communications Act 2003 ("the 2003 Act") gives effect in the UK to the EU's Common Regulatory Framework for electronic communications networks and services ("CRF"). The CRF consists of a series of five directives, originally adopted in 2002 and subsequently amended.[1]

8. The key provisions of the CRF in relation to usage fees are as follows:

   (1) Article 8 of the Framework Directive sets out a number of general objectives which National Regulatory Authorities ("NRAs") are required to take all reasonable measures to achieve. These include the promotion of competition (Article 8(2)). This is to be achieved, in particular, by ensuring that users derive maximum benefit; ensuring that there is no distortion or restriction of competition; and encouraging efficient use and ensuring the effective management of spectrum. As spectrum is a scarce resource and a critical input to the operation of mobile networks, it is unsurprising that the CRF should treat its efficient use and effective management as being central to the development of competition in this sector.

   (2) Specific rules in relation to spectrum usage fees are then laid down in the Authorisation Directive. The purpose for which these fees may be imposed is stated in Recital 32:

[1] Directives 2002/21/EC, 2002/20/EC, 2002/19/EC, 2002/22/EC and 2002/58/EC. These Directives, which have since been amended, are respectively known as the Framework, Authorisation, Access, Universal Service, and Privacy and Electronic Communications Directives.

> *"In addition to administrative charges, usage fees may be levied for the use of radio frequencies and numbers as an instrument to ensure the optimal use of such resources. Such fees should not hinder the development of innovative services and competition in the market."* (Emphasis added.)

(3) The actual power to levy usage fees is created by Article 13, which imposes additional constraints on the level of any fees:

> *"Member States may allow the relevant authority to impose fees for the rights of use for radio frequencies or numbers…which reflect the need to ensure the optimal use of these resources. Member States shall ensure that such fees shall be objectively justified, transparent, non-discriminatory and proportionate in relation to their intended purpose and shall take into account the objectives in Article 8 of Directive 2002/21/EC (Framework Directive)."*

9. These provisions have been given effect in the UK primarily in sections 3 and 4 of the 2003 Act and sections 3, 12 and 13 of the 2006 Act:

(1) Sections 12 and 13(2) of the 2006 Act enable Ofcom to impose licence fees which exceed the level required to cover its administrative costs.[2] However, the latter section makes clear that such fees are only permissible to the extent that Ofcom considers them appropriate in the light of the matters to which it must have regard under section 3 of the 2006 Act.

(2) There are seven relevant matters which Ofcom must take into account under section 3 of the 2006 Act. These include the extent to which spectrum is available for use; current and future demand for spectrum; the efficient management and use of spectrum; the economic and other benefits that arise from its use; the development of innovation; and competition in the provision of electronic communications services.

[2] In addition to licence fees payable under sections 12-13, Ofcom is also empowered to impose fees for access to recognised spectrum under section 21 of the 2006 Act. This Opinion is confined to the licence fees imposed under section 12 which are the only fees affected by the Direction. We refer to such fees as "usage fees", which (as set out in paragraph 9 above) is the terminology used in the Authorisation Directive.

(3) In addition, Ofcom is subject to an overarching "principal duty" under section 3(1)(b) of the 2003 Act to further the interests of consumers, where appropriate by promoting competition. Guidance in relation to the achievement of these objectives is contained in sections 3(2)-(5):

(a) Section 3(2) specifies that the principal duty requires Ofcom to "ensure" (among other objectives) the "optimal use" of spectrum.

(b) Section 3(3) requires Ofcom to have regard to the principles of transparency, accountability, proportionality, consistency and targeting its activities only at cases in which action is needed.

(c) Section 3(4) requires Ofcom additionally to have regard to other factors, insofar as it considers them to be relevant, including the promotion of competition, and the encouragement of investment and innovation.

(d) Section 3(5) stipulates that, in performing its duty under section 3(1)(b) to further the interests of consumers, Ofcom must have regard to consumers' interests in respect of choice, price, quality of service and value for money.

(4) Section 4(2) of the 2003 Act imposes a duty on Ofcom, in carrying out its radio spectrum functions (among others), to act in accordance with the six so-called "Community requirements" which are expressly intended to correspond to the requirements of Article 8 of the Framework Directive.

10. To the extent that these provisions of the 2003 and 2006 Acts give rise to any difficulties of interpretation, it is axiomatic that provisions of national law which implement an EU directive must be interpreted in the light of the wording and purpose of the directive, in order to ensure that the purpose of the directive is achieved.[3] In the context of telecommunications, with their obvious importance in terms of trade between Member States, the need to ensure a consistent approach throughout the EU provides a good reason for national regulatory authorities ("NRAs") to pay

[3] Case 14/83 *Von Colson* [1984] ECR 1891, paragraph 26.

particularly close attention to the terms of the CRF. Thus, the English courts have specifically held that the 2003 and 2006 Acts must be interpreted consistently with the CRF.[4]

11. Having said this, we can detect no significant differences between the above provisions of the 2003 and 2006 Acts and the corresponding provisions of the Framework and Authorisation Directives.[5] In particular, it is abundantly clear from both sets of provisions that usage fees may only be imposed by Ofcom if and to the extent that Ofcom considers this necessary to ensure the "optimal use" of spectrum. As Article 8 of the Framework Directive and sections 3(1) and 3(2) of the 2003 Act make clear, ensuring the optimal use of spectrum is itself an important means of achieving one of the ultimate aims of telecommunications regulation, namely to promote competition and benefit consumers. To impose (or increase) usage fees purely, or even substantially,[6] for a purpose unrelated to these goals – such as raising revenue for Ofcom or for the state – is not permitted by the legislation and would be unlawful.

12. Against that background, we turn to consider the scope of the powers conferred on the Secretary of State under section 5 of the 2006 Act. At first sight, the section is drafted in very broad terms, in that it purports to authorise the Secretary of State to require Ofcom to exercise its powers in any manner whatsoever, without restricting the purposes to be achieved. However, this apparently unlimited discretion is in fact substantially qualified by two principles of UK constitutional law.

13. The first is that delegated legislation may not contradict primary legislation. As Lord Goddard CJ said in *Powell v. May* [1946] KB 330, 335, *"Obviously [a statutory instrument] cannot permit that which a statute expressly forbids nor forbid that which a statute expressly permits..."* So, in the event of a direct conflict between the

[4] See e.g. *Arqiva Ltd v. Everything Everywhere* [2012] 1 All ER 607, paragraphs 32-36.

[5] In the event that there was such an inconsistency, the terms of the CRF would prevail and would be capable of being relied on directly as against Ofcom: cf Case 41/74 *Van Duyn v. Home Office* [1974] ECR 1337.

[6] In *R v. Inner London Education Authority ex p. Westminster City Council* [1986] 1 All ER 19 the Court of Appeal held that it was unlawful for a public authority to act for a combination of authorised and unauthorised reasons, if the unauthorised reason was a substantial factor in its decision.

Direction and the 2003 Act or the 2006 Act, Ofcom would be bound to perform its duties under the Acts and disregard the offending parts of the Direction. Similarly, the Secretary of State could not, by issuing a Direction, validly require Ofcom to act in a way which was plainly contrary to the terms of the CRF.

14. The second principle, which is related to the first, is that delegated legislation can only be made in order to further the policy of the enabling Act itself, and not for other purposes.[7] A direction which required Ofcom to act in a way which was inconsistent with the general objects of the 2006 Act would thus similarly be *ultra vires* and of no effect, and could not provide a valid basis for any decision taken by Ofcom.

15. For these reasons, notwithstanding the wording of section 5 of the 2006 Act or of the Direction itself, it is clear that the Direction is invalid and incapable of being followed by Ofcom if and to the extent that it requires Ofcom to act inconsistently with its statutory duties to ensure the optimal use of spectrum and promote competition. Whether or not it does run counter to these objectives is a question that we consider below.

The interpretation and application of the Direction

16. In construing the Direction it is important to have regard to a further relevant principle of public law, whereby ministers are presumed to act lawfully when making delegated legislation. The Direction must therefore be interpreted and applied, so far as possible, in a way which is consistent with the requirements of the 2003 and 2006 Acts and the CRF.[8] Only if this is impossible must the offending provisions of the Direction be disregarded altogether as *ultra vires*.

17. In principle, there is in our view nothing objectionable about the Direction inasmuch as its fundamental purpose is to ensure that the fees for spectrum in the 900MHz and

[7] See *Padfield v. Minister of Agriculture* [1968] AC 997, 1030.

[8] cf *DPP v. Hutchinson* [1990] 2 AC 783, 818 per Lord Lowry: "[W]hen construing legislation the validity of which is under challenge, the first duty of the court, in obedience to the principle that a law should, whenever possible, be interpreted *ut res magis valeat quam pereat*, is to see whether the impugned provision can reasonably bear a construction which renders it valid."

1800MHz bands correspond to the "market value" of the spectrum. Although the assessment of the market value of the spectrum is likely to be a complex and uncertain exercise, there is nevertheless no inherent tension in principle between charging a market price for a resource and ensuring its optimal use. On the contrary, provided the market value can be calculated accurately, a system in which operators pay that value should be the most efficient system possible.

18. There are however two respects in which the Direction needs to be interpreted and applied with particular care, in our view, in order to ensure that it does not cut across Ofcom's primary duty, as an independent NRA, to ensure the optimal use of the spectrum in the interests of promoting competition and benefiting consumers.

19. The first point concerns the requirement that Ofcom "have particular regard" to the sums bid in the auction when assessing the market value of the 900MHz and 1800MHz spectrum. While the Direction assumes a potential connection between the market value of the 900MHz and 1800MHz spectrum and the sums bid in the 800MHz and 2600MHz auction, it says nothing about the nature of that connection; nor does it dictate any particular approach to the auction bids which Ofcom must follow. How then should Ofcom observe this requirement?

20. It is well established in English law that the only effect of a provision requiring a decision-maker to "have regard" to particular matters is to establish that the criteria in question are relevant factors that must be taken into account by the decision maker. Thus, if the evidence shows that the decision maker has not considered them at all, its decision will be unlawful. However, the relative weight to be attached to the various relevant factors is a matter for the decision-maker itself. So, if the decision-maker does have proper regard for the prescribed matters, it is entitled ultimately to give them little or no weight in coming to its decision, provided only that it does not act irrationally.[9]

21. This position is not significantly altered by the fact that the Direction requires Ofcom to have "particular" regard to the sums bid in the auction. The inclusion of the word

[9] *Tesco Stores v. Secretary of State for the Environment* [1995] 1 WLR 759, [56].

"particular" indicates that Ofcom should give a heightened degree of weight to the amounts bid. But ultimately it cannot be criticised if it rationally concludes that the mandatory consideration is outweighed by other relevant considerations, such that it plays little or no part in its eventual assessment of the market value of the 900MHz and 1800MHz spectrum.[10] That argument would be even stronger if Ofcom reasonably formed the view that basing the charges on the amounts bid in the auction would actually reduce the accuracy of its calculations of market value, or conflict with its primary duty of ensuring the optimal use of the spectrum.

22. Indeed, in our opinion Ofcom would be obliged in those circumstances not to make any use of the amounts bid in calculating the market value or the resulting charges for the non-auctioned spectrum. This is because Ofcom does not have a general discretion in the setting of charges, but has a positive duty to achieve particular results, namely to secure the optimal use of the spectrum and thereby promote competition, and may therefore only impose charges insofar as they are consistent with, and proportionate to, those aims.[11] Consequently, if the sums bid in the auction are an unreliable or unhelpful guide to the market value of the non-auctioned spectrum, such that they would lead to the imposition of inaccurate or discriminatory charges, they must be disregarded altogether. Otherwise Ofcom would be in breach of its cardinal duties under sections 3(1)(b) and 3(2)(a) of the 2003 Act.[12]

23. The second important point of interpretation relates to the requirement that the spectrum charges reflect the "full" market value. The concept of the "full market

[10] See e.g. *R v. Housing Benefit Review Board ex p. Mehanne* [2001] 1 WLR 539 at [13]. The provision at issue in that case used the phrase "special regard", but in our view there is no distinction between the adjectives "special" and "particular" in this context.

[11] cf *R (Baker) v. Secretary of State for Communities and Local Government* [2008] EWCA Civ 141 at [31], where Dyson LJ described the distinction between a duty to take certain factors into account and a duty to achieve a positive result as a "vital" one.

[12] We are not in a position to express a view as to whether the sums bid in the auction are in fact a useful guide to the market value of the 900MHz and 1800MHz spectrum. However, it seems to us that the relationship between the two sets of values cannot be a straightforward one, in view of the differing physical characteristics of the different types of spectrum and the technologies for which they are capable of being used both in the short term and the longer term. It will also be necessary to take into account the effect of existing spectrum holdings of the size of the bids, as well as the possibility that some undertakings may have made tactical bids with a view to influencing the price of the 900MHz and 1800MHz spectrum. Considerations such as these may have the effect of reducing the weight that Ofcom can properly give to the amounts bid in the auction by comparison with other relevant criteria.

value" of spectrum is not used in the CRF or in the 2003 and 2006 Acts. However, in its consultation document dated 22 March 2011, Ofcom states that:

> "We interpret the term 'full market value' to mean that we do not discount our estimate of the price that would occur in a well functioning market, nor do we set it conservatively compared with the available market information."[13]

24. In our view, this interpretation is not quite correct. In particular, whilst we agree that the Direction does not permit Ofcom to discount its best estimate of the market value to such an extent that the resulting price can no longer actually be said to reflect the market value, we do not consider that the Direction prevents Ofcom from adopting a conservative approach to the valuation process. Indeed, in our view, for the reasons explained below, Ofcom's statutory duties under UK and EU law positively require it to adopt a conservative approach to the imposition of usage fees.

25. In the first instance, it seems to us that in construing Article 6(1) in such a way as would rule out a conservative approach, Ofcom places too much emphasis on the word "full". We do not consider that, in referring to the "full" market value, the Secretary of State should be taken to have intended to lay down any particular approach to the setting of charges, let alone an approach which fixes the "market value" at or towards the upper boundary of the range of possible values. It seems more probable that the word "full" serves no particular purpose other than simply indicating that the process of bringing the usage fees into line with the market value is likely (at least in the view of the Secretary of State) to lead to the fees being increased, as opposed to maintained or reduced.

26. Even if a conservative approach is not the most natural construction of Article 6(1), however, we consider that it is a construction which must be adopted if the Direction is to be interpreted and applied in a manner consistent with the 2003 and 2006 Acts and the CRF (as of course it has to be).[14] This is for three principal reasons.

[13] Paragraph 10.4.

[14] cf *Litster v. Forth Dry Dock & Engineering Co Ltd* [1990] 1 AC 546, where the House of Lords held that it was necessary to read words into a statutory instrument, as part of a "purposive" approach to its interpretation, in order to bring it into line with an EU directive.

27. First, lower charges can be assumed to translate into clear benefits to consumers, through lower prices and/or increased investment and innovation. Conversely, higher charges may well result in higher prices and/or may deter operators from investing in network improvements or expansion. As noted above, the interest of consumers in lower prices and the desirability of encouraging investment and innovation are both matters that Ofcom is specifically directed to take into account when performing its principal duties under section 3 of the 2003 Act. Recital 32 to the Authorisation Directive also makes clear that usage fees should not operate as a brake on innovation.

28. Secondly, any loss of efficiency resulting from unduly low charges is likely to be mitigated to a substantial extent by the possibility of trading spectrum. Where the charges are set below market value, the ability to trade spectrum between operators means that a less efficient operator has an incentive to sell spectrum to a more efficient operator and receive a payment in return (representing a proportion of the higher value that the purchaser privately attaches to the spectrum). In this way the shortfall between the usage fees and the true market value can, in effect, be corrected through the operation of the market itself.

29. This process cannot operate the other way round if spectrum charges are set above the true market value – or at any rate not to the same extent. This is because a more efficient operator will have no incentive to purchase additional spectrum if the market value still exceeds its own private valuation. Consequently, the higher the spectrum charges, the narrower the pool of potential buyers for any marginal spectrum that becomes available. This is plainly detrimental to competition insofar as it results in theoretically efficient competitors being prevented from competing for spectrum which they might otherwise have acquired if the charges had been set at an appropriate level.

30. Thirdly, the imposition of high spectrum charges also carries the risk that spectrum will be returned to Ofcom altogether, in the event that the charges for a given piece of spectrum exceed the private valuation of even the optimal user (or potential user) of that spectrum. Self-evidently, spectrum which ends up being returned in these circumstances would not be being optimally used: Ofcom would therefore be in clear

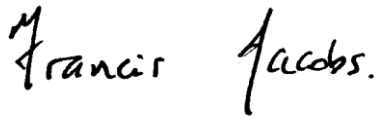
breach of its duty under section 3(2)(a) of the 2003 Act to ensure the optimal use of the spectrum. Even if the spectrum were later to be reallocated at a lower price, the period during which the spectrum lay unused would still potentially cause significant detriment to consumers and the economy in general. (The economic benefits resulting from the use of radio spectrum are another matter to which Ofcom must have regard when carrying out its functions, under section 3(2)(b) of the 2006 Act.)

31. It is no doubt at least partly for these reasons that the CRF contains a number of explicit indications that usage fees should be no higher than strictly necessary to ensure the optimal use of the spectrum. Thus, Recital 32 to the Authorisation Directive warns that fees should not hinder innovation or competition; while Article 13 requires fees to be objectively justified and proportionate.

32. By contrast, there is nothing in the CRF which could serve as a warning against imposing unduly low usage fees. Indeed, it is notable that Article 13 of the Authorisation Directive provides only that NRAs "may" be given the power to impose usage fees: it does not require this power to be available, even where it might help ensure the optimal use of the spectrum. This is consistent with the fact that there is a significant asymmetry of risk between the situations in which usage fees are set, respectively, above and below the true market value of the spectrum in question. Whereas excessive fees are inherently liable to distort competition and harm consumers, unduly low fees are not: instead, low usage fees can be expected to generate benefits for consumers that at least partially compensate for any loss of efficiency, while any loss of efficiency can itself in any event be effectively corrected through spectrum trading. Indeed, we are not aware of any evidence that the current approach to setting usage fees or the existing level of those fees has been inadequate to attain all the objectives of the CRF, including those of the effective management and efficient use of spectrum.

33. For all these reasons we are of the view that Ofcom should set the usage fees at the lower end of the range of possible fees that can reasonably be said to reflect the market value of the spectrum. This is the only way in which Ofcom can both discharge its obligations under the Direction and at the same time minimise the risk that the usage fees will exceed the market value of the spectrum. If that risk were to

eventuate, the result would be that competition and the interests of consumers would be harmed, and the spectrum would not be optimally used, so that Ofcom would be in breach of its fundamental duty under section 3(1)(b) of the 2003 Act. For the reasons explained above, it would not be a defence to any proceedings brought against Ofcom in respect of such a breach that Ofcom had been required to set the charges at a particular level by the terms of the Direction.



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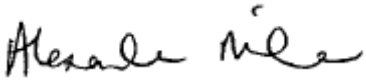

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13 May 2013

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