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Market Forces, Not Gaming, Should Govern the Incentive Auction

by

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Although now delayed until 2016, the FCC [has asked for comments](#) concerning some critical details relating to the incentive auction. The incentive auction is designed to permit broadcasters to voluntarily give up over-the-air broadcast spectrum in the “reverse” portion of the auction in exchange for part of the proceeds realized in the “forward” portion of the auction in which mobile broadband providers are expected to bid. The proposals in the FCC’s December 17 Public Notice appear to further tilt the auction in favor of particular forward auction participants and otherwise interfere with free-market bidding principles. The Commission should reconsider these anti-free-market proposals and stick with proven past auction designs that will maximize revenues and thus encourage maximum broadcaster participation, the key goal of the incentive auction.

Fundamental details of the auction [were decided](#) last summer, but are still subject to pending petitions for reconsideration. As indicated [here](#) and [here](#), the FCC’s current decisions already unreasonably favor certain potential bidders in the forward auction, i.e., every bidder other than Verizon and AT&T. But the new proposals contained in the Public Notice, if adopted, would make matters worse.

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Commissioner Pai got it right in his dissent to the auction procedures Notice:

When it comes to spectrum auctions, we know what works. Keep it simple. Don't restrict participation. And let the outcome be driven by market forces, not centralized planning. We stayed true to these principles in the AWS-3 auction and the results are obvious. We've already raised approximately \$43 billion, more than twice as much as the most optimistic predictions.

These remarks are right on point. The real lessons from the AWS-3 auction, as well as historical evidence outlined [here](#), is that simplicity and the lack of restrictions maximize revenues, encouraging broadcaster participation. Furthermore, the amount of AWS-3 spectrum is still far below the Administration's goal of 500 MHz of spectrum for mobile broadband use. Therefore, it is critical that the Commission achieve all the spectrum it can from the incentive auction.

In fact, the most effective method of implementing the [authorizing legislation](#) would be to conduct an unfettered auction that mimics real world market results. By straying off course from the optimal design, the agency has become more focused on achieving the agency's idea of what competition should look like, rather than maximizing the amount of spectrum volunteered by broadcasters, and hence awarded to mobile providers.

In this regard, the incentive auction notice has three major problems.

First, the artificial skewing effect of creating "reserve spectrum" available only to particular bidders, if the proposal is adopted, would be exacerbated by creating two additional categories of spectrum, "impaired" and "unimpaired," and then assigning only unimpaired spectrum to the favored "reserve spectrum." Spectrum would be impaired if between 15 and 50 percent of "pops" (population served in a market) would receive some interference. Creation of these two categories would create second class licenses, possibly available only for bidders seeking unrestricted spectrum. This proposal violates the Commission's original goal of seeking bids on generic licenses. And it would inevitably suppress auction prices.

Second, the Notice proposes to manipulate "reverse" auction prices, by establishing what the FCC dubs "dynamic reserve prices." Although the Commission already decided to set going-in reverse auction prices last summer, the precise implementation plan seems to exacerbate the problem. The Notice states that the "dynamic reserve prices" of certain stations would continue to decrease even though the price declines below what broadcasters estimate their spectrum is worth, theoretically because the price is too high. The Notice itself only indicates the proposal "will increase the likelihood of a successful auction" without saying why, but in any event would fundamentally violate the "incentive" theory behind the auction. Broadcasters [have already identified](#) 1100 TV stations potentially impacted.

Third, the proposals would seriously increase auction design complexity. Complexity breeds uncertainty, which again risks deterring broadcaster participation in the first place.

It is indeed distressing that the legislatively mandated “expert agency” is straying markedly off course from the authorizing legislation, and is refusing to address potential issues identified by certain Commissioners. The apparent unwillingness of the majority to accommodate these expert differences of opinion as to the scope of relevant considerations appears to be mimicking the dysfunction in other parts of the federal government, which does not serve the FCC well in terms of maintaining its “expert role.”

Achieving competition in the broadband marketplace does not justify such manipulations. Real competition for mobile broadband subscribers depends on a number of factors, including customer needs, the providers’ end user offerings, the number of competitors, and the availability of alternatives, such as wired broadband. All of these factors have little to do with the allocation of spectrum. Even the recent [Seventeenth Annual Report](#) on wireless competition produces no evidence demonstrating that any mobile provider is unable to compete because of the lack of capacity or access to a particular type of spectrum. The Report only couples an identification of spectrum holdings with a theoretical needs analysis, rather than a cause and effect demonstration.

Thus, the only issue relevant to bidding in the auction should be achieving the main goal of the incentive auction as stated by both the [FCC](#) and Congress: to encourage maximum broadcaster participation. The best way to maximize participation is to use free market principles to re-purpose that spectrum for mobile broadband use. The current incentive auction procedures, as well as the misguided further complications proposed in the recent notice, are straying far from this bedrock principle.

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