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IN THE COMPETITION
APPEAL TRIBUNAL

Case Nos. 1238/3/3/15

Victoria House,
Bloomsbury Place,
London WC1A 2EB

11 December 2015

Before:

ANDREW LENON QC
(Chairman)

WILLIAM ALLAN
PROFESSOR COLIN MAYER

(Sitting as a Tribunal in England and Wales)

BETWEEN:

BRITISH TELECOMMUNICATIONS PLC

Appellant

- and -

OFFICE OF COMMUNICATIONS

Respondent

- and -

SKY UK LIMITED

Interveners

TALKTALK TELECOM GROUP PLC

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HEARING - DAY THREE

APPEARANCES

Mr. Rhodri Thompson QC, Mr. Nicholas Gibson and Ms. Anita Davies (instructed by BT Legal) appeared on behalf of the Appellant (British Telecommunications Plc).

Mr. Josh Holmes and Mr. Tristan Jones (instructed by Ofcom) appeared on behalf of the Respondent.

1
2 (10.30 am)

3
4 **MR. SIMON BISHOP (continued)**

5 **Cross-examination by MR. HOLMES (continued)**

6 MR. HOLMES: Good morning, Mr. Bishop.

7 A. Good morning.

8 Q. Can we turn now to consider effects in more detail. At this stage of your analysis, you are
9 assuming that BT has incentives to engage in an arithmetic price squeeze, that is right,
10 isn't it?

11 A. Correct.

12 Q. If the incentives arise because BT has correctly assessed that there is a long-term benefit
13 available to it from marginalising its rivals, which outweighs any short-term costs,
14 anti-competitive effects can in that case be assumed to follow, would you agree?

15 A. I don't think so, but can you repeat the question, please?

16 Q. Of course. So if the incentives arise because BT has correctly assessed that there is
17 a long-term benefit available to it from marginalising its rivals, I have in mind a price
18 increase or some other relaxation of competition at a later point in time, and that that
19 long-term benefit outweighs any short-term costs, anti-competitive effects can in that case
20 be assumed to follow?

21 A. Okay, but I think you are conflating the two steps of incentives and effects. So the incentive
22 step is to assess whether the benefits of increasing the VULA price or, alternatively,
23 lowering the retail price outweigh the costs of doing so. That is what the incentive step of
24 the analysis does. Then you go on and say, well, what are the effects on competition of
25 those incentives? What you've put to me, Mr. Holmes, is assuming that there is an incentive
26 to engage in an anti-competitive margin squeeze, will there be adverse effects? The answer
27 to that latter question is clearly yes, but you are not separating out the two steps.

28 Q. This is really just about structure of analysis, I'm not suggesting that one escapes any stage of
29 the analysis by the point that I am putting. My point is simply that, if the reason why you
30 conclude that there are incentives is on the basis that there is a correct assessment by the
31 dominant firm of a prospect of supra competitive profits at some point, then the effects
32 flow -- the reason why there are incentives can be expected to lead to effects?

33 A. You are conflating the two things again. You are jumping to the conclusion which says, if BT
34 in this particular case -- but it could be true of any vertically integrated firm in any

1 industry -- finds it has incentives to engage in an arithmetic margin squeeze, that is step two
2 in the whole process. Step three is: what are the effects of that? If you are asking me,
3 which I think you are, assuming that the incentives will give rise to an adverse effect, well,
4 yes, then it follows there is an adverse effect, but you can't put those two things together.

5 Q. But the incentives -- this isn't a big point but just to conclude it. Incentives could arise for
6 several different reasons, couldn't they? They could arise because of a balance of
7 short-term benefits and costs, or they could arise because of long-term benefits which
8 outweigh short-term costs?

9 A. Of course. But it is a big point. To be fair, it is a big point, to separate out these two steps in
10 the analysis. I think this is one thing which, and I think I said it yesterday, Mr. Matthew
11 assumes that the adverse effect to the competitor necessarily leads through to an adverse
12 effect on competition. I don't think you can make that step without the evidence to support
13 it.

14 Q. With respect, that is a different point. We are assuming here that this incentive arises because
15 the dominant firm has a well-founded belief which gives rise to an incentive that they will
16 enjoy supra competitive profits later. Of course, there is an assumption in what I am saying,
17 but if that is the basis for the finding of incentive, let's put it like this, there is not a lot of
18 work to be done at the effects stage of the analysis, is there?

19 A. When are you doing that analysis?

20 Q. As part of your conclusion that -- and this is why I say it is simply about where the arguments
21 arise in the process of analysis. But if at the incentive stage you have done an analysis and
22 you have found that there is a well-founded expectation of supra competitive profits later,
23 you have already there arrived at a conclusion that should lead to anti-competitive effects.

24 A. I'm not sure I particularly follow what you are saying --

25 MR. ALLAN: Sorry, I haven't followed the question.

26 MR. HOLMES: Let me try --

27 MR. ALLAN: Well, can I try --

28 MR. HOLMES: -- putting the point one more time, if I may?

29 MR. ALLAN: Please.

30 MR. HOLMES: Thank you.

31 So you assess incentives, and in the assessment of incentives you consider whether the
32 dominant firm will have long-term benefits that outweigh, let's say, short-term costs. The
33 long-term benefits will arise I think, would you agree, as a result of market power at some
34 later point in time which will allow a profit to be taken above that which would occur

1 without the price squeeze, is that right?

2 A. I think you need to be more precise, Mr. Holmes. First of all, we are talking about a dominant
3 firm, and then one increasing market power --

4 Q. Increasing market power at the retail level.

5 A. Right, okay. So again it comes back into why do we break this down? Because if -- you are
6 trying to do the whole analysis in one go essentially, is that correct?

7 Q. I am simply saying that there are some circumstances in which your conclusion about
8 incentives will have done most of the work -- the analysis is overlapping between
9 the effects stage and the incentives stage, and there are some bases for assessing incentives
10 which will lead you to a conclusion which already shows the prospect of anti-competitive
11 effects. It is nothing more than that.

12 A. Possibly.

13 Q. Possibly. Very good. Let's move on. Do you still have the table that I gave you yesterday?

14 A. I do.

15 Q. Somewhere to hand. Does the Tribunal have that?

16 So looking at category 1B, so this table shows consumer reactions if a downstream rival
17 raised retail prices in response to a price squeeze. Category B involved consumers
18 remaining with the rival, and paying a higher price?

19 A. Yes.

20 Q. That would be detrimental to those consumers?

21 A. Yes.

22 Q. Category C involved consumers substituting from superfast broadband to standard broadband,
23 do you see that: purchase SBB instead?

24 A. Uh-huh.

25 Q. This would again be detrimental to consumers whose preference would have been to buy
26 superfast were it not for the price increase?

27 A. No, I disagree, because again you -- here it is saying I am making a choice given the relative
28 prices in the marketplace.

29 Q. But absent the price squeeze.

30 A. Okay, so now we are being very clear that it's only about a price squeeze.

31 Q. Yes. Yes, indeed. Sorry, the table is drawn from paragraph 79 of your first statement.

32 A. Yes.

33 Q. And the premise of that table at 78 is that the VULA fee led to -- so:

34 "The response of BT's VULA-based downstream rivals to an increase in

1 the VULA fee were to be an increase in the retail price of those bundles."
2 So we are assuming here a price squeeze which led to -- and on the table you will see in
3 the title, it is "The response of end consumers if faced with a price squeeze", so I accept that
4 that assumption is built in. But taking that assumption, would you agree that consumers
5 who substitute as a result of the price squeeze from superfast to standard would suffer
6 a consumer detriment in going for a second best option?

7 A. Correct. How big that is we don't know, but yes.

8 Q. No, indeed. But those consumers would have taken a package other than the one they would
9 have preferred, absent the price squeeze?

10 A. Uh-huh.

11 Q. Similarly the same point must apply to E, no purchase of broadband at all. There is also
12 a consumer detriment resulting to the extent that they have effectively left the whole of the
13 market, and with A customers switching to BT, this would be detrimental to consumers
14 whose preference would have been to buy superfast as part of a bundle offered by the rival?

15 A. Uh-huh.

16 Q. Very good.

17 A. Can I just make a point here which is obviously this characterisation was all put forward in
18 the context of incentives, and if we look at this table, we see benefits to BT in a number of
19 the columns, and we see loss to BT in a number of columns. So the overall question about
20 whether these potential consumer detriments would arise or not is predicated on BT having
21 the incentive to engage in the behaviour in the first place.

22 Q. Yes. The first point we are assuming here, once we reach effects, is that there is an incentive,
23 and on that assumption I think you are accepting that if scenarios A, B, C, and E were to
24 arise, there would be a detriment to those consumers, is that correct?

25 A. Sorry, can you repeat the question?

26 Q. You are accepting I think that if the consumer reaction -- if consumers reacted in the ways set
27 out in A, B, C and E, there would be a detriment to those consumers?

28 A. Yes.

29 Q. Yes. Very good.

30 A. In the short run, yes.

31 Q. In the short run.

32 In your discussion of effects, you deal first with BT's current share of supply of retail
33 superfast broadband. Perhaps I can ask you to open your statement in hearing bundle II,
34 tab 9. If you could turn to page 21, you see the effects heading there.

1 A. Yes.

2 Q. It is 86, paragraphs 86 to 89 I have in mind. You say there:

3 "Historic market shares are likely to provide a poor proxy for BT's market
4 power going forward."

5 Could you please turn to Ofcom's decision which is -- it might be worth keeping that open if
6 there is space on your table -- hearing bundle III, part I, tab 1. The relevant paragraph is
7 3.55 on page 29.

8 You will see from the third bullet point that Ofcom also looked at forecasts of BT's market
9 shares in the future and that those forecasts came from BT and Virgin. You will also see
10 that the forecasts were for BT to acquire a higher share of superfast customers than it
11 currently has?

12 A. Yes.

13 Q. As far as we are aware, those forecasts are not predicated on the assumption that BT will
14 engage in a price squeeze?

15 A. That is my understanding.

16 Q. So if BT were to price squeeze, its share of the retail market might be even larger?

17 A. Right, yes, but again you are starting off from the assumption that BT has an incentive to
18 engage in this anti-competitive behaviour.

19 Q. But we are agreed that that is the assumption that one adopts when one turns to effect.

20 A. I do, but when you put it into the context of these numbers, it is also relevant to think about
21 what impact would this have on their incentives. And I think again it was a point I made
22 yesterday: if you have a highly developing -- a fast-moving market, everyone accepts the
23 retail market is competitive, everyone accepts that Virgin is a first grade competitor, on
24 these numbers I wouldn't have the incentive.

25 But I take your point and say, okay, let's assume they do have the incentive --

26 Q. These paragraphs, they are in your effects section, so ...

27 A. Yes, but if they do have the incentive, are there adverse effects at the moment arising in the
28 marketplace with this growth in market shares? And I think the answer is no. I think we all
29 agree on that. Then we say, well -- I really don't know where this leads us. We are doing
30 well, we are competing in a competitive market, it's predicated on, well, now wouldn't it be
31 bad if we engaged in some anti-competitive behaviour? Yes, of course it would be.

32 Q. And subject to the caveat that market shares are only one consideration when assessing market
33 power, those forecasts do support the view that BT could obtain a degree of retail market
34 power in the future?

1 A. No, no. Why do you presume that a share -- first of all, these are shares of superfast
2 broadband. Again we are all on common ground that the relevant market is all broadband.
3 But even if we were to take these market shares at face value, why does having
4 40 per cent/45 per cent give you market power in an economic sense rather than just the sort
5 of market -- based purely on market shares?

6 Q. You accept that --

7 PROFESSOR MAYER: Could I just pursue that point a little bit. I think we would benefit from
8 hearing the extent to which you think that there is actually substitution between the two
9 markets. Because we heard yesterday how the superfast broadband market could be
10 regarded as essentially a premium market attracting premium customers, so are we really
11 talking about a high degree of substitutability between those two points?

12 A. I think those are essentially matters of fact. It is one which Ofcom's own analysis indicates
13 there is a high degree of substitution. Now, clearly there are going to be some customers
14 who will only ever take the superfast fibre product, and particularly if it is a very high
15 speed, there are other consumers who are only interested in a very low speed, and what
16 really matters is the overlap between people who want speeds -- and I don't know if these
17 numbers are right, 20 megabits is probably appropriate for most people, and then make
18 a trade-off of whether they want to upgrade to 30 or more megabits depending on the relative
19 relative prices, and it is that relative price which will provide the competition between
20 standard and superfast broadband.

21 PROFESSOR MAYER: In making that assumption about a constraint, that is predicated on the
22 presumption of a high degree of substitutability?

23 A. My starting point for the analysis is Ofcom's finding that there is a high degree of substitution
24 between those two products which is where they have defined the relevant market as all
25 broadband.

26 PROFESSOR MAYER: Do you think that will persist into the future?

27 A. I think it will certainly persist -- first of all, to argue it won't one would have to have a pretty
28 good understanding of why the markets dynamics are going to change considerably. Even
29 on the figures that I have seen, in the next two years 50 per cent of the market will be
30 superfast broadband, the other 50 per cent will be standard broadband. We are
31 talking -- Mr. Heaney talks about the need to upgrade people. BT, I think with 50 per cent
32 of the subscribers still there, that competition in the next couple of years is still going to be
33 pretty intense.

34 PROFESSOR MAYER: Thank you.

1 MR. ALLAN: Can I just ask, to follow up Professor Mayer's question, do you see that
2 substitutability working both ways? In other words, with SBB constraining SFBB almost as
3 strongly as SFBB might constrain SBB?

4 A. I think so, yes. If you are trying to get a subscriber to either enter the broadband market or to
5 upgrade, and it can be upgrading within standard broadband, it is not one homogenous
6 product within standard broadband, people will make choices based on speed, quality and
7 relative price.

8 MR. ALLAN: Thank you.

9 MR. HOLMES: May I consider the question of differentiation a little further to explore the
10 constraints from standard broadband. Could you ask you to turn to Mr. Matthew's
11 statement in the evidence bundle, so you can put away the decision. The paragraph I have
12 in mind is paragraph 96 --

13 A. Which tab please?

14 Q. Sorry, tab 12. Paragraph 96. If you could just read the opening words of that paragraph.

15 A. Yes.

16 Q. So what Mr. Matthew is saying is that because of the differentiation between standard and
17 superfast broadband, competition in the supply of superfast is likely to deliver specific
18 benefits to consumers. If you look through the subparagraphs which follow, you see that
19 they are emphasising the extent to which superfast is differentiated and expected to become
20 more so.

21 A. But I think it comes back to this is the sort of ex post -- you know, trying to move away from
22 the finding, Ofcom's own finding, that standard broadband does provide an effective
23 competitive constraint on superfast broadband. And if we do the definition of the relevant
24 market properly, what that is saying is even a hypothetical monopoly supplier of superfast
25 broadband wouldn't have market power, because they would be constrained by standard
26 broadband.

27 So all of the things that Mr. Matthew talks about here are sort of true in terms of talking
28 about the characteristics of superfast broadband vis-a-vis standard broadband, but that
29 doesn't get away from the fact that standard broadband is still providing an effective
30 competitive constraint on superfast broadband.

31 Q. But the degree -- you would agree this is a matter of degree rather than necessarily of binary
32 distinctions? There are degrees of differentiation, degrees of constraint as between different
33 products within a market?

34 A. I don't know. Because again this is -- we are talking about standard broadband and superfast

1 broadband as if that is the only thing consumers are buying. But if they are buying the sort
2 of TalkTalk TV add-on, BT Sport or Sky options, it goes into a big bundle. Sorry for the
3 pun. And the weight that consumers will -- one consumer will place on superfast broadband
4 will be different from another.

5 So I don't think you can say, well, the intensity of competition between superfast broadband
6 providers is overwhelmingly much, much more important than the competition between a
7 standard broadband provider and a superfast broadband provider.

8 Q. But would you agree that the evidence suggests a shift over time towards greater
9 differentiation between standard and superfast?

10 A. No, the evidence suggests the proportion of people in the broadband market who would take
11 up superfast broadband is increasing.

12 Q. You suggested this was ex post justification. May I briefly take you to Ofcom's findings about
13 the retail market which are contained in the review of the wholesale broadband access
14 markets, which is in volume III, part II, at tab 7, page 43. You see the heading there
15 "Future Developments", and if you could just cast your eye over those paragraphs, and the
16 conclusion at 3.71.

17 A. Yes.

18 Q. You see at 3.71 that there is evidence at the moment to define the single market:

19 "... factors pointing to a separate market potentially emerging at the retail level
20 for SFBB products at some point in the future but insufficient evidence to
21 conclude this is likely to occur during the three-year forward-looking period of
22 this market review."

23 A. Yes.

24 Q. So a suggestion of factors pointing to a separate market potentially emerging in the future.

25 A. Okay, but on the basis of the available evidence over the period of the review, the best, most
26 appropriate definition of the relevant market is all broadband. If things change in the future,
27 maybe the competitive assessment will change, but what we are looking at here is the here
28 and now, and the relevant market is broadband.

29 Q. But it might be rational, might it not, for a company in BT's position to take steps now, in
30 view of an anticipated change in the market, outside the market review period, which runs
31 until March 2017 I think.

32 A. This then comes back to the incentives point. I thought we were on to effects. This is -- this
33 comes back to a point which we haven't really touched on, which is the risk of BT engaging
34 in -- having the incentives to engage in a margin squeeze which then give rise to a risk of

1 adverse effects for consumers. Now we are layering on, on top of that, a risk that
2 the market in the next couple of years will change. So now we have added another
3 undefined probability into the overall competitive assessment.

4 Q. May I turn now and pursue further the line of questioning that Mr. Allan raised with you,
5 namely, the symmetry of constraint between standard broadband and superfast broadband.
6 We saw yesterday the evidence of Mr. Heaney that once customers switch to superfast
7 broadband, they will be less likely to switch back.

8 A. I remember that, yes.

9 Q. We heard also yesterday the evidence of Mr. Murray, accepting that access speed is one key
10 factor affecting the broadband experience and customer perception of ISP performance. Do
11 you recall that?

12 A. Yes.

13 Q. If that is correct, competition in relation to standard broadband pricing is unlikely to provide
14 as strong a constraint in relation to superfast broadband for the ever increasing proportion of
15 consumers who have already made the switch?

16 A. That may well be true. But again, you know, what we are talking about is the overall market.
17 The incentive to increase the VULA price applies to the whole market. As you eloquently
18 described, Mr. Holmes, this is not about discrimination, this is about an increase in the
19 VULA price to everyone, and the fact that there may be pockets of people who would
20 never, ever, ever switch away from superfast broadband is relevant, but what is also
21 relevant is how large -- what proportion of consumers they account for in the overall
22 market, and we don't have any indication of that.

23 Q. We have forecasts about the expected numbers of superfast broadband consumers by the end
24 of the period as a proportion of all broadband consumers, and we also have indications of
25 the trend and the expected move in the market.

26 A. And again, all of those trends are predicated on a non-margin squeeze behaviour by BT.

27 Q. But when assessing effects they're relevant, aren't they?

28 A. When assessing incentives they are relevant.

29 Q. Very good. At paragraph 96 of your first report, you say that BT's VULA-based rivals could
30 re-enter the superfast segment at low cost even if they had been excluded?

31 A. Yes.

32 Q. Can I check, this is on the assumption that BT subsequently ceased the price squeeze which
33 led to the exclusion?

34 A. Correct.

1 Q. And there is no economic reason why BT should do this. The margin squeeze would involve
2 end to end profitability after the rivals had been excluded from the market? They could
3 decide where they took their profit at the upstream or the downstream level?

4 A. Right. I think -- again, I know you want to just talk about effects, but I think we do need to
5 keep coming back to the incentives. What I would have liked to have seen in the Ofcom
6 final statement is some assessment about what proportion of TalkTalk subscribers and Sky
7 subscribers would switch to BT because it's not obvious that even if large numbers of those
8 were to do so, this price increase in the VULA would actually be profitable.

9 Moreover, what we heard from Mr. Petter yesterday is that there is -- it does make
10 a difference, the functional separation does make a difference on the incentives of this
11 particular vertically integrated firm in terms of where the profits are taken. In other
12 industries without functional separation, whether you take the profits upstream or
13 downstream may not be relevant, but in this particular case it is relevant.

14 Q. So working down the assumption that BT did for some reason cease the price squeeze which
15 led to the exclusion, Mr. Heaney gives evidence about the costs of re-entry that would then
16 arise. That is at paragraphs 39 to 41 of his statement at tab 14 of hearing bundle II. We will
17 see in paragraph 39 that, based on his business experience, he disagrees with your view that
18 the cost of re-entry would be low.

19 A. Yes.

20 Q. His view is that if TalkTalk were excluded from the superfast segment, its reputation for
21 providing attractive services would diminish.

22 Sorry, just to -- that is in the second sentence of paragraph 41.

23 A. That is his view, but why? If TalkTalk had a reputation for providing attractive services in
24 standard broadband, then why would it not be able to carry that over? And indeed my
25 understanding is that that is part of the argument, it's about I've got a standard broadband
26 subscriber today, I am providing great service, that is the person I want to upgrade.

27 Q. But if they are not active specifically in the superfast segment, their brand won't be associated
28 with providing that service in the minds of consumers.

29 A. Does TalkTalk at the moment have a branding strategy focused on superfast broadband?

30 I don't think so.

31 Q. He also expresses the view that higher marketing expenditure would be needed to re-enter the
32 superfast segment in order to overcome lack of awareness and credibility.

33 A. Yes, and again we talked about this at some length yesterday. They may have to spend a bit
34 more money, but when they get back into the marketplace they are effective competitors.

1 Q. But it might take them time and it would involve costs for them to undertake that re-entry.
2 They won't immediately acquire the reputation for brand, the awareness -- the brand
3 awareness and credibility in superfast broadband?

4 A. But again I think how important is the brand awareness related solely to superfast broadband?

5 Q. We heard the evidence yesterday that BT had established a separate brand for superfast.

6 A. Yes, that is BT. But has TalkTalk? Has Sky? I'm not -- I haven't done a detailed analysis of
7 this but just sort of casual internet browsing doesn't come out with something like TalkTalk
8 superfast broadband on a completely separate page from TalkTalk standard broadband.

9 Q. He also refers at paragraph 40 to customer inertia which would need to be overcome,
10 particularly for the large base of customers who had already made the switch to superfast
11 broadband.

12 A. Yes.

13 Q. If the position is as he states, there will therefore be time and costs involved in re-entering?

14 A. I think in any market there are customer inertia and degrees of switching costs, but do they
15 prevent people from competing effectively? No. So he is basically -- what Mr. Heaney is
16 talking about is wouldn't the world be better if there was no customer inertia, it would be
17 much easier for me to get consumers. Yes, but the world isn't like that. But does this stop
18 TalkTalk, upon re-entry, being an effective competitor?

19 And here, remember, this is all predicated on BT through the benefit of trying to increase its
20 own retail prices in the future. If it did that, TalkTalk would be in the position that it is in
21 today to undercut that offering, and some consumers, potentially not all, but some
22 consumers would switch and find that new offering attractive.

23 PROFESSOR MAYER: Could I just intervene at that point. You are saying that if a competitor
24 had left, that they could re-enter if prices rose again. But if they have observed BT
25 engaging in a margin squeeze once in the past, why would they not predict that happening
26 again and thereby be discouraged from entering on a subsequent occasion?

27 A. Presumably if BT had engaged in an anti-competitive margin squeeze they would have been
28 subject to some competition law investigation which would involve potentially significant
29 finds, bad damage reputation to the business, why would they want to go through that
30 again? I think it comes back to what is the role of ex post competition law in preventing
31 such behaviour?

32 PROFESSOR MAYER: So you would rely on the operation of subsequent interventions to
33 prevent that happening in the future?

34 A. As a backstop. But where my main reliance is on is the analysis of BT having the incentives

1 to engage in this behaviour in the first place. But predicated that they did, I think the
2 ex post competition law, why wouldn't it have those effects?

3 PROFESSOR MAYER: Thank you.

4 MR. HOLMES: Turning to the constraints from Virgin Media --

5 A. Sorry, if -- before we move on I would just like to -- one of the points here in terms of re-entry
6 is made by Mr. Matthew in his report, footnote 19, where it states:

7 "TalkTalk has argued that it would be commercially irrational for a CP to make
8 a strategic decision not to compete with superfast broadband customers when
9 superfast broadband is the fastest growing sector in the market ..."

10 And here is the point:

11 "... the incremental investment required to develop a fibre retail proposition is
12 relatively small."

13 So it is saying that the cost of getting into superfast broadband is relatively small.

14 Q. That is a matter that can no doubt be discussed with Mr. Matthew. We have the evidence of
15 Mr. Heaney about his perception of the costs.

16 Virgin Media can plainly impose some constraint on prices for superfast broadband but you
17 are not saying, are you, that the existence of Virgin Media as a competitor would replicate
18 all of the advantages which would otherwise be gained from competition in the superfast
19 segment from other VULA-based providers?

20 A. Where it is not active, that is clearly the case.

21 Q. And that is the point about the limited coverage. We have seen that TalkTalk's data suggests
22 that consumers are more likely to move to BT or Sky, which also uses a BT network, than
23 to Virgin. Would you agree that those factors also serve to limit the extent to which Virgin
24 would be able to exercise a competitive constraint?

25 A. Well, I don't know. Because again, as we discussed yesterday, those figures covered all
26 switching and were not related just to superfast broadband. Again, that is a relevant piece
27 of information which one would have expected to see in Ofcom's analysis.

28 Q. Another point you mention is the possibility that other communications providers might invest
29 in their own fibre network, and that is at paragraph 92 of your report.

30 A. Correct.

31 Q. As we discussed yesterday, and as I know you are well aware, Ofcom has found that BT has
32 significant market power at the wholesale level. Can I ask you to turn to the relevant
33 statement. It's the Fixed Access Market Review statement which is in hearing bundle III,
34 volume II at tab 8. The page is 155 and the paragraph is 7.87. So this is discussing the

1 assessment of market power in WLA which is the market within which the VULA remedy
2 is imposed. Do you have that?

3 A. Yes.

4 Q. You will see there a discussion of barriers to entry, Ofcom's assessment of the likelihood of
5 entry at scale.

6 A. I do.

7 Q. If the position is as stated there, one cannot safely rely on entry at scale?

8 A. Correct.

9 Q. Mr. Heaney has also given evidence on this point at paragraph 44 of his statement, so turning
10 back to tab 14 of the witness bundle.

11 A. Yes.

12 Q. You will see his view in the opening words of that paragraph, that:

13 "The constraint of upstream entry is very weak."

14 He refers to similar factors to Ofcom, and he notes in 44.2 in relation to the York venture
15 that:

16 "It will take a decade or more to roll out ... the build out is relatively slow and
17 would cover in any event a relatively small proportion of Openreach's customer
18 base."

19 A. Yes, but if you also look at paragraph 44.4 of this:

20 "The decisions regarding roll-out of our own infrastructure are based on our
21 view. Over time, the prices of wholesale SFBB products will be brought down
22 from the current alleged excessive levels by price regulation."

23 So the incentives to invest in the own infrastructure are, in Mr. Heaney's own words, related
24 to on what terms he can get access to BT's network.

25 Q. But if there were a successful margin squeeze in relation to TalkTalk, and its subscriber base
26 fell, this would affect the business case for investment of this kind, wouldn't it? You would
27 have fewer customers to spread the costs of the network build over?

28 A. What Mr. Heaney is saying here is if I get good enough access terms, I'm not going to build
29 my own infrastructure. That is how I read this paragraph. But if I get -- and the better
30 terms I get access, the less incentive I have got to invest in my own infrastructure. And that
31 clearly has to be correct.

32 MR. HOLMES: Sir, those are my questions.

33 **Re-examination by MR. THOMPSON**

34 MR. THOMPSON: Mr. Bishop, the issue of the relationship between standard broadband and

1 superfast broadband and future development was raised both by Mr. Holmes and then more
2 recently by Professor Mayer. We looked at paragraph 3.71 of the wholesale broadband
3 access market review, if I could ask you just to look at that again.

4 A. Where is that, please?

5 Q. It is in tab 7 of bundle III/II. If you start at page 35 in the clip, paragraph 3.40, you will see
6 a heading, "Our Conclusions"?

7 A. Yes.

8 Q. I think you referred to Ofcom's market analysis in various places in your evidence. Was this
9 what you had in mind as the type of analysis you were talking about?

10 A. I haven't reviewed this, but -- so my analysis was based on Ofcom's own conclusions. But
11 looking at this, this is exactly the kind of analysis which supports Ofcom's conclusions, that
12 the relevant market includes standard broadband and superfast broadband.

13 Q. In particular, if you turn forward to 43 and 44, it was a point that I think Mr. Holmes made in
14 his opening submissions, you will see a heading "Future Developments".

15 A. Sorry, which paragraph?

16 Q. Pages 43 and 44.

17 A. Yes.

18 Q. I think really the point that was being put to you is covered at 3.70 at the top, just before the
19 conclusion. If you could read that and give any response you may have as to how that bears
20 on the debate that has been raised with you by Mr. Holmes and Professor Mayer.

21 A. Yes, I think this is a more articulate expression of what I was trying to say, which is that if
22 you still have 50 per cent of the market who haven't upgraded then standard broadband will
23 still provide an effective competitive constraint.

24 Q. I don't think you were taken to the last sentence of 3.71 which deals with the EU issue, and
25 what is your response to that?

26 A. I think the EC decision here, or this last sentence, again I haven't reviewed it, but it seems to
27 be confirming Ofcom's own conclusions.

28 Q. I think that is the starting point, but if you could then turn into the next tab, the market review
29 itself, and turn to page 135. Is that the type of thing you had in mind in terms of Ofcom's
30 market definition?

31 A. Yes.

32 Q. And it goes through. If, for example, you turn through to pages 138 and 139, you see
33 an approach described at 7.29 at the bottom of 138?

34 A. Yes.

1 Q. Preliminary observations followed by identification of focal product, and then the vexed
2 question of the modified greenfield approach arises here. Then product market definition,
3 geographic market definition and conclusions. You see that is the structure of the analysis?
4 A. Yes.
5 Q. Then a conclusion, I don't think we need go through it all, is at page 149, paragraphs 7.62 to
6 7.63.
7 A. Yes.
8 Q. Is that what you had in mind in relation to Ofcom's position as at June last year?
9 A. This is talking about the wholesale market. I think I was really focusing on the retail market.
10 Q. Yes.
11 A. The two are going to be related. But I think my assessment was based on Ofcom's own
12 conclusion that the relevant retail market included standard broadband and superfast
13 broadband.
14 Q. Yes. I have taken it slightly quickly. It may assist you if I take you back to 7.36 at page 141
15 so you understand how the analysis develops. Is that the point you had in mind?
16 A. Yes, agreed.
17 Q. Then just for good measure, because this obviously only takes the matter up to June 2014, but
18 I think you have effectively been asked to look at the position as at the date of the decision
19 which is obviously the right date, and this is partly a legal question, but Ofcom's under
20 an obligation to reconsider this matter and bring it up-to-date. This is just -- I'm not
21 intending to lead, I don't think it is a matter within Mr. Bishop's knowledge.
22 If you could turn to the decision itself, which is in bundle III/1, and in particular at page 9,
23 you will see a red line heading again, "No Material Change Assessment", and then
24 an explanation of the legislation under there, do you see that?
25 A. Yes.
26 Q. 2.9?
27 A. Yes.
28 Q. Then if you read at 2.14 and 2.15 the conclusion, and I would just like your comment on how
29 that bears on this debate. (Pause)
30 A. I think this is just supporting my starting point for the analysis which I took as Ofcom. They
31 are -- I think this is a sensible conclusion for Ofcom to reach, that the relevant market
32 includes both products.
33 Q. Thank you very much. You were also asked about the pattern of additions that could be
34 anticipated going forwards and, in particular, the evidence of Mr. Matthew which is at

1 tab 12 of the witness bundle. Paragraph 34 gives three confidential figures for BT net
2 additions in 2012/2013 and 2013/2014 and 2016/2017. Do you see any trend in those
3 figures without going into the confidential numbers themselves?

4 A. I do. I think I mentioned these figures yesterday, it's BT's share of VULA connections, so that
5 is excluding SFBB connections from Virgin, so just on the VULA connections is decreasing
6 significantly.

7 Q. Yes, and if you turn over the page to the figure 4, which is again confidential, I think you will
8 see the point you have just made, that the green line, the Virgin line, is moving in
9 a particular direction and the red/orange lines, who I think are the two CPs for whom
10 Mr. Heaney and Mr. Blumberg are the champions, are moving in the opposite direction?

11 A. Correct.

12 Q. So what do you infer about the relationship between those two trends?

13 A. It's hard to come to overall conclusions about the overall competitiveness of Virgin, but the
14 fact that Sky and TalkTalk are increasing indicates that they are able to compete effectively
15 for standard -- sorry, for superfast broadband customers in the market today.

16 Q. In terms of the figures at 34, how do you interpret the relationship between those lines and the
17 figures at 34?

18 A. I'm not sure I know the question, but it's certainly saying that the take-up from Sky and
19 TalkTalk combined is greater than that from BT VULA connections.

20 Q. There was some discussion of bundling and the significance of triple play bundling.

21 I don't think you were taken to what I think is at least one of the relevant passages in the
22 final statement, which is at paragraph 5.107.

23 A. In bundle?

24 Q. Bundle III, tab 1. In particular, the sentences in the middle about the significance of triple
25 play and the associated figure over the page, and I would just like you to comment on that
26 finding by Ofcom.

27 A. It speaks for itself. Triple play is becoming increasingly important in the fixed broadband
28 sector, and therefore, going forward, we expect triple play to have a more important role in
29 determining consumer choice.

30 Q. Then, finally, could I just take you to the table that you were asked questions about both
31 yesterday and today which I have put into your statement at the relevant point, if I can find
32 it. I would like to ask you about the left-hand column. I think you were mainly asked about
33 the right-hand column and you were asked a bit about the left-hand column.

34 A. Yes.

- 1 Q. There are two options there, that there might be a response either to increase prices or to
2 absorb price increases?
- 3 A. Correct.
- 4 Q. I think the "rival" here was intended to focus on TalkTalk and Sky. Did those two options
5 exhaust the possibilities for TalkTalk and Sky as responses or not?
- 6 A. I think the only alternative is rather than push SFBB products, they push standard broadband
7 products, but I think that is sort of covered under 1C.
- 8 Q. But in terms of the right-hand column, is that a benefit or a loss to BT?
- 9 A. If they focus more on standard broadband than on superfast broadband, that would be a loss to
10 BT.
- 11 Q. In terms of rivals, does that exhaust the possibility or are there other rivals who should be
12 taken into account for BT?
- 13 A. There is obviously Virgin.
- 14 Q. What would Virgin's likely response be?
- 15 A. If rivals are putting up their price, then that is going to be a benefit to Virgin.
- 16 Q. How will that sit in the right-hand column for BT?
- 17 A. That would be a loss.
- 18 Q. It is put in terms of "rival", I assume that is because of the wooden dollars point. But if you
19 put "customer" there, you would presumably include BT Consumer itself?
- 20 A. Yes. I don't want to overplay the functional separation point, BT is a vertically integrated firm
21 so will take -- overall consider upstream and downstream, but the functional separation does
22 affect the incentives. And as John Petter described yesterday, the profits of BT Consumer
23 are important to the overall share price and to him personally.
- 24 Q. Thank you. Finally, and I think it was roughly where we ended, paragraph 3.55, the market
25 analysis. And it ties in with the chart we were looking at from Mr. Matthew just a moment
26 ago. It's at pages 29 to 31 of the decision. If one looks at the first bullet point on page 30,
27 you will see a figure for Virgin at just over 50 per cent. I don't think that is confidential, it
28 is approximately 51 per cent.
- 29 A. Correct.
- 30 Q. Then over the page at 31, you see a figure for Virgin which is confidential but which is
31 consistent with the graph, in fact it may be the same number that appears in the graph of
32 Mr. Matthew.
- 33 A. I would hope it is the same number, yes.
- 34 Q. I think it was put to you by Mr. Holmes that if the VULA price went up, it would be all good

1 news for BT. But what about its relationship with Virgin, how would you anticipate those
2 figures to move if the VULA price went up?

3 A. Well, you would expect the Virgin share to increase.

4 MR. THOMPSON: Thank you. I have no other questions. I don't know if the Tribunal has any
5 further questions.

6
7 **Questions from THE TRIBUNAL**

8 MR. ALLAN: Mr. Bishop I did just want to clarify one thing with you. In your evidence
9 yesterday, it's at transcript -- do you have the transcript?

10 A. I don't.

11 MR. ALLAN: Perhaps you can be provided with a copy of the transcript. Others may not have it
12 but I will quote the sentence. It's page 86, lines 15 and 17, where you say:

13 "Again those are commercial decisions, but what is relevant in terms of whether
14 they can compete is whether they earn positive margins."

15 My question is simply: positive margins measured on what base of cost?

16 A. In terms of -- I would say sort of the average incremental cost, so provided they have
17 a positive margin then they can compete effectively against BT, Sky and Virgin.

18 MR. ALLAN: Long-run or short-run?

19 A. I think at this stage in the market you would be looking at short-run, because it is very difficult
20 to work out in a fast-moving market what are the long-run costs involved.

21 MR. ALLAN: You referred yesterday and in your report to the Commission guidance, and I think
22 the Commission would use a long-run incremental cost assessment.

23 A. Yes, but the question -- and even if everyone accepts that is the appropriate standard, I think it
24 is going to be very difficult to calculate what that long-run average incremental cost is, and
25 I think that takes us into the other half of this process in determining what is the appropriate
26 margin squeeze test.

27 MR. ALLAN: Thank you.

28 PROFESSOR MAYER: Could I just pursue that a little bit further. Notwithstanding the
29 problems of measurement, is a long-run average incremental cost the right approach to be
30 taken?

31 A. I think it depends on over what period firms need to recover that. So you'd assume that there
32 is full agreement over what the long-run average incremental cost is. As Mr. Petter
33 described yesterday, if he buys -- BT buys some Premier League sports or Champions
34 League, that is an investment. If he is required to recover the costs of that investment over

1 the life of the investment, that would give you a very different answer to if you are required
2 to recover the costs of that investment on a month by month basis. I think that is the real
3 difficulty here, when you have got lumpy upfront investments, trying to work out how
4 you -- how that should impinge on short-term pricing incentives.

5 PROFESSOR MAYER: But supposing you were advising them as a client, what would be the
6 appropriate way for them to be thinking about this?

7 A. For me, I think they need to earn positive short-run average incremental costs, and then there
8 is an element about -- with an expectation, and purely an expectation, that over the life of
9 those investments they will recover the full cost. But of course the expectations is the
10 important part here, because I can invest in an asset thinking that it is going to be hugely
11 attractive, which will give me one level of long-run average incremental cost, and I turn out
12 to be wildly optimistic, suddenly my long-run average incremental cost is twice the size,
13 assuming I get half the subscribers I effect.

14 I think that is the difficulty here, and that is why looking at the short-run average
15 incremental cost is not going to give you the total answer, but at least it indicates whether,
16 on the short-run basis, firms can compete profitably for incremental subscribers.

17 PROFESSOR MAYER: Right. But in terms of what one might expect over the long-run, the
18 expectation should be inconsistent with recovery.

19 A. I think so. But it is then, how does that impinge on the short-run pricing decisions? And as
20 soon as it is factored into the short-run pricing decisions, that is when I think things can go
21 seriously awry.

22 PROFESSOR MAYER: Thank you very much.

23 MR. ALLAN: Just to follow up a little bit on that. If we are looking at a test which is concerned
24 with sustainable competition then, as part of the assessment, does that tend to suggest we
25 are looking at the more long-run element of the approach and that the expectations to which
26 you refer are quite important?

27 A. Answering your question in two parts, first of all, yes, the expectations are critically
28 important, but then the first one comes back to, well, what is the competitiveness of the
29 market that we are discussing today? We are discussing a highly competitive retail
30 broadband market, and so given that, plus all the difficulties associated with implementing
31 one of these margin squeeze tests, it says you've got to have very strong evidence before
32 I would want to intervene in this marketplace.

33 This is not a situation where you have an upstream monopolist, there is no other way of
34 getting into the market, who is controlling the inputs of everyone else in the marketplace.

1 I think that is the context in which I sort of view this whole issue about whether a margin
2 squeeze test should be introduced at the moment.

3 MR. ALLAN: Thank you.

4 THE CHAIRMAN: Shall we break then for five minutes.

5 (The witness withdrew)

6 (11.45 am)

7 (A short break)

8 (11.50 am)

9 MR. HOLMES: Sir, may I call Mr. Clarkson.

10 THE CHAIRMAN: Yes.

11
12 **MR. DAVID PETER CLARKSON (affirmed)**

13 **Examination-in-chief by MR. HOLMES**

14 MR. HOLMES: Good morning, Mr. Clarkson. You should have, I hope, hearing bundle II to
15 your left.

16 A. Yes.

17 Q. Could you turn to tab 11 in the bundle?

18 A. Yes.

19 Q. On page 2, is that your name and address given at the top of the page?

20 A. Yes, it is.

21 Q. If you turn to the final page of the bundle, does your signature appear there?

22 A. It does, yes.

23 Q. Is this the evidence that you have given in these proceedings?

24 A. It is.

25 Q. Very good. I think Mr. Thompson may now have some questions for you.

26 **Cross-examination by MR. THOMPSON**

27 MR. THOMPSON: Yes, I can say good morning as well, only just. Good morning,
28 Mr. Clarkson.

29 I will do my best to follow the order of your witness statement, which hopefully will be
30 easy for everyone, although I will jump about a bit.

31 Could I ask you just to take it up and go straight to paragraph 2?

32 A. Yes.

33 Q. Where you say that:

34 "The Notice of Appeal relates to Ofcom's decision made as part of Ofcom's

1 recent Fixed Access Market Review."

2 I understand why you say that, but just to clarify, there was a consultation in relation to this
3 matter that started a week before the FAMR decision -- I think one finds that, I don't think
4 you need to open it at this stage, it's at tab 6 of the bundles -- whereas the FAMR decision
5 itself was issued the next week on 26th June, that is right, isn't it?

6 A. That's correct.

7 Q. Indeed the whole point of the two documents was that there was a separate consultation on
8 this matter that we are concerned with now.

9 A. Yes.

10 Q. There were a number of options that were put out in the consultation and I think it might be
11 worth at this point just taking that up and having a look. As I said, that is at tab 6 of
12 bundle III/II if you could find that.

13 I think the reference I was giving was to the other document which made clear there was
14 going to be a separate consultation, but here it is, so I don't think we need to go into that.

15 Your original idea had been to retain the 2010 approach, that was the original idea going
16 back into 2013, do you remember that?

17 A. Yes, it was. It was to retain the fair and reasonable non-discrimination condition and
18 supplement it with detailed guidance, as I recall.

19 Q. And you find that at page 5, paragraph 2.6. That was the original consultation?

20 A. Yes.

21 Q. I think you then had another thought which was to supplement the existing obligation with
22 an information obligation, do you recall that? A monitoring obligation? You are looking
23 a bit blank, so if we turn to the other bundle, it is in the previous bundle, III/I, at tab 4.

24 A. Okay.

25 Q. Do you remember, if you turn to page 9, there was a consultation question. You see at 5.1 the
26 question --

27 A. Yes.

28 Q. -- about an obligation for BT to provide more information?

29 A. Yes.

30 Q. Do you remember that?

31 A. Yes.

32 Q. I'm sorry to make you jump about in the bundles but just for clarification of what was going
33 on. Then the 2010 approach was still an option in the consultation, and I think you see that
34 at paragraph 4.49 on page 47.

1 A. Yes, I have that.

2 Q. So there are four options, the first of which is essentially the status quo, is that right? Option
3 A, do you see that?

4 A. Yes, it is subtly different from 2010 because it has the supplementary guidance on how we are
5 likely to take the assessment.

6 Q. Yes, and we will come to that in a moment. You will recall there was some perhaps rather
7 informal guidance given in 2010 but there were some indications given at least?

8 A. It was, it was quite short, but ...

9 Q. Yes. And then the description of option A is at 451 to 453 on the opposite side, and I think it
10 is a debate. One sees in 4.52 there is a reference to a lesser degree of certainty, do you see
11 that at lines 3 and 4?

12 A. Yes.

13 Q. And then at 4.53:
14 "On the other hand, flexibility ..."

15 A. Yes.

16 Q. So there is a sort of give and take --

17 A. A trade-off.

18 Q. -- that you make it rigid, it's more certain, or you leave it to the guidance, it is more flexible.
19 And that I imagine was a debate Ofcom had over a period of months, indeed years, as to
20 which was the better approach?

21 A. Sure.

22 Q. So the position if I can put it to you: by 19th June 2014, Ofcom had moved in its preferences
23 from the original 2013 proposal but it was still an open consultation, if I can put it that way.
24 So it wasn't a foregone conclusion at that point that there would be a new condition
25 imposed, is that right?

26 A. Yes, that's correct.

27 Q. I can see you nodding --

28 A. Sorry.

29 Q. I am assuming all the questions I've asked effectively you've said yes in relation to. If you
30 said anything different -- so maybe for the transcript we can bear that in mind.
31 Then the other question is given this uncertainty and given that the decision has been taken
32 the following week in relation to VULA and everything else, is it right to assume that the
33 2010 approach, given that there was a FRAND condition, essentially rolled on until
34 March 2015, or was there a gap?

1 A. So at the time, and from a point of view of policy, it was the intention that the fair and
2 reasonable condition as per 2010, which also sort of required BT to not margin squeeze,
3 would be in place, and then in fact we would be sort of either changing it or supplementing
4 it depending on where we went to with the VULA margin consultation.
5 I say that was the intention, because in light of this appeal I have sort of subsequently been
6 advised by our lawyers that, in fact, had we have needed to actually do a margin assessment
7 in that period from June 2014 to March 2015 and rely on that condition, the FAMR
8 condition, then it possibly might have been unsound.
9 The reason that I have been advised that is sort of it goes to the heart of the BT appeal here,
10 in that the accusation is that we hadn't actually done enough to sort of pass the legal hurdle
11 of demonstrating risk, and of course that accusation is as part of the VULA margin
12 consultation. In fact I think in your opening remarks two days ago you said we had only
13 devoted 14 pages to that particular question which was insufficient. Of course, when we
14 introduced the FAMR condition as part of the actual -- sorry, the fair and reasonable
15 condition as part of FAMR in 2014, we didn't actually assess that risk, because of course we
16 had taken it outside as part of the separate VULA margin work.

17 Q. I think that is the point I am trying to get at, that it wasn't a foregone conclusion how the
18 process would end in March 2015 --

19 A. Yes.

20 Q. -- as it turned out, because it was a genuine consultation?

21 A. Yes.

22 Q. Or I assume it was. And indeed you did -- and we looked at it, you were in court I think when
23 I was talking to Mr. Bishop a moment ago?

24 A. Yes.

25 Q. We looked at the market change analysis that was done in section 2. So you did look at it like
26 a proper decision?

27 A. Yes.

28 Q. And indeed, as we all know, you notified it to the Commission --

29 A. That's correct.

30 Q. -- as a proper decision. So it wasn't like it was just a sort of sham, you were genuinely doing
31 the exercise?

32 A. Yes.

33 Q. And I think in parallel to that you were investigating the TalkTalk complaint and BT was
34 contacting Ofcom about that, is that correct?

1 A. Yes, in fact it was part of the reason why the VULA margin work under the FAMR was sort
2 of pushed out of sync with the rest of the review. Because at the beginning of 2013 we had
3 the Competition Act complaint from TalkTalk and that ran into 2014, and because the two
4 things were very, very similar and covered the same issues and so on, we sort of had to
5 defer the VULA work to some extent so we didn't start tripping over ourselves.

6 Q. One of things that was done for that was modelling of the BT margin? That was precisely
7 what was being investigated, wasn't it? BT was providing information and providing
8 a model to Ofcom for that purpose, is that right?

9 A. Yes, and we were producing our own models, but yes, we were gathering information.

10 Q. And also, as it were, a sort of dry run for the decision, there were some debates about BT's
11 margin on that modelling for this purpose as well, is that right?

12 A. Sorry, if I ...

13 Q. You will recall that there was a sort of trial run of the condition, I think a first quarter trial run
14 that was done and an indicative assessment was made in that -- in the decision itself, and
15 then the condition itself was imposed, is that right?

16 A. Sorry, I think we did an indicative assessment at the time of the consultation.

17 Q. Yes.

18 A. And then we sort of gave another indicative assessment at the point of statement.

19 Q. Exactly.

20 A. Yes.

21 Q. But I think your lawyers are now saying that actually BT wasn't really constrained by anything
22 from June to March 2015. Is that what you are being told by your lawyers?

23 A. So what I am being told is under the ex ante framework, had we have tried to -- had we have
24 received the complaint of margin squeeze or indeed we had wanted to look at it ourselves,
25 had we have done so and used that fair and reasonable condition, we could have been
26 challenged almost on exactly the grounds we are being challenged now, that we hadn't
27 passed the relevant legal tests to sort of -- to implement it in that way.

28 Q. Yes, I think it is a slightly different point. I think you're saying we would be arguing that the
29 FRAND condition that was in place somehow didn't cover a margin, that is I think what you
30 are --

31 A. Yes.

32 Q. -- saying you have now been told?

33 A. That's correct.

34 Q. I think that is probably a legal question and I will move on from that.

1 Can I now look at paragraphs 13 and 17. It's a bit of a jump, but --

2 A. Of my witness statement?

3 Q. Yes, of your witness statement. We may well go back to the main decision in a moment.

4 A. I will keep it. 13 and ...

5 Q. Look first at 13. There are three coloured numbers.

6 A. Yes.

7 Q. In fact four coloured numbers, all of which are marked as confidential so we won't read them

8 out. But the gist of it says that:

9 "The overwhelming majority of UK consumers take their fixed broadband

10 service from one of the four main providers ..."

11 And then a reference to the smaller fringe providers?

12 A. Correct.

13 Q. And then at 70, towards the end.

14 A. Yes.

15 Q. You say that:

16 "VULA net adds have dropped from about 84 per cent in 2012/13 to

17 approximately 58 per cent in quarter 1, 2015."

18 Then you say:

19 "This is arguably a measure of the effectiveness of Ofcom's regulatory approach

20 to broadband and in particular VULA."

21 In relation to that, can I ask you to look at one or two other figures. First of all,

22 I don't know whether you were present when Mr. Tickel was being cross-examined, but his

23 witness statement is in the same bundle, tab 3.

24 A. Yes.

25 Q. We have looked at the chart at page 21 before.

26 A. Yes.

27 Q. I think on your evidence of what you're being told by your lawyers, the period from June 2014

28 to April 2015 was a period when BT wasn't subject to any margin squeeze control at all as

29 a matter of regulatory obligation. I have been assuming that it was subject to the old regime

30 throughout, and I think in due course my submission will be that that is obviously the case.

31 But anyway, on the assumption that it was either under the old regime or unregulated

32 altogether, you see the trend, I think it is still confidential, but the increase is by a very

33 considerable multiplier, I make it between seven- and eight-fold, would you accept that?

34 A. From the beginning in April --

1 Q. Over the two years from April 2013 to April 2015, so these are the two years before the
2 condition was imposed?

3 A. Yes.

4 Q. Then finally Mr. Matthew's own evidence, which is at tab 12, page 20. Again this is
5 confidential but you will see the trend for both Sky and TalkTalk, both historic and
6 projected. Those look like figures showing rapid development of competition from
7 established standard broadband operators into superfast broadband, would you agree with
8 that?

9 A. It certainly looks like early entry, obviously lagging BT and Virgin, but absolutely, they are
10 beginning to market and enter.

11 Q. If we go back to paragraph 70, I think what you are saying is that the existing approach or
12 indeed, on your evidence, no approach at all, but at least the concerns possibly over
13 TalkTalk and the debate that was going on about margin controls generally, is to be held to
14 be responsible for these improvements. You say:

15 "The measure of the effectiveness of Ofcom's regulatory approach to
16 broadband ..."

17 Is reflected in those figures, is that right?

18 A. Sure. At the time there was a number of things going on. We had the existing FRAND until
19 it was -- until 2014, so for the earlier period. We had whatever happened after 2014; what
20 people believed it was and what it actually was might be a point for legal debate. And
21 obviously in the middle of all of that as well we had the ongoing Competition Act complaint
22 which was ...

23 Q. Yes. So none of this case is really worrying about poor old Virgin whose margin share is
24 projected to go down. They haven't come and complained. But in relation to Sky
25 and TalkTalk, this doesn't look like a situation that is crying out for additional regulation,
26 does it?

27 A. I guess it depends how you look at it. Sky and TalkTalk at some point had to enter this market
28 or sort of think about some strategy of exit as people moved to superfast. They were
29 clearly, as part of the consultation process, pushing for greater clarity, TalkTalk had already
30 submitted the Competition Act investigation which -- these sorts factors they believe,
31 I would assume they would believe it just puts a bigger spotlight on it and the hope in their
32 mind is that it gets more regulatory scrutiny. Whatever the form of the actual ex ante
33 conditions we put out ultimately, there is just more ongoing scrutiny.

34 Q. Yes. I don't think there is anyone in any doubt about the enthusiasm of TalkTalk and Sky for

1 BT to be regulated in this respect. I'm sure they would like it to be more so, and indeed
2 Mr. Heaney made it quite plain he would like a cost control as soon as possible and
3 presumably at as low a level as possible. But that is not really the issue here. I am looking
4 at the objective position which is, under the existing regime, Sky and TalkTalk's figures
5 seem to have gone up probably seven- to eight-fold under the existing regime, you would
6 accept that?

7 A. Yes, I mean ... yes.

8 Q. Can I ask you now about paragraphs 16 and 17 of your statement.

9 A. Yes.

10 Q. You see there at 16 you say:

11 "The competition we see in the retail broadband market today is the result of
12 past regulatory decisions and interventions."

13 Then you give the example of Sky and TalkTalk's LLU growth.

14 A. Yes.

15 Q. And then in 17 you say:

16 "The current competition in the retail broadband market is the result of past
17 regulatory decisions and interventions and Ofcom expects the future
18 competition in this market to be the result of regulatory decisions and
19 interventions that we make today."

20 A. That is right.

21 Q. So I think what you are saying is that Ofcom's regulation has had a major impact on the
22 incentives of companies, that is what you are saying?

23 A. Yes.

24 Q. Both in the past and you expect it to do so in the future?

25 A. We certainly hope that is the case if we get it right.

26 Q. In terms of incentives, price regulation is one of the tools that Ofcom has used most
27 consistently over the past decade to affect the incentives of firms, that is right?

28 A. Yes, of various different forms, price regulation. They are obviously -- they are coupled up
29 with access regulation and the two sort of go hand-in-hand.

30 Q. And the impact on incentives will be greatest on the firm subject to the greatest regulation,
31 and that is true. If you are imposing regulation, the biggest incentive effects will be on the
32 most regulated firm, that is correct, isn't it?

33 A. Sorry, can I understand the question?

34 Q. If you introduce a complicated system of regulation --

1 A. Yes.

2 Q. -- and it bears on one firm?

3 A. Yes.

4 Q. That is the firm whose incentives are going to be affected, isn't it?

5 A. I guess everyone's incentives are affected to some extent. So this is if we put regulation on

6 a firm, are their incentives affected?

7 Q. Yes.

8 A. Almost certainly. But equally, other firms that are thinking of entering the market, their

9 incentives would hopefully be affected as well.

10 Q. Yes. Supposing you put a price cap on a firm or, to take another example totally at random,

11 a wholesale must-offer regulation on a firm, that would affect the incentives of that firm. It

12 will have other incentives on the beneficiaries of regulation but it will certainly be targeted

13 at the incentives of that firm, won't it?

14 A. It's absolutely targeted at that firm and it will affect their incentives, yes.

15 Q. Exactly. So would you agree with me that BT is the firm that has been most regulated by

16 Ofcom over the past ten years?

17 A. In the space of the broadband market, yes. I think I even say that in my witness statement at

18 some point.

19 Q. Can we look at paragraph 19B I think it is. You say at the bottom:

20 "By providing pricing flexibility, Ofcom seeks to promote investment and

21 innovation in broadband services."

22 A. Yes.

23 Q. We can turn it up if you like, but I am sure you can remember that in the FAMR decision you

24 took account of those incentive effects in deciding not to regulate BT's VULA prices, is that

25 right? You remember that?

26 A. That is correct.

27 Q. We have looked at the discussion. I think you have been in court and we have looked at the

28 discussion. I think you looked at the competitiveness of the market, the risk of regulatory

29 failure and the effect on investment incentives, those were the three sort of headline points.

30 A. Yes.

31 Q. If you had ignored historic regulation of the UK market, you wouldn't have an accurate picture

32 of the incentives of undertakings on that market, would you?

33 A. Sorry?

34 Q. If you just ignored your role, you wouldn't have an accurate picture of the incentives on the

1 UK broadband or telecoms market, would you?

2 A. Okay, yes, I think you are saying if we hadn't intervened in the past would people have had
3 different incentives?

4 Q. No, what I am imagining is you look at what has happened, Sky and TalkTalk have grown
5 enormously in LLU, for example, we will come to that in a moment.

6 A. Yes.

7 Q. And you had ignored Ofcom's role.

8 A. Yes.

9 Q. That wouldn't be an accurate picture of BT's incentives, would it?

10 A. I'm not quite sure I understand the question. Sorry.

11 Q. You say this amazing thing has happened?

12 A. Yes.

13 Q. Sky and TalkTalk have moved from almost nothing to 93 per cent coverage with LLU?

14 A. Yes.

15 Q. You say why has that happened? And you had ignored Ofcom's role completely. That
16 wouldn't be an accurate account, it would be a misleading account of what had happened?

17 A. Yes.

18 Q. In fact that is the very point you are making at paragraph 70, that you take credit for what has
19 happened on the market, both standard and superfast broadband, isn't it?

20 A. So the point at paragraph 70, which is particularly about superfast broadband, and it's based on
21 I think it was Mr. Murray's evidence that now -- and it is the point in Mr. Tickel's witness
22 statement as well, that actually over the last couple of years Sky and TalkTalk have started
23 using these products. I think the point I was making at 70 is, well, yes, and our regulation
24 has required it and we have -- we have sort of had fair and reasonable and we have been
25 investigating margins ex ante -- sorry, ex post, and yes, and probably it is the combination
26 of those various regulatory interventions which has sort of allowed the providers to do this.

27 Q. Thank you. Can we just -- it's really just a matter of clarification. At pages 8 and 9,
28 paragraph 25, you draw three distinctions between three types of product, or three types of
29 access, depending on how far you go into the BT network, if I can put it in that way. I think
30 it might just help if you explained those three in your own words.

31 A. Okay. So this is -- so these are meant to be generic and then I tie in particular sort of access
32 remedies and I try and align them with one of them later on in my witness statement. But
33 effectively what this is sort of saying is you can either have what would be referred to as
34 quite upstream remedies, and that would sort of be at the A, wholesale access to existing

1 assets. And if other operators were to use those types of wholesale access, they would
2 probably have to do the most work themselves, undertake the most risk and so on. But you
3 of course can go for sort of remedies which are further downstream, and going from B to C
4 would be moving -- A, B, C is moving in that sort of downstream direction. And as you go
5 more downstream, the work that the access seeker has to do is less and therefore the work
6 that BT does is more. But there's various trade-offs here as well, so as you go more
7 downstream to products like C, the scope for access seekers to actually control their
8 services and the innovation potential that they get over those services is less, so it's
9 a trade-off between --

10 Q. I think C is the sort of Tesco case where they basically take a BT service and label it with
11 Tesco?

12 A. It is more that end. For Tesco there might even be a D camp but, yes, it's more that end.

13 Q. And LLU I think you are classifying as an A case?

14 A. Yes.

15 Q. Where the CP has done something quite substantial themselves, they have invested at the level
16 of the exchange, and that is an A case whereas I think VULA you classify as a B case
17 because BT is doing most of the work, they are producing the fibre to the cabinet, and
18 TalkTalk and Sky, or whoever, are basically taking it to that degree as a prepacked service
19 to the cabinet, that is the distinction you are drawing?

20 A. Yes, that is right. So VULA I have sort of said more aligns to B. BT does a lot of the work,
21 BT has to make the investment in upgrading the network. The other provider then uses it,
22 but it is not as easy to use as C because they still have to do a fair amount themselves in
23 terms of building and running their network from those local access nodes. So it's still
24 significant but clearly not as significant as building themselves.

25 Q. There is no reason why CPs couldn't move up the supply chain in one way or another and
26 invest a bit further up if they wanted to?

27 A. I guess in theory, absolutely, people could, and in fact I think they have even been mentioned
28 so far in these proceedings. So in theory, people like Sky and TalkTalk could use existing
29 assets, and I think sub loop unbundling had been mentioned, and sub loop unbundling
30 would allow them to build their own fibre to the cabinet network. There is always
31 a question about the economic viability of doing that because of the economies of scale that
32 you get when you get to these very small cabinets: are there enough customers to split
33 between multiple providers such that all the providers achieve economies of scale?

34 One of the reasons that we had identified an active product, which later became VULA, as

1 being our focus for competition with superfast networks, which we did in 2009 in our
2 superfast strategy, was based on the evidence we had at the time, which I think still stands
3 at the moment, is the economics to support multiple providers at those higher levels or
4 deeper in the network just do not look attractive, so yes.

5 Q. I think there is no difference between BT and Ofcom on this, and Mr. Tickel I think indicated
6 that at the moment that is why we have accepted SMP in this part of the market. It's as it
7 were -- the transition from B to A is at a relatively early stage here and who knows whether
8 it will happen.

9 A. Yes, whether we get that transition or whether we stay on B for superfast is that open
10 question.

11 Q. Can we now go back in time, if we may. I'm not proposing to go into the detail of all the
12 regulatory changes that you describe very helpfully in your witness statement, but there is
13 obviously one critical one which happened about ten years ago which you describe in
14 paragraph 33. You say:

15 "In 2005, competition in the retail broadband market was still nascent and
16 Ofcom was keen to nurture its ongoing development."

17 A. Yes.

18 Q. So it's not exactly the same but it's at a stage when there was a potential move from B to A, or
19 something approximating B to A, at the level of LLU. There was a paper which Ofcom put
20 out which in fact I think has not crept into the bundles but it is in your witness statement.
21 You should have some defence bundles that you refer to, it's DF2/13.

22 A. Tab 13?

23 Q. Yes. It must be one of the shortest documents Ofcom has ever published but no worse for
24 that.

25 A. I would love them all to be as short as this.

26 Q. It's a statement which is called "Broadband Regulation", again it's straight to the point. It was
27 issued on 30th June 2005 which, I don't know if you remember, we will see in a moment
28 was the same day as the consultation document on the undertakings. Do you recall that?

29 A. I do recall it.

30 Q. If we turn in you find at paragraph 7, which I think is the point you are making, it is going
31 back in time because we find there that:

32 "LLU remains relatively embryonic today with only about 70,000 unbundled
33 loops to date, representing about 1 per cent of the broadband market. It has
34 been suggested that further improvements and clarity are needed before LLU is

1 a fully viable platform upon which LLU operators can compete effectively."
2 Can you put your mind back to those naive days?
3 A. The numbers look quite amusing but, yes, I can vaguely remember.
4 Q. It's not a parallel, but you will recall there has been some evidence about the position in York
5 and Sky and TalkTalk and how this is all fairyland. But it must have seemed something like
6 that in 2005?
7 A. Yes, I think probably there was quite a big difference between LLU and building your own
8 network, but, yes.
9 Q. Then the reason -- but you will recall that -- I don't know if you have seen Mr. Blumberg's
10 evidence but I am sure you know as a matter of fact that Sky has expanded I think to almost
11 100 per cent, it's over 90 per cent anyway --
12 A. In terms of its LLU, yes. I think the number is somewhere -- almost in the middle between 90
13 and 100, probably about 93/94.
14 Q. If you turn over the page, paragraphs 15 and 16, you will see that the -- do you want to read
15 those two paragraphs?
16 A. 15 and 16, sorry?
17 Q. 15 and 16.
18 A. Yes, one second. (Pause) Okay.
19 Q. Do you remember what happened? In 15 they are referring to some commitments, do you
20 remember, BT made some commitments, I think they are described as paragraphs 9 to 11,
21 about pricing and what would happen at various stages?
22 A. That is right. It was to do with their wholesale broadband prices not going down, in fact,
23 I think was the commitment, which created a sort of a margin between LLU and those
24 prices, those were the commitments.
25 Q. Ofcom decided that, given the commitments, ex ante margin regulation wasn't needed, do you
26 remember that?
27 A. Yes. Yes, I mean effectively the commitments would sort of have the same -- would provide
28 the same sort of function.
29 Q. Yes. Then at 16 there is reference to what are in fact the undertakings and the creation of
30 what became Openreach, do you recall that?
31 A. That is correct.
32 Q. And then Ofcom says this:
33 "This levelling of the playing field should further address the medium term
34 concerns of LLU operators."

1 A. Sure.

2 Q. So they were saying there are two things in place. There are the commitments and there is this
3 creation of Openreach and those will address these concerns about margin, is that what they
4 are saying there?

5 A. I don't think they are both getting at margin necessarily. The first one in 15 is getting at
6 margin, because that was the commitments to protect the margin. I guess the undertakings
7 at 16 address other factors like product equivalence and so on. So now they can get access
8 on an equivalent basis as well.

9 Q. Right. But it's said to be in addition to BT's commitments and further addressing their
10 concerns, so it sounds like it's in the same general area?

11 A. Yes, I mean it all helps with their case. So they wanted access on an equivalent basis and the
12 undertakings sort of delivered that, and they wanted assurance about the margin and
13 commitments gave them that. So they all act to fill in various pieces.

14 Q. Yes, although I think the concern is stated at the start of 15 and then there are two responses,
15 that is what this says, isn't it?

16 A. Sorry, so 15 is about margin.

17 Q. Yes.

18 A. About margin protection, and 16 was the undertakings, it gets us to what the undertakings do
19 which is about equivalence of supply and so on.

20 Q. Yes, but the two are both addressing the first sentence of 15, aren't they?

21 A. I'm not sure I make that connection.

22 Q. Okay. If we look at the other exciting event that happened that same day, that appears
23 in -- I think you have bundle IV somewhere.

24 A. DF4. Yes.

25 Q. These are the hearing bundles. Volume IV?

26 A. Yes.

27 Q. And it's tab 2. Just for completeness, we could peep forward to tab 3, which was issued on
28 22nd September, and that was Ofcom's actual statement on the undertakings. And if you
29 turn into that just briefly, we don't need to go to the small letters, but from 48 onwards,
30 which what we have got, is a large number of comments and detailed responses from
31 Ofcom.

32 A. Yes.

33 Q. But the gist -- certainly that is what we have got, the bulk of what we have got of Ofcom's
34 reasoning in is the consultation document which is in tab 2 which, as you see, was issued on

1 the same day as the broadband regulation statement.

2 A. Yes, so tab 2 is the consultation issued in June, and tab 3 is the statement that came out
3 in September.

4 Q. Yes. I may have -- it may actually be a rather more substantial I am giving it credit for but
5 that is what we have here.

6 A. I think it had the first copy of the undertakings attached to this document as well at the time.

7 Q. If we look again at the consultation document which Mr. Holmes put to Mr. Petter yesterday,
8 I think you were here. First of all, we were looking at 1.4 which was put to Mr. Petter on
9 the basis of essentially discrimination. And then 1.9 summarises Ofcom's general position.
10 You see that:

11 "Ofcom considers the package of undertakings offered by BT is appropriate to
12 address the difficulties which it has identified and offers as comprehensive
13 a solution as is reasonable and practical."

14 Do you remember that?

15 A. Yes.

16 Q. And then when you go into the -- you have a summary of the undertakings which essentially
17 have two main limbs, EOI and the creation of Openreach, the equivalence of inputs and
18 access services division?

19 A. Yes.

20 Q. And then there were a number of other perhaps slightly less sort of headline points, although
21 no doubt important, and the creation of the EAB, the Equality of Access Board, is I am sure
22 also an important factor?

23 A. Yes.

24 Q. Then when you look at section 4, there is a large number of features identified over the
25 following six pages, 9 to 15.

26 A. Okay.

27 Q. And in particular at 4.16 to 4.18 there is reluctance to supply a wholesale product.

28 A. Okay.

29 Q. And then at 4.24 there is "Response to supply of upstream products deters investment by
30 competitors", and then there is the first bullet point headed "Downstream Product
31 Improvements", and then a reference to a particular issue in relation to data stream and IP
32 stream, and then issue about pricing which was said possibly not to amount to a margin
33 squeeze but to raising uncertainty and further price competition which might deter
34 investment, do you see that?

1 A. Do you want me to read it?

2 Q. Certainly. (Pause)

3 A. Okay.

4 Q. Then the response and Ofcom's analysis of the appropriateness of the proposed undertakings is

5 at section 5, isn't it?

6 A. Okay. Yes.

7 Q. It looks at various points: the seriousness, alternative means, Competition Act, Comms Act,

8 appropriateness of the undertakings and the comprehensiveness of the undertakings, those

9 four bullet points at 5.1, do you see that?

10 A. Yes.

11 Q. And then 5.5 through to 5.15 looks at first of all the Competition Act and then ex ante

12 regulation.

13 A. Okay.

14 Q. And then at 5.15, do you want to read that or I could read it out:

15 "The proposed undertakings would constitute a more comprehensive solution to

16 the problem and could be achieved by a series of interventions under the

17 Communications Act. A product by product approach allows discrimination

18 effectively to move from product to product within a chain of supply.

19 For example, competition in upstream market may be restricted if BT improves

20 a downstream product without altering the margin between the two products.

21 Alternatively, changes in the margin between an upstream and downstream

22 product affect competitors' ability to compete in each of these markets. The

23 resulting uncertainty has the effect of reducing investment in these markets by

24 operators competing with BT."

25 So quite a familiar selection of concerns, would you agree?

26 A. Yes.

27 Q. Then if you go on to 5.16 and 5.17, you see the purpose of the undertakings was to address

28 these concerns, and then at 5.17 there is a finding about their suitability for that purpose.

29 A. Okay.

30 Q. So in particular they say that:

31 "The undertakings constrain BT's ability and remove the incentives of its

32 component divisions to engage in the types of conduct identified which have the

33 effect of restricting competition."

34 So that obviously includes what we have just read there at 5.15? That must be what it says,

1 isn't it?

2 A. I guess that is how it has been constructed.

3 Q. Yes. Then in relation to Openreach specifically, one finds the description at 5.27 and 5.28.
4 5.26 is simply describing what we all know and love as Openreach and then 5.27 and 5.28
5 draws some implications. First of all, 5.27 is a selection of prohibitions, but then
6 particularly 5.28 and then 5.29.

7 A. Okay.

8 Q. So you see in particular the second sentence of 5.28:

9 "The undertakings include provisions regarding the incentives-based
10 remuneration for ASD senior management which would be aligned with the
11 performance of ASD only and provisions prevent undue influence and
12 inappropriate information flows between ASD and the rest of BT Group. The
13 purpose of these provisions to address the competition concerns arising from the
14 combination of BT's enduring upstream market power and its vertical
15 integration. As set out in section 4 and in more detail in annex F, it is these
16 features that give rise to both the ability and the incentive to provide inferior
17 upstream products."

18 Do you see that?

19 A. Yes.

20 Q. So the core purpose of creating Openreach was to alter the incentives of BT to engage in
21 practices of this kind, including those at 5.15, that is correct, isn't it?

22 A. Yes, okay, I can see where you are going, but, yes, it essentially was to alter their incentives.

23 Q. Again there are further discussions of the organisational structure at 5.34 and 5.35, and the
24 conclusion at 5.35 is that the restructuring says:

25 "... the incentives of the senior management of ASD, [so Openreach] would be
26 aligned with the performance of ASD only."

27 So again it's intended to affect the incentives of Openreach. You would accept that?

28 A. Yes.

29 Q. Can we now look at paragraphs 40 and 43 of your statement. In the middle of paragraph 40
30 you refer to the 2010 obligation.

31 A. Yes.

32 Q. It says:

33 "In particular, Ofcom imposed a requirement on BT to provide access to VULA
34 on fair and reasonable terms, conditions and charges, but didn't regulate the

1 absolute level of the VULA charge."
2 A. Yes.
3 Q. So that is the 2010 position and then you refer to some high level principles being set out?
4 A. Yes.
5 Q. And you give the classification of VULA at the bottom in your paragraph 25 terms. Then you
6 go on to refer to the recommendation that Mr. Holmes took the Tribunal to on the first day
7 and then you describe your approach in the FAMR statement and in the final statement as
8 being the same as in the 2010 review and you criticise Mr. Tickel at the end. You say:
9 "Mr. Tickel is wrong to suggest, as he does at paragraph 74 of his evidence, that
10 the design and application of the VULA margin control is a significant
11 departure from the previous approach Ofcom has adopted."
12 You see that?
13 A. Yes.
14 Q. Can we look at Mr. Tickel's evidence and see what you do or don't agree with about it. That is
15 at tab 3.
16 A. Yes.
17 Q. Page 30.
18 A. Okay.
19 Q. At 75 through to in fact 80, Mr. Tickel makes the point which I think you say is wrong, but he
20 does it fairly carefully. He does it by reference to condition FAA 11.2, do you see that at
21 76?
22 I think we do actually have this review somewhere in the bundles but I think only in
23 the electronic version as far as the Tribunal is concerned. So if I may, I will rely on
24 paragraph 77 where Mr. Tickel sets out some extracts from the 2010 market review.
25 A. Okay.
26 Q. I don't know how familiar you are with this material.
27 A. Reasonably familiar.
28 Q. Do you want to read through 8.130 to 8.135 in the box.
29 A. I will have a quick read. (Pause) Okay.
30 Q. Then at 78, Mr. Tickel points out four main points made in the 2010 document. First of all,
31 and I think he is looking at the bold passage in 8.132, he says it is a LRIC approach, and
32 that to some extent touches on some of the issues that I think the Tribunal was debating
33 with Mr. Bishop, although it was more in terms of long- and short-run, but in some ways it
34 raises similar issues. Here the position was taken as a long-run incremental cost rather than

1 a LRIC plus approach and that is obviously one issue in the design debate as to both the
2 nature and extent of the plus and that is a change.

3 A. Okay, what would I say to that? We never had to test these -- the 2010 FRAND condition,
4 what we did in 2010 is in some respects we were quite light, we gave a very short piece of
5 guidance which really didn't have a lot of detail in it. Had we have had to use this, would
6 we have really not put a plus component into LRIC? I'm not sure we would have done.
7 This was sort of the point -- this was some very, very high level guidance which we sort of
8 felt was appropriate at the stage of the market.

9 Q. Yes.

10 A. And what we have done now is just put the --

11 Q. I see that -- I don't want to interrupt, but I can see the point you are making. And likewise you
12 would probably say the REO/EEO debate is also somewhat of a grey area that has been
13 debated by competition lawyers and no doubt regulators for many years?

14 A. Absolutely. Most people will generally sort of assume an REO test, if you like, favours the
15 entrant and not the incumbent and an EEO test is more about the incumbent. That is what
16 most people would assume as the starting point. And yes, we used the REO because I think
17 at the time we assumed we might have to make some adjustments for some advantage that
18 BT might have. But again we hadn't specified it, it was just ... yes.

19 Q. Can I put three slightly more concrete points to you, I think again it is picked out by the bold
20 analysis. There is reference to:

21 "Any such analysis [so analysis of the margins] would depend on the specific
22 circumstances surrounding any concerns."

23 And then at the end of 8.132 there is reference to an initial analysis in the first sentence, and
24 then in the last sentence:

25 "Depending on the outcome of this initial analysis, we may conduct further
26 work including requesting evidence from BT."

27 And then at 8.133 you specify that there may be over a particular time period.

28 A. Yes.

29 Q. Would you accept, first of all, that there was flexibility over the relevant time period
30 depending on the circumstances, that was part of what Ofcom was envisaging then?

31 A. I think we hadn't specified it, so I guess what time period we would have chosen we would
32 have had to have sort of worked out after the event.

33 Q. It would depend on the nature of the market and the nature of market developments, how fast
34 things were moving, the nature of competition, types of cost you were talking about, that

1 sort of issue?

2 A. Yes.

3 Q. And in effect because it is -- I say "in effect", in substance because it is a two-stage process,
4 an initial analysis and then further work, in substance it is a sort of an effects approach, it is
5 a sort of a look at the numbers and then if there is a problem you look into the detail of the
6 effects on the market, that was what was being suggested here, wasn't it?

7 A. I don't think that was what we were suggesting, actually. I think it was more a suggestion that
8 we would do an initial look and, depending on where the numbers lie, then if it was -- if it
9 was a clear pass, there wasn't a margin problem, then we might not bother to go any further.
10 If it was sort of borderline, that is when actually we would want to drill in a bit deeper to
11 sort of get a better handle on the numbers.

12 Q. Yes, it was a two-stage process and presumably the first -- what they call a quick and dirty
13 look, would focus on the numbers, would it not?

14 A. It would focus on the first chunk of the numbers, yes. So rather than boiling the ocean, you
15 would try and have a quick and dirty look and, if that clearly put you into a sort of a safe
16 place, you might not bother to sort of drill down and interrogate those numbers any further.

17 Q. Yes. Then looking a little bit more concretely at the type of issues that will come up in due
18 course in the design debate, there were no prescriptive rules in relation to fixed costs and
19 how they should be treated?

20 A. No, it was very light on detail.

21 Q. And no prescriptive rules in relation to the treatment of bundles?

22 A. No, again it was -- again, light on detail.

23 Q. Whereas when we look at what we've got now, I think you have effectively answered it
24 already, there were some pretty major changes.

25 A. Well, let's -- I think that is worth probably drilling into a bit more. So I guess the way I see
26 this evolving is, 2010, we sort of said, you know what, you shouldn't be margin squeezing
27 and, if we were to look at it, this is sort of roughly some things we would look at, but really
28 not much detail.

29 So, come 2014/2015, I think where we are is saying you shouldn't be margin squeezing, but
30 now the question is: how much detail do I provide? In some respects what we have sort of
31 done in the margin rule is we have sort of said to ourselves: if we were to do a margin test
32 on you today, what would we do? How would we handle all of these complexities? And
33 we've sort of said: this is how we will handle your current business case. This is the
34 detailed approach that we would adopt, if your products are structured in this way.

1 So what we have done is we have -- if you like, we have provided more certainty to BT and
2 other players in the market about exactly what we would do, should we actually have to
3 investigate.

4 Q. But if I can tie it up, in the 2010 approach there was no prescription on timing. In the new
5 approach, it's a monthly pass/fail test. Yes?

6 A. Well, yes, that is how we have constructed it. Yes.

7 Q. In the 2010 approach, it is a two-stage quick look intensive, whereas in 2014/15 it's a pass/fail
8 test. Yes?

9 A. Yes.

10 Q. In 2010 there are no prescriptive rules on how fixed costs are to be treated. In 2015, highly
11 prescriptive rules, particularly in relation to retail costs?

12 A. Sure. But we come back to this point again. So in 2010 it is not that we wouldn't have treated
13 things this way had we have needed to, had we have had to do an investigation, it's just that
14 we hadn't told anybody upfront exactly what we would do. We hadn't thought of it. We
15 had only provided high level, yes.

16 Q. The point I am putting to you is, when you say that Mr. Tickel is wrong at paragraph 74 when
17 he says that this is a significant departure from the previous approach, would you accept
18 that it was in fact a very significant departure from the previous approach?

19 A. I have put in my witness statement that I don't accept it and I sort of don't. The reason I don't
20 accept it is because our market finding of SMP is the same, our approach to giving pricing
21 flexibility is the same, our approach that is saying BT is not allowed to margin squeeze is
22 the same. The difference is that, come 2015 compared to 2010, we have provided more
23 explicit guidance on exactly how we would come about the test, which at one level
24 will -- should allow BT -- I know they don't like it and that is subject to the other part of the
25 appeal, but at one level that should just give BT more reassurance about exactly how to
26 comply.

27 Q. That is a further difference which I haven't put to you, which I should put to you: this isn't
28 actually guidance, it is actually rules?

29 A. Sure.

30 Q. Which is another significant departure. Would you accept?

31 A. Sure. On the face that it's a clear rule set out, that I think is the big difference --

32 Q. That is a significant departure, don't you think? If you break a rule, you get fined, potentially?

33 A. Whether it's significant or not, I guess ... anyone could sort of judge whether it's significant or
34 not. In my mind this is just an extension of what we did in 2010, which is to provide more

1 guidance rather than just the high level principles.

2 Q. Yes. Can I put one more point to you, which is: both article 13 of the Access Directive and
3 the Act, and indeed the case law of the Court of Justice on margin squeeze, draws
4 a distinction between an arithmetical margin squeeze, a failure on the numbers, and the
5 effects on competition, and that distinction is in this guidance, in the two stages, if you look
6 at the numbers, if you look at the effects. Whereas the new test is a unitary test, and that is
7 a significant departure too, isn't it?

8 A. As I say, I'm not sure that is exactly how we would have run the 2010 test, had we had to do it.
9 We would have -- we may well have. We didn't have to ever sort of test it, but we may well
10 have just done it on the numbers. That is sort of --

11 Q. That is a convenient place to break. But you will recall the Wholesale Calls case and that is
12 exactly what you did, and then you admitted you had to do effects. So I think that is
13 probably a good place to break.

14 A. But, sorry, this is an ex ante intervention for promoting things into the future, so ...

15 MR. THOMPSON: I think that debate is probably drawing to a close, so that would be a good
16 place to break.

17 THE CHAIRMAN: 2 o'clock.

18 (1.05 pm)

(The luncheon adjournment)

20 (2.00 pm)

21 MR. THOMPSON: I can definitely say good afternoon now, Mr. Clarkson.

22 A. Good afternoon.

23 Q. Just really for the transcript because I went a bit quickly at the end, and I think I referred to it
24 earlier, you will recall I was discussing at one point the decision in relation to the TalkTalk
25 complaint, and you will recall that was decided on 21st October 2014, so in the middle of
26 all this debate about, or the consultation for this.

27 Just for the transcript and the Tribunal -- I don't think we need turn it up, I am sure you
28 remember it -- it's at tab 60 of volume V of the authorities. And the other case I mentioned
29 briefly where I think some of the modelling issues between Ofcom and BT were referred to
30 and developed was the Wholesale Calls case which is at the fifth volume of authorities,
31 tab 59, and that was a decision of June 2013, do you remember that? I don't know if you
32 were involved.

33 A. I am not so familiar with the Wholesale Calls one.

34 Q. That was a competition case as well.

1 A. Okay.

2 Q. Brought by Ofcom on the complaint of I think Gamma and THUS, and after a fairly lengthy
3 investigation, I think it was some three years, it was closed in June 2013 essentially because
4 of lack of effects.

5 A. I think the point I made just as we were breaking was drawing the distinction between
6 obviously the ex post and the ex ante regulatory tools that we have, whereas those two other
7 cases were ex post, they are after the event looking back at historic abuse.

8 Q. Yes.

9 A. Whereas the rules we do under the ex ante framework are about putting remedies in place to
10 promote things like competition in the future on a forward-looking period.

11 Q. Yes, I understand that distinction and I know it appears in the legislation, I always thought it
12 was a rather uncertain one myself, because if anyone ever were to actually pursue any of
13 these cases, you would have to analyse the matter on an effectively ex post basis, and
14 somebody one day started article 102. So the line between ex ante and ex post is not
15 entirely clear but I understand the point that is made.

16 A. I think we probably see it slightly more stark. When we introduce a charge control on
17 a forward-looking basis we are obviously setting out rules about pricing for the future and
18 that is quite common under the ex ante regime.

19 Q. Yes, can we go back to where we were in the change that was made by this condition as
20 against the old regime. We have debated some issues which obviously merge into the
21 design questions which are going into the CMA process but I think you will agree with me
22 that there was a significant change in the enforcement risk, if I can put it that way, of
23 moving to a condition to be enforceable on a monthly basis as against the FRAND
24 condition which had no clear periodic assessment involved, that was a big change?

25 A. Yes, the change obviously to provide more certainty.

26 Q. It provided more certainty but it also provided more risk, and you will appreciate that the risks
27 of disputes and penalties for infringement are substantial in relation to a company such as
28 BT. You would accept that, would you not?

29 A. Sure, but I think the difference we are talking here is in 2010 there was always a risk that BT
30 could breach the condition but they didn't have clear guidance about what might or might
31 not be a breach before the event --

32 Q. I understand that.

33 A. -- whereas now --

34 Q. I think you were present when Mr. Tickel gave evidence about that and the trade-off between

1 certainty and flexibility?

2 A. Sure.

3 Q. And the fact that there is a risk of false positives of something that is not anti-competitive at
4 all being treated as a serious infringement which is the price of making something rigid and
5 certain, you see that point?

6 A. Sure, yes. They are the sort of trade-offs in lots of directions within setting these types of
7 conditions, providing ex ante certainty versus flexibility, sure.

8 Q. Yes. But you can understand why BT might be concerned about that change and regard it as
9 significant?

10 A. I can understand why BT -- but I do sort of think it cuts two ways for BT. On the one hand
11 they do actually have more certainty so they know, if you like, where the line is upfront.

12 Q. Yes.

13 A. So the risk of crossing it should be lower.

14 Q. I think we understand where we are coming from on that issue.
15 Can I move on to paragraph 50 of your statement. You are referring to an argument or
16 a point that is made by Mr. Tickel and you draw a distinction between retail prices and
17 wholesale prices and you say there is no direct constraint on the wholesale price of VULA.
18 Do you see that?

19 A. Yes.

20 Q. You use the word "direct", but I think Ofcom is familiar with indirect constraints?

21 A. Yes.

22 Q. Is it not? And indeed that was the basis for the market definition in this case, was it not? That
23 retail competition imposes an indirect constraint effectively on wholesale and that is why
24 the market definition was defined as it was, is that broadly speaking --

25 A. Broadly, yes. We start looking at the retail level and then go upstream.

26 Q. Perhaps it's a bit unfair, perhaps we should go back to what Mr. Tickel actually said. That's at
27 paragraphs 26 to 29 of his statement.

28 A. Yes.

29 Q. He is saying there are constraints on BT's GEA price and you see that at 28.

30 A. Okay.

31 Q. And then at 29, first of all the first point is the charge control on copper access, so that is
32 standard broadband, and then at 29 he says:
33 "Ofcom's overall approach therefore reflects a judgment that the risk of BT
34 setting excessive prices for GEA absent a charge control is balanced by the

1 effectiveness of constraints from the availability of SBB services where
2 competition is underpinned by regulation of copper access service and for
3 Virgin Media."

4 Then he goes on:

5 "The same logic concludes that BT faces constraints in pricing GEA at excess
6 levels ... suggests that BT faces constraints in pricing GEA at levels that are not
7 commercially viable for CPs."

8 I think it is that point that you say he has misunderstood you because of the distinction
9 between retail and wholesale. But do you not think it is possible that Mr. Tickel is making
10 this distinction that effectively is in the market definition as well, the definition between
11 retail and wholesale and indirect and direct constraints, that is what he is talking about, is it
12 not?

13 A. I don't know. When I read this, and I think in my witness statement I did say it is a bit unclear
14 to me, but I was sort of reading this that there is this constraint on GEA, GEA being the
15 wholesale product, and the point that I was sort of making is, well, that is not quite the way
16 our analysis worked. We sort of said at the retail level, so the products that consumers buy
17 either from Virgin Media or standard broadband products, it has been our view that there is
18 a constraint between the standard broadband and the superfast broadband. That doesn't
19 mean you can't get a premium for the superfast but there is some sort of limitation on how
20 big that premium might be.

21 That is where the constraint applied, and what I was sort of trying to highlight is of course
22 at the wholesale level we have explicitly given this pricing flexibility so BT could set, you
23 know, in theory, any price it likes, and the constraint as we see it in regulation actually
24 comes from the margin squeeze, because that then sets what the minimum gap between the
25 two, the retail price and the wholesale price, can be.

26 Q. Yes, I understand it is a different type of restriction from the charge control, but the question
27 about whether there is a constraint from standard broadband on superfast broadband
28 operates at both the retail and the wholesale for the reasons that we have discussed.
29 It may help you if we look at the discussion in the FAMR document which I think is still, as
30 it were, good law as far as this case goes because of the no market change assessment that
31 was made in this case. One finds that at tab 8 of bundle III/II and it's page 381. Then the
32 first bullet point at 12.135, you say -- I think that is the point you are making:

33 "The retail price of standard broadband would act as a constraint on the retail
34 prices that can be charged for retail products that use VULA."

1 A. Yes, that's correct.

2 Q. But then it goes a little bit further. If you look at the bottom, 12.136, they are looking at
3 I think the wholesale price and in particular the passage that starts:
4 "However, the risk of BT setting VULA prices that are higher than the
5 underlying costs is balanced against the drawbacks of regulation (which we
6 discuss in further detail below). In addition, we consider that any adverse
7 effects from VULA pricing are likely to be greater where the VULA price is
8 substantially above the underlying costs, and we consider a difference of such
9 magnitude to be unlikely during the period covered by this review given the
10 constraints on retail superfast broadband pricing set out above."
11 So Ofcom's finding is that they don't think that BT will price substantially above costs
12 because of the indirect constraint from retail pricing, that is right, isn't it?

13 A. Sure, but that is assuming there is sufficient margin.

14 Q. No, I think that is just talking about VULA pricing, is it not?

15 A. I am trying to work out exactly what it's saying. But if the constraint is applying at the retail
16 level, then what would be the link to the wholesale VULA price if it is not the VULA
17 margin?

18 Q. But the concern is excessive pricing of VULA, is it not?

19 A. Sure --

20 Q. They are saying they are not going to price it significantly above because of the constraints
21 from retail.

22 A. Sure. So there is a retail constraint between superfast products based on VULA, the Virgin
23 network and standard broadband. Then we have the wholesale VULA product, and absent
24 worrying about the margin between the retail and the wholesale prices, what would be the
25 constraint at the wholesale level?

26 I'm sort of trying to read this and work out exactly what was meant. It's obviously sort of
27 deeply buried in the document. When we were building this and doing this analysis, our
28 view was, yes, you can use the word "VULA" generically, there is a constraint on VULA,
29 but the constraint applies at the retail level, but then is reflected to the wholesale level
30 through the margin.

31 Q. Yes. I certainly -- obviously we are in this case arguing on relatively narrow ground because,
32 as I think we have already discussed, there was the FRAND condition in place from 2010.

33 A. Yes.

34 Q. And indeed continued to be in place in 2014.

1 A. Sure.

2 Q. So there was that degree of constraint directly on the VULA price or on the margin depending
3 on exactly what the FRAND condition meant.

4 A. Yes, so provided we have got some route from retail to wholesale through a margin then we've
5 got a constraint at the wholesale level.

6 Q. Yes, I understand what you're saying.

7 A. Yes.

8 Q. Then I think a similar point is made at 12.153 looking forwards, which is that they would only
9 think about introducing a future regulation directly, effectively if the two markets or
10 submarkets split away so that there was no longer a constraint from standard broadband.
11 Do you recall that?

12 A. Sure, so in terms of, if you like, deciding when you might want to move away from pricing
13 flexibility I guess there are a lot of factors. One could be that there is no constraint from the
14 other products. Other ones could just be, you know, the sort of perceived risk of the
15 original investment. A big part of the pricing flexibility, as we have said, was to try and
16 promote that innovation and investment.

17 Q. Yes. We actually looked at the three points you took into account which was the constraints
18 from Virgin and standard broadband, the risk of getting it wrong --

19 A. Yes.

20 Q. -- and the effect on investment incentives?

21 A. Yes.

22 Q. Those things could change over time?

23 A. Sure.

24 Q. But we are looking at the constraint from standard broadband at the moment.

25 A. Yes.

26 Q. And that would be analysis. Can we then move on to 51, which is just below, where you talk
27 about:

28 "If BT were to set VULA prices at excessive levels then providers who use BT's
29 copper access services, such as LLU to provide SBB, would not be able to
30 up-sell their customers to SFBB and, accordingly, their customers would remain
31 on SBB. Indeed this is the very situation that the VULA margin regulation is
32 seeking to prevent."

33 It's a point that I think was discussed to some extent with Mr. Bishop, but would you accept
34 that Sky and TalkTalk would have an incentive to stay with standard broadband for as long

1 as possible if standard broadband was more profitable for them than superfast broadband
2 even if superfast broadband was itself profitable? So as long as standard is more profitable
3 than superfast they would have an incentive to stay there, do you accept that?

4 A. I think that is right. Obviously it was a combination of profitability and customer retention,
5 but yes.

6 Q. I think that is a point you made yourself in the original FAMR consultation, which is at
7 bundle III/II -- sorry, I am calling it you, Ofcom, but you understand there is nothing
8 personal here. It's in III/I, tab 3, the analysis at 301 which is page 279.

9 MR. ALLAN: Sorry, I am still struggling with the document.

10 MR. THOMPSON: III/I, tab 3.

11 MR. ALLAN: That starts at page 320.

12 MR. THOMPSON: Do you have hearing bundle volume III?

13 MR. ALLAN: Yes. Part I.

14 MR. THOMPSON: It should be the Fixed Access Market Review consultation dated
15 3rd July 2013.

16 THE CHAIRMAN: It's the wrong page number.

17 MR. THOMPSON: Sorry, I have given you the wrong number. 279, sorry.

18 MR. ALLAN: Thank you.

19 MR. THOMPSON: It's the passage running 11.301 through to 11.303. It's a fairly elementary
20 point but none the worse for that. It runs down to 304.

21 A. Yes.

22 Q. I think it's particularly 303:

23 "... in the early days, when few customers are motivated by the prospect of
24 superfast broadband, some CPs may only engage in limited, targeted promotion
25 of superfast broadband, in order to avoid cannibalising their profits on standard
26 broadband. They are thus likely to have few superfast broadband subscribers.
27 However, if many more consumers were highly interested in superfast
28 broadband then these CPs will need to promote superfast broadband in order to
29 avoid losing customers altogether."

30 So the basic point is the one I have made, I think, that while standard broadband is more
31 profitable for them there is no real incentive?

32 A. Yes, and as that paragraph says, until they have to start doing it because there is a risk of
33 losing customers, but yes, absolutely.

34 Q. There is an even more basic reason that is if the product doesn't exist, and this was obviously

1 being rolled out over a period, then they don't have an incentive to follow it, you would
2 accept that?

3 A. Sorry, if the product doesn't exist?

4 Q. You will recall this product was rolled out from 2009 to -- well, to some extent until the
5 present day, but it only reached, I don't know when it reached, say, 40 per cent, 60 per cent,
6 80 per cent, but you would accept I think that someone like Sky or TalkTalk wouldn't have
7 an incentive to pursue it or market it when it was only covering, say, 20 per cent of the
8 country, would you accept that?

9 A. I don't know about that point. If it was more profitable and it would only cover 10 or
10 20 per cent of the country they might want to go for it. You are probably right that it's
11 an easier proposition to market the bigger the coverage is, but if it is a profitable product
12 and it's available they might decide that it was worth going, even on a small coverage. It
13 would be their choice.

14 Q. Yes. And in assessing this, another factor would be if Ofcom itself had created or maintained
15 incentives for Sky or TalkTalk to stay with standard broadband during the relevant period,
16 would that be a relevant factor as well?

17 A. So if we had done things that made the standard broadband products look more attractive to
18 them, then yes, it makes them look more attractive to them which plays directly into this.

19 Q. Yes. I suspect you will know this issue quite well. It appears in the evidence of Mr. Murray,
20 paragraph 25, which is at tab 5 of the witness statement bundle. It's page 8, paragraph 25.

21 A. Yes.

22 Q. If I can summarise it, we can go to the documents if necessary, but in summary, what
23 happened was that Ofcom found that the price differential between Sky and TalkTalk and
24 BT on the standard broadband market was based on regulated prices which gave a cost
25 advantage of £19 to Sky and TalkTalk whereas the cost difference was less than £4. Do you
26 remember that?

27 A. Yes, I do.

28 Q. It's dealt with in section 6 of FAMR. I don't know if we need look at that, it's a fairly dry
29 discussion. But the gist of it was that a glide path was put in place which will bring it down
30 to an aligned position by the end of this market review, do you recall that?

31 A. I do, and in fact actually I think by the end of the market review period, in fact actually March
32 next year because that is the beginning of the final year of that charge control, I think the
33 difference, if I have got the right one, the WLR SMPF difference, I think it will be down to
34 £1 something by March next year.

1 Q. But would you accept that there has been a regulatory incentive, if I can put it that way,
2 created by Ofcom itself in favour of Sky and TalkTalk on the standard broadband market?
3 Would you accept that?

4 A. There was and -- you know, if you like, there was a distortion that made the MPF product
5 slightly more attractive historically and Sky and TalkTalk used the MPF product so they
6 took advantage of that distortion.

7 Q. Yes, and in effect BT is obliged to keep the two split. I think that was a regulatory obligation
8 initially and I think it is still in place?

9 A. Yes, I'm not sure there is a regulatory obligation. That sort of came about historically because
10 BT had a telephone network which it then -- and then built a separate broadband network,
11 so it had these two separate networks, so it almost had to have that arrangement. So I think
12 it was one of just practicalities.

13 In terms of could BT use MPF, I think the answer to that question is yes, and in fact there
14 have been conversations over the last ten years with BT about if they were to upgrade their
15 network, what would they consume as the input and would be it be MPF? We have sort of
16 discussed it with them and even gone out to ask them questions in consultations in some of
17 our narrowband reviews.

18 So it's not so much a requirement that they are there, it's a historical sort of consequence,
19 and it is sort of BT does have some control about when it could move to MPF itself if it
20 chose to.

21 Q. But I think you would accept the substance of the position is that Sky and TalkTalk have had,
22 and will continue to have I think you are saying until next March, a pricing advantage on
23 the standard broadband market?

24 A. Yes. So they have had an advantage, and as you say, for the next three months or so they will
25 have an advantage. The advantage now is I think a few pounds per year different than what
26 it should be and that disappears next year.

27 Q. Can we look at 57 and 62 in your statement.

28 A. 57 and 62?

29 Q. Yes. At 57 you say:

30 "BT Group might make healthy margins on the sale of wholesale fixed access
31 connections, in this case VULA, but lower margins on its retail activities. This
32 would allow BT Group to make an acceptable margin on an end to end basis,
33 and at the same time would weaken retail competitors who are reliant on
34 VULA."

1 That assertion is entirely neutral from a competition point of view, it is simply saying you
2 can make more margin on one market than on another?

3 A. Yes.

4 Q. And it doesn't matter if you overall make it?

5 A. Yes.

6 Q. And I take it Ofcom has no objection in itself to retail price competition?

7 A. No.

8 Q. And if one market is more competitive than another, would you accept that it's likely that the
9 margins on the more competitive market will be lower?

10 A. Generally, certainly absent regulation.

11 Q. And the reduction in the margins on the retail market or the competitive market would
12 normally be pro-competitive and with benefits for consumers?

13 A. Sure.

14 Q. Were you in court, in the Tribunal, for the evidence of Mr. Petter?

15 A. I was.

16 Q. And you will recall that his evidence was that in fact BT's superfast business was more
17 profitable than its standard business, do you recall that?

18 A. I can't remember exactly. I remember him saying there was some higher revenues or
19 something, [Confidential] more revenue with superfast customers.

20 Q. Yes, I think there were some confidential figures ... that is all right.

21 Can I also ask you, there are some documents which are appended to the decision and then
22 some more that are appended to Mr. Matthew's statements, I can go to that as well, with
23 Mr. Matthew, but I suspect you will be reasonably familiar with these documents. It's at
24 tab 13 of the same bundle. If you turn over the page to point 4 there is a number of
25 paragraphs, there is a fat paragraph followed by four thin paragraphs. Given that this is
26 marked as confidential to BT I won't read it out, but you see the last two sentences --

27 A. Of the first paragraph?

28 Q. Yes, the first paragraph. I can't think that the first sentence is confidential but the second one
29 makes a point about the relative margins for wholesale and retail broadband.

30 A. Sure.

31 Q. Presumably you had no objection to that either?

32 A. No.

33 Q. Can we turn to -- there is one other point. Mr. Petter made a point which I am sure you will
34 recall about the effect on the share price of shifting profits between different parts of BT

1 and the fact that if you shifted from the unregulated retail to the regulated wholesale, if I can
2 put it that way, then that would have an adverse impact on the BT share price?

3 A. Yes, I recall that.

4 Q. Do you have any reason to dispute that?

5 A. It is not really an area I am particularly familiar with, how analysts would value a company
6 under those circumstances. Some colleagues of mine might be better placed.

7 Q. I understand.

8 Can we look at paragraphs 62 and 63. This is an important paragraph, it feeds to some
9 extent into the design issues but it is also I think an important point to understand what
10 exactly Ofcom was concerned about.

11 A. Yes.

12 Q. In the middle you say:

13 "I would note that in its appeal, BT is essentially arguing it should not be forced
14 to recover all of its costs in a linear manner but should instead be allowed to
15 defer the recovery of certain costs ..."

16 And you don't spell out what those costs are, but I think you will recall, if you were in court,
17 some fairly eloquent statements by Mr. Tickel and Mr. Petter about the likely impact of this
18 on their ability to bid for expensive sports rights, which are effectively a particular kind of
19 fixed cost, and also their ability to enter into certain types of agreement which had fixed
20 revenue guarantees. Do you recall that?

21 A. Sure, I remember what they said.

22 Q. So when you refer to "certain costs", is it that type of cost that you are referring to?

23 A. That type of cost is definitely one and probably quite a big one in this particular piece of
24 regulation in this appeal.

25 Q. So if we placed "certain costs" with "major fixed cost investments such as sports rights",
26 would that be a more explicit account of your evidence?

27 A. I think that that is definitely one of the big costs that would fall into this bucket, absolutely.

28 Q. That is what Mr. Bishop was talking about, I don't know if you have read his report but we can
29 look at it, for example at tab 9. We discussed the monthly bit which appears at page 29, but
30 there is a passage at page 28 through to 29 and I think you will understand the complaint:

31 "The inclusion of common fixed costs creates a price umbrella for BT's
32 VULA-based rivals."

33 And I think the point is summarised at paragraph 120 where he talks about the sufficiency
34 of a margin to cover incremental costs, but they don't need to be able to cover very large

1 fixed costs. You understand that is the point that is being made?

2 A. Sure. And this I think -- as you just said a moment ago, this all goes to the design of the test.

3 Q. But it also goes to the nature of the test and also the nature of the concern that motivated this

4 test, because you go down to set out the complaint -- or the concern at points A, B and C?

5 A. Yes.

6 Q. And if we put in the correction we have put in, and it says:

7 "BT Consumer does not cover all of its major fixed cost investments such as

8 sports rights in the early phase, it then grows its customer volumes and then it

9 recovers [at C] all of its major fixed cost investments such as sports rights in the

10 future."

11 And I think Mr. Bishop suggested over the term of those rights, for example. Then the logic

12 doesn't really go through, does it? That is just a perfectly normal commercial approach?

13 A. Well, this -- so clearly this is one of the points that BT disagrees with us on. And undoubtedly

14 what we have said in this test, given the market conditions, is things like big fixed costs, and

15 sports rights is clearly one, should be recovered in some sort of linear manner. So we are

16 recovering them over the sports rights periods, so three years or whatever it is. But what we

17 are sort of saying is, for example, if you had a static customer base, you would -- you would

18 recover them a third in the first year, a third in the second year, a third in the final year.

19 You wouldn't be able to recover none in the first two years and then expect to get them all

20 in the last year, for example, in the two extremes.

21 Q. Yes, but can we just read into a focus because at 63 you say:

22 "This market outcome is exactly what the margin rule is attempting to prevent."

23 A. Yes.

24 Q. But can you really say that the purpose of a margin rule is to prevent someone spreading

25 major fixed cost investments over an extended period? That is not the purpose of a margin

26 rule, is it?

27 A. So this margin rule as an ex ante price control, which is what it is, has its aim of promoting

28 competition in superfast in the future.

29 Q. Exactly.

30 A. And what we are saying is if we believe that a market outcome followed this pattern of A to

31 C, that effectively thin or below cost margins are recovered in the early stages, whatever

32 cost standard you are looking at, and this resulted in a situation where we had weaker

33 competition, where somebody like BT had won more customers and churn was low, and

34 then they could actually recover costs in the future, which at that time would actually have

1 to be quite high margins, then we would have failed in our aim of promoting competition in
2 this market. And given that under the ex ante rules we are trying to introduce here, we are
3 trying to ensure we do have competition in the future, that is the intent of this ex ante
4 regulation.

5 Q. Yes. I don't want to delay this, but you say that BT's complaint relates to certain costs, and
6 those costs are the very large fixed costs being recovered on a monthly basis. You say that
7 is exactly what the margin rule is intended to prevent. I'm not sure whether you stand by
8 that or not, once we have clarified what the certain costs are. Is that the purpose, to prevent
9 BT spreading its fixed costs over a period or is that not the purpose?

10 A. The purpose of the rule is to try and ensure that we have competition in superfast broadband in
11 the future.

12 Q. Yes. And the point that is made by Mr. Bishop is you don't need this type of rule for that type
13 of purpose. And I'm not sure whether you are accepting it or denying it?

14 A. Well, it was a point raised during the consultation and it was put to us by BT and we rejected
15 it. We actually came to the conclusion that allowing too much flexibility in how the shape
16 of cost recovery occurs could in fact undermine our objective for promoting competition
17 and that is why we designed the rule in the way we did.

18 Q. Yes. And you will remember this is an issue, and here -- it's an important issue for this
19 purpose, although it obviously flows over into other issues, that in saying that, I think you
20 must be aware that the European Commission has expressed considerable doubts about this
21 approach even on a six monthly let alone a monthly basis, you recall that?

22 A. Are you talking about the Commission's comments to the article 7 notification?

23 Q. Yes, I am.

24 A. So, yes. The Commission made certain comments. I believe some of them we took on board
25 and addressed, others perhaps we didn't address to the same extent, but we set out, given the
26 national circumstances, why we believed the approach we finally adopted was the right
27 approach for the UK.

28 Q. So at 63 you are saying that the margin rule is exactly intended to prevent what the
29 Commission thinks you should do, that is the purpose of this margin rule?

30 A. I am saying the margin rule is intended to promote competition in broadband --

31 Q. But that is not what you say --

32 A. -- and its construct we believe is a right balance to achieve that aim.

33 Q. But that is not what you are saying. You specifically set out A, B and C?

34 A. Yes.

1 Q. Which is preventing BT Consumer recovering its fixed costs over a period, which is precisely
2 what the Commission says you should be allowing and you are saying your rule is exactly
3 intended to do the opposite?

4 A. Our rule in terms of those costs sets out, if you like, the recovery profile over the rights
5 periods. So it puts limitations on the profile of cost recovery that BT can adopt, absolutely.

6 Q. Yes. Can you turn to paragraph 72 and you will recall that -- and this is a matter that has also
7 raised some excitement from Sky and TalkTalk's witnesses. You refer to Mr. Tickel and
8 Mr. Murray effectively saying there is an incentive for BT to encourage people to use
9 VULA given the amount of money they have spent on it, and I think in outline you accept
10 that is correct as a matter of principle?

11 A. Yes.

12 Q. Then you go on:

13 "In making these claims, I assume Mr. Tickel and Mr. Murray are seeking to
14 demonstrate that Openreach has made developments to VULA to make it more
15 attractive to all CPs and that is keen to sell VULA to all CPs."

16 If we take it in stages, I think you will probably recall without my going back to it that
17 Mr. Tickel says that BT has strong incentives to grow incremental volumes for the reasons
18 we have just mentioned, and you accept that. And you accept of course that BT is entitled
19 to charge for its product?

20 A. Yes.

21 Q. You say at 75:

22 "In terms of Openreach having strong incentives to grow incremental volumes,
23 I accept this point to a certain degree. Clearly Openreach will want to grow
24 volumes but there will be a trade-off between volumes, price and profit."

25 And then you make what is certainly a correct but perhaps a somewhat elementary point
26 that the profit maximising strategy will not necessarily be to give it all away for free. There
27 will be a time at which just making more and more of it but not charging enough won't be
28 the profit maximising strategy and I think everyone can agree on that.

29 Do you find it surprising that BT, Sky and TalkTalk haven't always been able to agree on
30 the terms on which Sky and TalkTalk obtain access to the VULA product?

31 A. No, no, clearly not.

32 Q. Have either Sky or TalkTalk raised any disputes alleging that BT has been acting in breach of
33 its regulatory obligations in relation to VULA?

34 A. I don't think they have raised any formal disputes as far as I can remember.

1 Q. Has Ofcom ever suggested to BT that it's acting in breach?
2 A. I don't think we have ever formally had those types of conversations with BT.
3 Q. Did Ofcom find any merit in TalkTalk's claim under article 102?
4 A. Under the Competition Act investigation?
5 Q. Yes.
6 A. No.
7 Q. At paragraph 76, you express an opinion about capacity, I don't think we need to turn it up, but
8 Mr. Tickel gives detail about capacity. Do you have any reason to doubt Mr. Tickel's
9 evidence about the capacity of its engineers?
10 A. No, I don't. I saw Mr. Tickel's response, and I think he basically said -- he sort of said, well,
11 we've got enough engineers to do what we need to do, type of thing, I think was broadly his
12 response. I don't think he claimed that they had infinite resource or lots of resource sitting
13 around, but yes.
14 Q. Do you consider as a regulator that the fact that BT may have, at some limit, some capacity
15 constraints or that there may be evidence that customers and suppliers have sometimes had
16 disagreements, does that provide any support at all for the suggestion that BT might engage
17 in a margin squeeze?
18 A. So it is probably worth taking those one at a time. In terms of people just complaining,
19 I guess maybe not, people complain. We'd just investigate those and look at the facts at the
20 time. In terms of if there was constraints, you know, I guess if you do have constraints and
21 you do want to, if you like, hold off demand, one way of doing it is through pricing,
22 certainly I think it happened before in various markets. So BT could decide that through
23 pricing they might want to hold off, to sort of chaperone demand in, if that was the situation
24 they faced.
25 Q. Yes, but on the one side you accept the basic point that here is a huge investment, BT has
26 reason to grow volumes. You make an academic point that it is not infinite and they don't
27 want to give it away for nothing. You say Sky and TalkTalk on occasion have not been
28 able to reach agreement. And you say there might be a capacity constraint. Does any of
29 that give the slightest reason that BT might engage in a margin squeeze?
30 A. I think it is the point I just said a moment ago. It is possible that BT might want to sort of
31 manage demand, and if through pricing that could be done, and if that happened to impact
32 on Sky and TalkTalk initially, then I guess fine --
33 Q. Perhaps I put it wrongly. On the one side there is a clear incentive you do accept, the need to
34 grow volumes to cover the investment?

1 A. Yes, as I say, to a point. We have already I guess agreed that you don't just want to
2 necessarily get one million orders next month or -- there are lots of ways of growing
3 volumes. You certainly want to grow enough volumes to ultimately pay for the investment.

4 Q. And then on the other side are these three factors that you have put in place, and I can make
5 submissions but I would say that one side is clear and the other side is, at best, tenuous.
6 At 78 you also say that the fact that BT wishes to increase its volumes would not preclude
7 BT from imposing a price squeeze, and this is a point that is made at various places by
8 Mr. Matthew, by Ofcom, in their skeleton argument. And it is as if what matters is to prove
9 that there is somehow a shutter come down so that BT can't impose a margin squeeze, that
10 seems to be what you are saying there. That just because BT has incentives to increase
11 volumes and it doesn't matter where they come from, that wouldn't preclude BT from
12 imposing a price squeeze and I think we can all agree on that.
13 But you understand in this case the core issue is about incentives, not about what would be
14 precluded, it's about incentives, you understand that, yes?

15 A. Yes, in terms of the risk that BT will -- might impose a margin squeeze, yes, okay.

16 Q. So the point that is being made is that BT has strong incentives to grow its wholesale volumes,
17 you understand that?

18 A. That is the point that you are making now, yes.

19 Q. Yes, but the point is not about what would or wouldn't preclude BT, it is what would or
20 wouldn't incentivise BT, you understand that?

21 A. Okay, I'm not sure if I am understanding the distinction. Sorry.

22 Q. I think a regulator probably does understand it and I suspect the Tribunal does. I don't want to
23 waste time --

24 A. Sorry, I am probably being a bit slow. So the point of 78 I guess I was making is sort of let's
25 suppose Openreach wants to sell 2 million GEA connections, VULA connections. The
26 point is that TalkTalk, Sky and BT Consumer might all be prepared to buy 2 million
27 connections under a certain scenario, and what this point is saying is but if BT Openreach
28 really just wants to sell 2 million, what they could do is impose a margin squeeze such that
29 in fact it is more attractive for BT Consumer to buy the 2 million and they still sell the
30 2 million lines and they still get the volumes that they desired.

31 Q. Yes, I understand. But we are talking at the level of incentives because I think in terms of
32 ability, BT conceded for these purposes at least that having made an SMP finding, you were
33 entitled to make an ability finding, and that is the premise we are all working on. So I think
34 it's not about precluding, it is all about incentives. That is the only point I make.

1 Then just finally, and it is in fact your final paragraph, you note that BT hasn't reduced its
2 price over six years?

3 A. Yes.

4 Q. Since 2009, and I just wanted to pick up two points. First of all, Ofcom looked at this very
5 question about BT's VULA price in the FAMR and we have looked at the paragraphs
6 already, and they didn't impose a price control, and they indicated that they thought that
7 standard broadband pricing would prevent or constrain BT from raising its prices, that is
8 correct, isn't it?

9 A. Yes, so I think the main point is it is sort of accepted that we -- we have given pricing
10 flexibility, so the actual price that BT charges is up to them.

11 Q. Yes.

12 A. Yes.

13 Q. And at 10.39 and 40 of FAMR, which we might just look at because I don't think we have
14 looked at it yet and it's of some relevance to the point we discussed at the start.
15 Bundle III/II, tab 8.

16 A. What paragraphs?

17 Q. The way it worked and you will probably recall this, is that section 10 were general remedies
18 and section 12 were specific remedies. So in section 10 you will see at 10.2 there's
19 a description of what general remedies are, it's page 172. And then there is a reference to
20 specific remedies in 10.4. Then volume II sets out detailed approaches to LLU and WLR.

21 A. Yes.

22 Q. If you turn through, you find at 10.39, page 185, for VULA they refer forward to section 12,
23 No imposition of cost base but BT is required to ensure that its charges for network access
24 should be fair and reasonable.

25 Do you see that?

26 A. Yes.

27 Q. Then when you go on to 10.76 at page 191, the box above, I think VULA comes under WLA,
28 is that right?

29 A. Yes, it does.

30 Q. And it says:

31 "Including fair and reasonable charges where no other pricing obligation
32 applies ..."

33 So that would be this case?

34 A. Yes.

1 Q. 10.76, second half:

2 "Section 87(9) of the CA03 also authorises SMP services conditions imposing
3 on the dominant provider such rules as they may make in relation to matters
4 connected with the provision of network access about the recovery of costs and
5 cost orientation, subject to the conditions of section 88 of the CA03 being
6 satisfied."

7 And then across at 10.79 there is reference to the test in section 88, and I think the point that
8 probably takes us right back to the beginning again is that the concern at 10.79 is couched in
9 terms of excessive rather than margin squeezing as being the relevant risk for the FRAND
10 position --

11 A. Yes.

12 Q. -- in 2014 as against the position in 2010. So I think it is the word "price excessively" rather
13 than "may impose a margin squeeze" that was probably the point you were talking about at
14 the beginning.

15 A. Yes.

16 Q. There is obviously a legal question as to whether an identically worded condition which has
17 a different justification changes its meaning but I understand that is the point that FAMR's
18 lawyers are now suggesting may be the case?

19 A. Sure.

20 Q. Can you just flick back to paragraph 34 of your statement and about six lines down you will
21 see a reference to ceilings and floors.

22 A. Yes.

23 Q. What I understand that to mean is, and in terms of article 102, you are talking about the
24 possibility of excessive pricing or predatory pricing, and you impose a ceiling to prevent
25 excessive pricing and a floor to prevent predatory pricing, in broad terms, is that right?

26 A. In broad terms, although I don't think it was -- predatory pricing wasn't the issue --

27 Q. Not in that case but broadly that is what it means?

28 A. Yes, this was sort of an extension, so you -- we talked earlier about the June 2005 price
29 commitments, which was a margin that came out at the same time as that broadband
30 statement and the consultation on the undertakings. They expired at the back end of 2006
31 and BT made further commitments to effectively the floors -- so what was happening here
32 is because it was sort of recognised that local loop unbundling was unlikely to go
33 everywhere in the country, there were some areas where you would have local loop
34 unbundling and other areas where you wouldn't.

1 What these did was in the areas where you expected local loop unbundling to happen, BT
2 committed to a floor which protected the margins for local loop unbundlers, and in the areas
3 where you weren't expecting local loop unbundling to work they committed to a level of
4 ceilings which sort of protected consumers from excess prices in those areas because you
5 weren't expecting competition to --

6 Q. Yes, that is very helpful. And the point I was going to take you to was that -- given the focus
7 of this hearing it may seem slightly fanciful, but you will or you may recall that
8 Virgin Media expressed a concern about the lower price of VULA, do you recall that?

9 A. Yes.

10 Q. Just for the Tribunal's benefit, if we look at that, it's at the FAMR decision itself, tab 8 again,
11 and it's paragraph 10.42. Virgin has asked for more guidance, and then it goes through at
12 12.141, Ofcom said:

13 "We do not, as suggested by Virgin, consider it necessary to set out specific
14 guidance on how we would assess potentially below cost VULA prices under
15 our ex ante framework as the principles underlying competition law, which are
16 well developed, will be likely to form the starting point for any such
17 assessment."

18 Would you accept that the incentives point there is, and we have heard some evidence about
19 it, that Virgin has invested substantial sums and is planning to invest more and so there
20 would be a concern if BT priced VULA too low so that Virgin's investments became
21 unprofitable?

22 A. Sure. Obviously at the time this was written, I don't think Virgin had announced its plans to
23 make further investment --

24 Q. No, I'm not suggesting --

25 A. But, yes, this is essentially, as you say, Virgin have made the investment and they clearly
26 would not benefit from lower pricing in the market.

27 Q. No. And the investment issue goes further because we have seen some limited evidence of
28 Sky and TalkTalk spending money in York, and it may seem slightly fanciful given the
29 terms of Mr. Heaney and Mr. Blumberg's evidence, but in fact Mr. Heaney has given other
30 evidence in other cases, which I think went up to the Court of Appeal, where TalkTalk were
31 complaining that too tight a condition might be imposed on BT. So presumably in principle
32 reducing the VULA price could have adverse impacts on investment incentives for persons
33 other than Virgin, would you accept that?

34 A. It could do. Obviously, as you have just said, TalkTalk and Sky in their York venture haven't

1 come to that conclusion. I wasn't sure about the other TalkTalk case you were making
2 reference to.

3 Q. It was about roll-out I think of some form of LLU and it went to the Court of Appeal --

4 MR. HOLMES: Sir, I hesitate to interrupt. I wonder how appropriate it is really to be discussing
5 other evidence in relation to a witness that Mr. Thompson hasn't chosen to call for
6 cross-examination and where the witness statements aren't even before the Tribunal that
7 Mr. Clarkson could be shown.

8 MR. THOMPSON: No, that is a fair point. But in principle, you would accept that the incentive
9 for people other than Virgin to invest would potentially be impacted if BT reduced its
10 VULA price?

11 A. Sure. And if it was us taking the decision to set prices, those were the things we would have
12 to trade off in our decisions. In this case we didn't take the decision to set the price so ...

13 MR. THOMPSON: Those are my questions. Thank you, Mr. Clarkson.

14 MR. HOLMES: Sir, I have two very brief questions in re-examination, if I may.

15 **Re-examination by MR. HOLMES**

16 MR. HOLMES: Mr. Clarkson, you were taken to the broadband regulation document, the
17 statement from 30th June 2005. I see you have rather a lot of files in front of you.

18 A. I haven't been putting them away.

19 Q. I think that one you may have put away. It's DF2.

20 A. I have it.

21 Q. At tab 13. You were asked by reference to this document to comment on whether the
22 problems with BT's margin were addressed through the commitments or the undertakings,
23 which were more or less at the same time.

24 A. Yes.

25 Q. I think the paragraphs that you were taken to were 15 and 16.

26 A. Correct.

27 Q. Could I ask you please to review paragraph 10 and paragraph 17.

28 A. Okay.

29 Q. Is there anything you would like to add to your answer in the light of those paragraphs?

30 A. There was something else in here, because I think the point being asked was really about
31 whether or not margin protection in some way fell under the undertakings, and I was sort of
32 saying, well, paragraph 15 here was about the commitments, which is margin, and 16 was
33 about the undertakings, which is more to do with equivalence at the product level and so on.
34 There was -- there was something that I remember happening at the time, I bumped into it

1 the other day when I was just reading through the documents, and it related back to the
2 statement at the time of the undertakings being introduced which I will try and find now.

3 I think it is ... it's the bundle volume IV, if I can find it ... (Pause)

4 So, yes, we started looking at this document as well, so this is hearing bundle volume IV,
5 tab 3, and it was the statement in September 2005 when the undertakings were introduced,
6 and particularly page 56 which is in fact the very last page in this extract in this document
7 here.

8 So we had at the time these commitments from BT in June, and we were also introducing
9 the undertakings. Before we finalised the undertakings we did have various respondents
10 and at the very bottom of this page, under "Other Issues", people raised with us and said:

11 "BT's commitments on the LLU broadband margin ..."

12 These were the ones from 23rd June:

13 "... should be included in the undertakings."

14 And our view at the time, which -- you don't need me to read it out there, but essentially it
15 was that actually to the extent that we need to be looking at margins, then that is the rightful
16 place, is the ex ante framework.

17 MR. HOLMES: I have no further questions. Thank you.

18 THE CHAIRMAN: Thank you very much. We will break there for five minutes.

19 (3.10 pm)

20 (A short break)

21 (3.15 pm)

22 MR. HOLMES: Sir, may I call my witness Mr. Matthew.

23 THE CHAIRMAN: Yes.

24
25 **MR. DAVID HAMISH CURRY MATTHEW (affirmed)**

26 **Examination-in-chief by MR. HOLMES**

27 MR. HOLMES: Mr. Matthew, you should by your side have a number of bundles. If you could
28 pick up hearing bundle II and turn within that to tab 12, you should see there on the second
29 page of that document, at the top of the page, is that your name and address?

30 A. Yes, it is.

31 Q. If you could turn to the back of the document at that tab. Do you have there a signature?

32 A. Yes.

33 Q. Is that your signature?

34 A. Yes, it is.

1 Q. Is this your evidence in this case?

2 A. Yes, it is.

3 MR. HOLMES: I think Mr. Thompson may now have some questions for you.

4 **Cross-examination by MR. THOMPSON**

5 MR. THOMPSON: Good afternoon, Mr. Matthew. Just before I start, I referred to a case which

6 Mr. Holmes quite correctly said came a bit out the blue. If I can give the references, it's

7 [2013] EWCA Civ 1318 and [2012] CAT 1, that is the TalkTalk case I referred to.

8 Mr. Matthew, were you in court for Mr. Bishop's evidence?

9 A. Yes, I was.

10 Q. Could I ask you to turn to Mr. Bishop's second report.

11 A. Sorry, where is that?

12 Q. There is a bundle of witness statements which you should have in front of you, and then there
13 are two reports from Mr. Bishop at tabs 9 and 10, so just in front of yours.

14 A. Yes.

15 Q. He sets out a number of areas of agreement. Have you had a chance to read them?

16 A. This is in the second report?

17 Q. Yes. At page -- I don't know if it is numbered but it's at point 2, paragraph 6 to 11.

18 A. Yes, I read these before.

19 Q. Does he accurately identify points of agreement or not?

20 A. It is quite a long list.

21 Q. Yes.

22 A. The precise way in which he presents some of my observations I'm not sure I would agree
23 with, but I would need to go through them now somewhat point-by-point if you are going to
24 ask me do I agree with all of them.

25 Q. That's fine. So do you agree with the first point, that there are costs and benefits associated
26 with imposing the margin squeeze?

27 A. I agree there could be in some circumstances, but as I set out in my report, it is conceivable
28 that BT might even impose a price squeeze without having to face a trade-off. And the sort
29 of dynamics I had in mind were we have heard from BT about how the fact that they are
30 vertically integrated with Openreach leads BT Consumer to have quite strong incentives to
31 drive sales of superfast broadband and that may lead to quite a low superfast broadband
32 price as a consequence.

33 But when Openreach -- even if Openreach is ignoring the interests of BT's consumer
34 division, when it comes to say what price should we set for VULA to Sky and TalkTalk,

1 they may take into account a number of factors. And even if we focus on just a narrow
2 profit maximising price, what is the most profit they can extract out of the price they set to
3 those two companies, with different parameters around that it is not inconceivable they
4 might choose to set a price to Sky and TalkTalk at such a level that it would result in a price
5 squeeze almost by default, even though the intention wasn't necessarily to support the
6 interests of BT Consumer.

7 But apart from that, I do understand the general point Mr. Bishop is making, so with that
8 caveat, I do understand it is useful to explore the trade-offs between the interests of
9 BT Consumer and the interests of Openreach.

10 Q. Yes. He draws out at 8 the fact that in assessing incentives, you need to look at the trade-off
11 between the benefits and also the costs, and I think with the qualification you have quite
12 properly introduced I think you agree at that sort of level of abstract figure that there are
13 trade-offs?

14 A. Yes. I think it might be useful to hold a discussion assuming that the profit maximising price
15 separated Openreach would set is set at a level which would not itself result in a price
16 squeeze by default, and that therefore there is potentially a trade-off that BT Group would
17 need to make.

18 So if we can preface this discussion with that assumption in mind and recognise that that is
19 an assumption.

20 Q. Yes. I thought this might be a relatively quick way into this but I think you quite properly
21 don't want to be pushed into anything so I think it may be better to take the points
22 individually and see whether we get the agreement or not.

23 Can I then -- we will move away from that because I can see that you quite rightly don't
24 wish to be pushed into anything so that is fine. Let's move to a different topic which is the
25 question of regulation at the fairly abstract level. It's a point that Mr. Bishop makes and
26 I think at the level of abstraction, I hope there won't be any disagreement, there has been
27 a long dispute between economists and lawyers, but broadly speaking economists are in
28 favour of a realistic approach to regulations, so not a black and white but a realistic,
29 economically intelligent approach to regulation. You would agree with that?

30 It's not meant to be a trap. I was expecting you to say "Yes".

31 A. If you are asking me to agree, would I agree that good regulation from an economist's
32 perspective is good regulation? Then probably yes. But I think it is quite -- I'm not quite
33 sure what specific point one would draw from that.

34 Q. You can have economically unintelligent regulation, black and white regulation, which

1 a lawyer might like, and perhaps the Restrictive Trade Practices Act is the ultimate example
2 of that. You can see, looking down, whether this or that and count the number of people.
3 Or you can have intelligent regulation, as it were, which draws the distinctions in a more
4 economically intelligent way. I think it was generally thought, when the Competition Act
5 was brought in, that was an improvement because it was a more intelligent form of
6 regulation than the Restrictive Trade Practices Act.

7 I am really at that sort of rather abstract level and I think you would agree with me on that?

8 A. It's quite an interesting philosophical debate. The objective of good regulation from
9 an economist's perspective is something that is going to deliver the gains that you wish to
10 see at the least distortion you can get from the markets concerned. As to whether
11 that -- I think you are alluding to the introduction of the more effects based assessment in
12 cases, is that what this ...

13 Q. I was really think more of, for example, if we take paragraph 38 of the Ofcom skeleton
14 argument, it says:

15 "Ofcom agrees that a realistic economic approach is appropriate."

16 Would you agree with that? Or is that something that needs qualification?

17 A. Sorry, I thought you were asking a generic question about the nature of the best type of
18 regulation which I do see is quite interesting but ... I'm sorry, I was going to go on to say
19 that one can imagine an economist might support circumstances that a relatively binary test
20 was appropriate.

21 Q. I don't want to trap you. I was thinking you would probably agree with the things in
22 the Ofcom skeleton but maybe that is a rash assumption.

23 A. Perhaps you should take me to that context rather than ...

24 Q. Okay. Do you have access to it? It's in volume I, tab 2, page 14, paragraph 38:

25 "BT contends the need for a realistic economic approach is endorsed and
26 reflected by the structure of the CRF ..."

27 So that is the EU legislative scheme:

28 "... and Ofcom agrees that a realistic economic approach is appropriate."

29 Are you happy with that?

30 A. Yes, without reading around it I'm not absolutely sure what this is referring to, but ...

31 Q. I think it was meant to be a fairly bedrock point. If we can't agree that sort of thing we are
32 going to get on slowly but I don't want to hurry you.

33 A. I am just merely observing that this is a third point in a discussion of something else that you
34 are asking me if I precisely agree with this. I'm sure I would. All I am saying is I would

1 need to read back to remind myself what it is actually referring to.

2 Q. Let's move on to what is hopefully even safer ground which is Ofcom's policies. Would you
3 agree that Ofcom has a bias against regulation?

4 A. Yes.

5 Q. Both absolutely and in the design of regulation?

6 A. I think our general policy is that we regulate only where it is necessary, but when we regulate
7 we do regulate properly and effectively, so ...

8 Q. Let's have a quick look and then see if we agree with this. It's at authorities bundle I, tab 17.
9 "Better Policy Making" it is called and it was issued three weeks after the undertakings
10 consultation on 21st July 2005.
11 Point 1.1, you say:
12 "The decisions which Ofcom ..."
13 Or Ofcom says this, I wouldn't presume to say that you would say this:
14 "... makes can impose significant costs on our stakeholders and it is important
15 for us to think very carefully before adding to the burden of regulation."
16 And then you say:
17 "One of our key regulatory principles is that we have a bias against
18 intervention."
19 So would you accept that?

20 A. Yes. As I said, we should only regulate where it is necessary.

21 Q. It says:
22 "This means that a high hurdle must be overcome before we regulate ..."
23 Do you accept that?

24 A. Yes.

25 Q. "... [and i]f regulation is justified, we aim to choose the least intrusive means of achieving our
26 objectives, recognising the potential for regulation to reduce competition."
27 Do you accept that?

28 A. Yes.

29 Q. And then at 3.3 you say:
30 "At the outset, we should identify the issue to be addressed and the options
31 available to us. In doing so, we should continue to bear in mind the need for
32 options to be linked with our statutory duties. We will start by considering the
33 option of not changing the regulatory framework, either by not introducing
34 regulation or by retaining existing regulation. This option, no new intervention

1 will generally be the benchmark against which other options are judged, i.e.
2 what costs and benefits would be incurred additional to those which would be
3 incurred if there were no new intervention."

4 Do you agree with that?

5 A. Yes, it makes sense, because often we are talking about a long-run game and you don't want to
6 change the regulatory rules while that happens, so it tends to be poor regulation because
7 people often don't know where they stand at the time.

8 Q. I don't know whether you read -- there is reference in the papers to a speech that was given by
9 Mr. Chisholm, do you know who Mr. Chisholm is?

10 A. Yes.

11 Q. Did you read his speech?

12 A. No, I don't think I did.

13 Q. I think probably --

14 A. I saw it referred to in the papers although perhaps you could take me to it.

15 Q. I don't want to get into too nuanced a debate. If you haven't read it then I won't ask you to
16 read it quickly now. If you want to read it over the weekend we may have time to debate its
17 merits on Monday, but ...

18 A. Sorry, just to clarify, would you like me to read it over the weekend?

19 Q. We could then see whether you agree with it, but it is not a crucial line of cross-examination
20 so I won't impose that burden on you if you ... Don't feel obliged to, so let's leave that.
21 Would you accept in relation to regulation generally, and it's a point that I think Mr. Bishop
22 makes at some length, first of all that if regulation is introduced which isn't needed, that is
23 actually a bad thing and actually anti-competitive, do you agree with that?

24 A. Yes, I do.

25 Q. And if the design is bad, so if it is unduly rigid or needs to be updated all the time, that can
26 also be a bad thing?

27 A. If the design is bad then, yes, it is bad.

28 Q. Then being more specific, in relation to a margin type of regulation, it would be bad if the
29 margin was set at too high a level?

30 A. Yes. So in our assessment we go through various options for how one should go about setting
31 the margin and we recognise that if one does go too far, you can have negative effects.

32 Q. And you would agree I think, and it is a point I discussed with Mr. Clarkson, I assume you
33 were present, that you use regulation to create or modify incentives?

34 A. Yes.

1 Q. Would you agree that regulation is intended to affect the behaviour of regulated firms, not just
2 to lead to dispute and fines, do you agree with that?

3 A. Yes, it is intended to address incentives that regulated firms may have that would otherwise
4 distort competition in this case.

5 Q. Just as red traffic lights are not intended to cause great disputes when people go through them,
6 or speed limits to lead to fines, the idea is to regulate behaviour, is that right?

7 A. Yes.

8 Q. So any realistic approach of the behaviour of undertakings on a market must take account of
9 regulation and its effects on incentives, would you agree with that?

10 A. Yes.

11 Q. That applies both in the past and in the present and the future? So if you are trying to find out
12 what has happened in the past you will look at the regulatory model, if you are trying to find
13 out what is going to happen in the future you will look at the regulatory position, and if you
14 are going to find out what is happening in the present you will look at the regulatory
15 position, is that right?

16 A. Well, if you are asking what will happen given regulation, then, yes.

17 Q. So if we look at the past, I think you and Mr. Clarkson both agree about that because you refer
18 to it yourself. We see that if we turn to paragraph 84(a) of your witness statement -- do you
19 have that?

20 A. Yes.

21 Q. You say:

22 "BT has been subject to a regulatory obligation to supply its VULA product on
23 fair and reasonable terms since 2010, accompanied by guidance that we would
24 initially consider whether the VULA margin was above the costs of the
25 reasonably efficient operator. BT has not therefore been free to impose a price
26 squeeze to date and its actual conduct is not a reliable guide to BT's underlying
27 commercial incentives absent regulation."

28 I think what you are saying is that to understand what BT has been doing you have to
29 understand the regulatory obligations acting on it, is that right?

30 A. Yes, that's correct.

31 Q. Mr. Clarkson makes the same point in his witness statement and you find that in the previous
32 tab at page 23. He gives evidence that BT's share of net adds has dropped from around
33 84 per cent to 58 per cent, do you see that at 70?

34 A. Sorry, I didn't get the tab.

1 Q. Page 23, paragraph 70.
2 A. Yes, but what was the tab?
3 Q. The previous tab, 11.
4 A. Yes. Sorry, can I have the references again?
5 Q. Tab 11, paragraph 70, page 23.
6 A. Yes. (Pause)
7 Q. I think what he is saying is that there has been a drop in the net adds and that illustrates the
8 effectiveness of your regulatory approach on BT's incentives, is that right, or the incentives
9 of others?
10 A. Yes, it shows that with regulatory conditions in place we are now expecting BT's competitors
11 to start ramping up their sales in superfast broadband.
12 Q. But that is based on the position that has been in place for the past two years, so before this
13 came into force.
14 A. Yes. I think it's a combination of the understanding then but also the clarity they now have
15 under the VULA margin condition.
16 Q. I don't think he is saying that, I think he is saying it was the position up to Q1, 2015 which is
17 the old regime, is it not?
18 A. It's the old regime, although if we are talking about how does this link to what Sky and
19 TalkTalk were actually thinking of actually doing, in the run-up to this obviously they
20 would have been familiar with the process of the Fixed Access Market Review and the
21 VULA margin consultations and they may have started to factor in some of that sort of
22 forthcoming regulation when they made their decisions, but I don't know.
23 Q. You remember Ofcom in fact favoured the guidance model in its 2013 consultation, so unless
24 they were very sure, I think Mr. Clarkson gave evidence that TalkTalk and Sky were very
25 influential but I suppose they may have been confident of their persuasive powers but they
26 wouldn't necessarily have assumed it from the start?
27 A. I can't give evidence on precisely how the various consultation documents might have affected
28 precisely how Sky and TalkTalk thought things might pan out, I am just making the
29 observation that they would have had a forward look to these things and not just what
30 happened prior to Q1, 2015.
31 Q. I am saying that both you and Mr. Clarkson say past regulation, and there is a lot more of that
32 in Mr. Clarkson about the effects of various forms of regulation over the past ten years, but
33 you certainly take that into account looking backwards?
34 A. Yes.

1 Q. And then looking forwards, you yourself raise that point twice. I think at 59(b) there is
2 actually a bit of a quirk in your evidence and Mr. Clarkson's in fact.
3 It's part of Ofcom's case that there could be this wonderful scenario for BT of overcharging
4 indefinitely and reducing the margin and making profits upstream forever so that the normal
5 constraints on a margin squeeze wouldn't apply, but here you make the opposite point which
6 is that:

7 "BT may perceive a risk that Ofcom will introduce costs plus regulation at the
8 wholesale VULA price at some point in the future which could require a drop in
9 the VULA price and a corresponding reduction in the wholesale revenues
10 earned. This factor will tend to reduce the weight that BT will place on the loss
11 of wholesale upgrades to SFBB ..."

12 I think you are saying that BT's conduct will be affected by anticipated future regulation, is
13 that right?

14 A. I'm saying I think that, yes, if we are looking at what BT's actual incentives would be in this
15 period, then you may take a view as to what might happen in terms of future regulation and
16 that might affect some of their incentives. So we heard from Mr. Petter a lot about how the
17 City will value the consumer business more than revenue earned to the Openreach business,
18 and it is that sort of thing I am alluding to here.

19 So essentially where BT expects future Openreach prices to be regulated down to costs, and
20 it faces a trade-off between, well, should I promote earning revenues from Openreach
21 compared to promoting margins coming out of BT Consumer? They will tend to shade up
22 the value they put on BT Consumer rather than Openreach. I think he even says that when
23 the analysts come to look at this, the reason they tend to put more weight on Consumer
24 rather than Openreach is precisely for that reason.

25 So the analysts expect eventually Ofcom will regulate Openreach down to cost, or some
26 alternative form. They tend to place less weight on how well that bit of the business is
27 doing and more weight on how the consumer bit is doing because it is not expected to be
28 regulated.

29 Q. So in that sense future regulation is taken into account as part of the incentives. And you
30 make a similar point at paragraph 121(c) on page 58 where you say -- your first point is how
31 difficult it would be at 120, and then you come up with a list at 121, and at 121(c):

32 "A factor that would need to be taken into account in assessing BT's incentives
33 is speculation as to whether Ofcom would introduce cost plus regulation of
34 VULA at future regulatory reviews and how this might impact on the relative

1 value BT places on expanding VULA sales to competitors and winning
2 a stronger retail market position."

3 So you again say future regulation needs to be taken into account in assessing BT's
4 incentives and conduct, is that right?

5 A. Yes, if you wanted to come up with a precise estimate of what BT's incentives are in the very
6 short-run, that is one of a range of factors you would have to take into account.

7 Q. So I think your position is that both past and future regulation needs to be taken into account,
8 but then when we come to the present case you say that the present regulation doesn't need
9 to be taken into account, is that right?

10 A. Yes, my advice was that we were to assess the risk of BT setting a price squeeze assuming no
11 existing regulation on this market.

12 Q. You do take account of past and future?

13 A. I do when I come to looking at the evaluation of what precisely BT's incentives might be.

14 Q. Yes. So it's a homely analogy, I don't know if you are familiar with Alice Through The
15 Looking Glass, but there's quite a famous dictum: jam yesterday, jam tomorrow, never jam
16 today. Is that the approach of Ofcom to regulation, you look at the past and the future but
17 not the present, is that right?

18 A. No. I think -- I'm not sure I understand the Alice Through the Looking Glass analogy. In
19 terms of current and future regulation, I am advised that we are to analyse the risks in a
20 world where you can't assume that there is regulation because to do so would be circular.
21 So in respect of -- this is what I think is called the modified greenfield approach, so you say
22 well obviously if BT had an existing price squeeze obligation on it, then to ask the question:
23 would BT price squeeze? The answer would be no. But if the reason was there was a price
24 squeeze regulation, that is taking you no further. I think it's also right --

25 Q. There is a legal question but I'm asking you as an economist, and indeed the same point is true
26 of Mr. Clarkson, but he goes on at great length about the impact of Ofcom's past regulation
27 going back beyond 2005. And you also make similar points about BT's incentives in
28 the past and you do take account of the past regulation. And likewise in relation to
29 the future, we have just looked at two cases where you have looked at the incentive effects
30 on BT taking account of a hypothetical future regulation. That is right, isn't it?

31 A. So in relation to the past, I am making a quite important factual observation which is the
32 suggestion that was put that the fact that BT has not actually price squeezed to date was
33 evidence that it did not have incentives to do that, and the point I was making is actually
34 one reason that influences its conduct in that period may well have been the existence of the

1 fair and reasonable condition implemented in 2010.

2 So I'm not -- it's not a legal observation, it's not an observation about what legally we were
3 supposed to take into account, I am just trying to look at what their actual incentives -- what
4 the actual evidence tells us about what their incentives might be in a world where there
5 weren't regulators.

6 Q. Let's leave the FRAND condition out of it because there has been a debate with Mr. Clarkson
7 already about what exactly the FRAND condition was between June 2014 and March 2015
8 and there may be more argument about that, and Mr. Holmes hasn't said much about
9 greenfield yet but he may yet say something about it, so we don't really know where Ofcom
10 is on that.

11 But in terms of competition law, that has nothing to do with this regime at all. It sits there
12 whatever you decide. Even if you refused even to think about competition law the CMA
13 would still have responsibilities, so that is right out of it.

14 So competition law is there, yes? Do you agree with that?

15 A. Yes, although we were again advised to undertake this assessment assuming that that would
16 not be the constraints because essentially one looks at what the risk is, and the risk it would
17 have adverse effects, and then you go on to look at the appropriate remedies where
18 of course it is proportionate to look at competition law as a constraint.

19 Q. So you were looking at it assuming big bad BT was in a world outside the European Union in
20 some sort of bad lands where there was no competition law of any kind? That is what your
21 report is about?

22 A. Our assessment that there is a real and significant risk assumes no regulation of BT.

23 Q. So the market analysis is based on essentially 19th century pre-antitrust economics?

24 A. It's based on our legal instructions which was that we should not take into account existing
25 regulations --

26 Q. It doesn't really matter why, but just to be clear what it was you thought you were doing?

27 A. No, that's correct.

28 Q. And, likewise, the undertakings which were not part of this regulatory debate at all, they had
29 been in place from 2005 under completely different legislation. Were you instructed to
30 forget about them as well?

31 A. I don't think we were instructed in relation to the undertakings. We didn't think they would
32 constrain BT.

33 Q. That is a different point --

34 A. We took that as -- our market analysis assumes that they won't.

1 Q. I don't think that is right. I think your market analysis ignores them completely, is that not
2 correct?

3 A. The way I would put it is that it assumes that the undertakings are not going to be a constraint
4 on BT's conduct.

5 Q. Let's be precise about that. Is there any reference to them in your report?

6 A. In my report? No ... I don't think so.

7 Q. I think that would be something I would like you to research over the weekend, if there is any
8 reference to them in the decision, final statement.

9 A. Sorry, in my report or in the decision?

10 Q. Both. Can we look at the issue that we were addressing. Can we look first of all at
11 paragraph 18. You say this:

12 "I am advised that Ofcom are not to set an SMP condition imposing a price
13 control except where it appears to Ofcom from the market analysis carried out
14 for the purpose of setting that condition that there is a relevant risk of adverse
15 effects arising from price distortion. I am further advised that, for these
16 purposes, there is a relevant risk of adverse effects arising from price distortion
17 if the dominant provider might so impose a price squeeze as to have adverse
18 consequences for end-users of public electronic communications services.
19 Accordingly, the market analysis in the [final statement] assesses whether there
20 is such a relevant risk of adverse effects arising from price distortions."

21 Are you happy with that?

22 A. Yes.

23 Q. Now, I would say that was an excellent summation of what you were supposed to be doing.
24 Indeed, it is basically a paraphrase of the statutory language. But there is nothing there
25 about moving outside the European Union or the undertakings and looking at some form of
26 BT not subject to any regulation. There is no reference to that, is there?

27 A. No. There is no reference to other forms of regulation, no.

28 Q. Whereas, when we look at what you actually did, one finds that at paragraph 9. I imagine it is
29 particularly the first three sentences. You say:

30 "In this statement I explain why, absent regulation, there would be a relevant
31 risk of adverse effects from a price distortion in respect of VULA. Absent
32 regulation there is a real and significant risk that BT would have incentive to set
33 the VULA price in a way that favours BT's downstream retail business,
34 including through implementing a price squeeze."

1 Then you say:

2 "If BT did implement a price squeeze, there would be a risk that downstream
3 competition would be dampened with consequent adverse effects on customers."

4 I assume that was drafted fairly carefully, is that correct?

5 A. I would like to think my report is drafted carefully.

6 Q. What I see is that the third sentence doesn't include the words "absent regulation", does it? It's
7 a finding about potential risk?

8 A. It doesn't include those words, no.

9 Q. The first sentence says:

10 "Absent regulation, there would be a relevant risk of adverse effects ..."

11 Do you see that?

12 A. Yes.

13 Q. And so what you seem to be saying is -- well, you don't make any finding about what the
14 position would be, as it were, in the real world, you only make it absent regulation, is that
15 right?

16 A. Yes, that is correct. We assume no regulation.

17 Q. Yes, and in the second sentence, it's a slightly curious formulation. You say:

18 "Absent regulation, there is a real and significant risk that BT would ..."

19 But, again, I think that is not saying there actually is one, but, if there wasn't regulation,
20 there would be one. Is that right?

21 A. We -- I think I have given my answer several times. We assumed no regulation when we
22 undertook this analysis.

23 Q. No present regulation, because we have seen in your report that you do hypothesise about
24 future and you certainly rely on past?

25 A. Yes, in respect of future regulation, it probably is worth just making one point; one can
26 imagine two scenarios, one which I understand legally may be the right assumption, is that
27 one shouldn't assume that BT will ever be subject to regulation in this area, which you
28 might argue is the right approach under the modified greenfield approach. That is not for
29 me to say. One could take the analysis in that world and then one would conclude, as
30 I think I argue it elsewhere in my report, that, well, in that world BT can always exclude its
31 rivals permanently because it can hold the VULA price at the very high level without ever
32 needing to bring it down. So the particular circumstance that Mr. Bishop discussed where
33 you put a price squeeze for a period but subsequently you bring the VULA price down and
34 rivals could potentially re-enter the market wouldn't arise.

1 So that is one scenario. What I am doing here is just discussing in, as you say, the real
2 world, well, in reality, in the short-run, BT probably will take into account the potential
3 regulatory framework as it goes forward. That is what regulated firms usually do. All I am
4 doing is pointing out that, that being so, if it does take into account those matters, that is
5 likely to tend to lead it to balance the interests of BT Consumer and reduce the balance on
6 Openreach than otherwise would be the case.

7 Q. Yes, but you can't have it both ways; you can't look at the future and say, oh, there are these
8 incentive effects, which is what you do here, and then say, oh, but BT might behave like
9 this and, as it were, ignore all these incentive effects?

10 A. As a matter of uncertain futures, you could have it both. One world is actually they would be
11 able to continue in practice to price squeeze or set the VULA price freely. The other is they
12 may come under regulation at some point. So they are both potential scenarios that one
13 might want to consider if you are going to try and come up with a precise assessment of
14 BT's incentives in this area.

15 MR. THOMPSON: Sir, I don't know how long the Tribunal wants to go on tonight. We are not
16 going to finish Mr. Matthew tonight, but we will certainly finish him on Monday morning.
17 I'm happy to go on for another half an hour or twenty minutes or whatever suits the
18 Tribunal.

19 THE CHAIRMAN: We were going to ask you whether you had any thoughts on the timetable
20 generally.

21 MR. THOMPSON: Mr. Holmes and I had a discussion and, given that, on any view, we will be
22 finished with the evidence by lunchtime on Monday, there then comes a question about how
23 long we should take between that point and closings. I think both Mr. Holmes and I would
24 be grateful for some period to gather our thoughts before we set on. So I think it probably
25 comes down to partly the submissions of counsel and partly the convenience of
26 the Tribunal, obviously the second is more important, as to whether it would help you to
27 hear from us on Wednesday or Tuesday. I'm content with Tuesday. I think Mr. Holmes
28 would slightly prefer Wednesday. But I don't know.

29 MR. HOLMES: Sir, just to complete the picture, Mr. Thompson and I also discussed the length
30 of time required for closing submissions and I think I am right in saying that we think they
31 can be accommodated within a single day in response to the question that you raised with
32 counsel. My own preference, as Mr. Thompson rightly observes, would be to have a little
33 longer to prepare the closing submissions. This case has obviously gone off on a number of
34 tangents and there are a lot of potential false sort of blind alleys down which it could be

1 taken, and having a little extra time might ensure that we separate the wheat from the chaff
2 and can focus in on the issues that are really of importance. So, for that reason, my
3 submission would be that we should stick to the existing timetable, if it suits the Tribunal,
4 have Tuesday as a non-sitting day and come back on Wednesday, but with the aim of
5 concluding during the course of Wednesday. But of course we are in the Tribunal's hands
6 in terms of their availability. (Pause).

7 THE CHAIRMAN: As far as next week is concerned, it seems to us preferable that we should
8 keep Tuesday clear. There is a lot of material to assimilate and it gives us time to gather our
9 thoughts too before the final submissions. If you can conclude the submissions on
10 Wednesday, so much the better. In terms of today, if we are not going to finish, we may as
11 well draw stumps at this point.

12 MR. THOMPSON: I did see the time and sometimes on Friday people feel like doing something
13 else. It has been a fairly rigorous week for everyone.
14 So I think the only reservation is a fairly obvious one; that I'm the most likely person to be
15 prejudiced by this on Wednesday at this sort of time, if Mr. Holmes comes out with a lot of
16 fast bowling unexpectedly on Wednesday afternoon. So I think it must raise the possibility
17 of having some sort of submission at about this time that we should come back on Thursday
18 for reply.

19 THE CHAIRMAN: We will keep Thursday free in case that is necessary.

20 MR. THOMPSON: Obviously if we can finish on Wednesday we can all start Christmas early.

21 (4.05 pm)

22 (The hearing adjourned until 10.30 am on Monday, 14th December 2015)

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