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[redacted pages 1-107](Public session)

THE CHAIRMAN: I see we have reverted to more orthodox arrangements.

Dr Padilla, you are over there. You are still under oath, I don't have to remind you.

Whose witness is Dr Padilla? I keep forgetting.

Examination-in-chief by MR BEARD

MR BEARD: Dr Padilla is our witness, yes. Obviously we are in a situation where to some extent the swearing in of the witness has been done and he's got four reports in the bundles. I'm happy to go through them and confirm that they are his reports if the tribunal would like me to do so.

THE CHAIRMAN: I think you can do that very briefly. Not

1 perhaps the two we discussed this morning, but the two
2 we're going to discuss this afternoon, his 1 and 3.

3 MR BEARD: Yes, 1 and 3 I was going to take him to.

4 If we could have bundle N2, please. Dr Padilla,
5 could you turn to tab I in that bundle? There is
6 a document entitled:

7 "Evolution of competition in pay TV and its
8 implications for the assessment of Ofcom's decision to
9 remove the WMO obligation."

10 Is this your first report, Dr Padilla?

11 A. It is.

12 Q. Do you have any corrections to make in relation to it?

13 A. No, I don't.

14 Q. Thank you. Could you be passed bundle R, please? If
15 you go to tab G in that bundle, do you have a report
16 there "Response to Sky's factual evidence in relation to
17 the evolution of competition in pay TV."

18 A. I do.

19 Q. Is that your third report, Dr Padilla?

20 A. Yes, it is.

21 Q. Do you have any corrections to make in relation to it?

22 A. No, I don't.

23 MR BEARD: I don't have any questions for you, Dr Padilla,

24 I believe Mr Pickford and Mr Holmes may do.

25 Can I also make the point that if at any point

1 material you want to refer to has been marked
2 confidential in any part of any documents or indeed your
3 reports and you want to advert to that confidential
4 information, it would be perhaps sensible to indicate
5 that before you make any statements, in case there are
6 people within the room who shouldn't be here to hear it.

7 A. Noted.

8 THE CHAIRMAN: Sorry to keep quibbling, Mr Pickford.

9 Mr Holmes would normally be next. Does Mr Holmes not
10 want to say anything?

11 MR HOLMES: Yes, sir. Mr Pickford and I have liaised in
12 advance of cross-examination. We have decided, to avoid
13 duplication, that a sensible division of labour would be
14 for him to focus on the cross-examination of Dr Padilla
15 and I shall take the lead in the cross-examination of
16 Mr Harman on Monday. That's not to say, of course, that
17 I may not have some supplemental questions, but it seems
18 sensible to avoid re-inventing the wheel and covering
19 the same ground. So on that basis --

20 THE CHAIRMAN: That's fine. It sounds like a division of
21 labour to me.

22 MR HOLMES: Yes.

23 THE CHAIRMAN: Fine. We have also reflected over lunch,
24 Mr Pickford -- please, the court is yours -- but I think
25 we regard the issue of the modelling, the status and

1 validity and utility of the modelling exercise to be
2 done with, okay? So we would like you to talk to
3 Dr Padilla on his other evidence.

4 MR PICKFORD: That is understood, sir.

5 THE CHAIRMAN: I think that is out of procedural efficiency
6 and residual fairness.

7 MR PICKFORD: That is understood, sir.

8 The first topic I wanted to address concerns a paper
9 which Dr Caffarra did not look at, which is the discrete
10 choice analysis. I wanted to draw some implications
11 from that.

12 THE CHAIRMAN: That is still in the modelling box, I'm
13 sorry.

14 MR PICKFORD: Right.

15 THE CHAIRMAN: Right.

16 MR PICKFORD: It was not a topic which was canvassed at all,
17 and it was something that we did --

18 THE CHAIRMAN: But Dr Caffarra is not here, and we have had
19 a joint judge-led examination on the issue of the
20 validity and utility of the modelling exercise carried
21 out by Dr Padilla. You have asked questions and we
22 understand the issues now. We really don't need any
23 more. I don't think you are going to further your
24 point, put it that way.

25 MR PICKFORD: So just to clarify, I understand, sir, what

1 you are telling me. Just so I'm clear what I wanted to
2 ask about so there is no misunderstanding. It was not
3 to retrace our steps in relation to any of the matters
4 that we considered today. It was to examine the
5 plausibility of some of the assumptions made in that
6 choice analysis which was not something that we
7 considered. As long as I'm clear about that, and the
8 tribunal is telling me that you don't want to hear
9 about it, I understand, but I want to be clear what it
10 is I want to ask about.

11 THE CHAIRMAN: We would like to move on to the subject
12 matter of this afternoon's session.

13 MR PICKFORD: I'm grateful, sir. In that case, I can invite
14 my clients back into the room, because that was BT
15 confidential, but --

16 THE CHAIRMAN: We are still in BT/Sky confidential? The
17 room looks rather bare to me.

18 MR BEARD: Yes, I think we are, probably.

19 THE CHAIRMAN: I was just assuming that people were losing
20 interest.

21 MR BEARD: There is a queue outside.

22 THE CHAIRMAN: They don't know what they are missing.

23 MR BEARD: They don't.

24 THE CHAIRMAN: Just to be clear, we are now in open court.
25 Is that right, Mr Pickford?

1 MR PICKFORD: We can be in open court.

2 THE CHAIRMAN: This is an expert witness.

3 MR PICKFORD: There will be some moments at which it is
4 necessary for BT briefly to leave. There will be some
5 moments at which it is necessary for both of our
6 respective clients to leave, because we cover things
7 like market share, et cetera, but generally I think we
8 can proceed in open court. Although, generally, we have
9 also adopted a policy, given that there is no one, as
10 I understand it, who is not BT and Sky here on many of
11 the matters that we consider are not certainly
12 confidential as against either BT and Sky, that we
13 proceed on a BT/Sky confidentiality approach which is
14 what we did this morning.

15 THE CHAIRMAN: I would rather we proceed with everybody
16 here. If we start to -- we have to get into grounds
17 where people have to leave, then we will take a view
18 then. This is expert evidence, not, I hesitate to say,
19 the real world.

20 MR PICKFORD: It is, sir. There are some respects in which,
21 obviously, Dr Padilla does trespass into the real world
22 later on.

23 THE CHAIRMAN: I am sure you will point those out when you
24 get to them.

25 Cross-examination by MR PICKFORD

1 MR PICKFORD: In that case, I think, if we may, we'll start
2 with the issue of incentives, and the vicious circle.

3 I would like to very briefly go over in terms what
4 you say in your report about Sky's incentives, and talk
5 about the vicious circle, and we will have a chance to
6 look at areas in more detail, but the purpose of this
7 preliminary session is just to contextualise the
8 questions that will follow so that everyone is clear.

9 If you go, please, to your first report which you
10 will find in bundle N2, tab 5. Do you have that?

11 A. Yes.

12 Q. If you turn to page 3, please, and paragraph 2.8. You
13 will see that you say there:

14 "My assessment is that the vicious circle which
15 underpinned Ofcom's conclusion that led to the
16 introduction of the WMO in 2010 remains today."

17 Do you see that?

18 A. That's in the middle of the paragraph, is it?

19 Q. Yes.

20 A. Yes.

21 Q. Yes. It is correct, isn't it, that Ofcom, itself, never
22 refers in terms to the "vicious circle"?

23 A. In the 2010 statement?

24 Q. Correct.

25 A. I don't recall. I think that it may be my way of

1 summarising their theory --

2 Q. Quite. Your point is that you say Ofcom in 2010 was
3 guided by a particular theory, and it is the theory that
4 is summarised in paragraph 2.10. The WMO was required
5 to prevent a vicious circle which Mr Petter correctly
6 summarises in layman's terms as follows:

7 "By limiting the distribution of its Sky Sport's
8 proposition, either by not providing access at all or by
9 providing access only on terms that ... competition, Sky
10 was able to prevent other pay TV retailers from growing
11 their own premium sports subscriber base and to
12 establish ... sports channels over time, thereby
13 limiting their ability to channel the live sports rights
14 in the future."

15 A. I think that is correct. And I seem to recall that
16 Ofcom used to refer to it in the 2010 statement as the
17 strategic incentive.

18 Q. Yes. You say that this was central to Ofcom's 2010
19 decision?

20 A. In 2010, I believe so.

21 Q. You reference in footnote 2 there, the passage in the
22 2010 decision that you are referring to. It is in fact
23 an appendix 4, annex 8, of the 2010 pay TV statement.

24 A. That's the reference (inaudible), yes.

25 Q. Your view is that the vicious circle obviously remains

1 today. That's what you say?

2 A. That's what I said, yes.

3 Q. Now, back in 2011, you also endorsed the theory of the
4 vicious circle because you wrote an expert report on
5 behalf of BT for the 2011 proceedings saying as much?

6 A. That's correct.

7 Q. Now, I want, perhaps ambitiously, to see whether I can
8 spare everyone quite a lot of time and pain and
9 short-circuit what may otherwise be a somewhat longer
10 cross-examination, there was some evidence that you may
11 not have been aware of before that was given by
12 Mr Petter on Wednesday. I would like to see what your
13 reaction is to it, whether you consider that it
14 potentially changes your views.

15 [redacted]xx
16 xxx
17 xxx
18 xxx

19 A. So, I had access to the transcripts and I read bits and
20 pieces of it, but I have not read any transcript in that
21 detail to be able to recall every statement. I'm
22 prepared to accept what you are telling me.

23 Q. Okay. We will assume for the sake of these questions,
24 the transcript -- sorry, I heard a cough from Mr Beard.
25 Would you like to take the witness through the

1 transcript? I am very happy to do so.

2 MR BEARD: I think there is a danger of proceeding on the
3 basis of assumptions in relation to other people's
4 evidence in relation to these matters.

5 THE CHAIRMAN: My approach to this would be that you can
6 take what Mr Petter said -- we have to assess that,
7 obviously -- and you can put that as a question which is
8 based on that assumption. But what you can't do is ask
9 Dr Padilla to say whether or not Mr Petter was right.

10 MR PICKFORD: No, indeed, I was not --

11 THE CHAIRMAN: Okay? Not even by implication.

12 MR PICKFORD: That was not the purpose of my question, sir.

13 THE CHAIRMAN: I was not quite sure where the
14 short-circuiting comes in.

15 MR PICKFORD: Hopefully, all will be revealed.

16 THE CHAIRMAN: Okay. Fine.

17 MR PICKFORD: At page 129, do you have -- I'm going to
18 summarise the point. If Mr Beard considers that I've
19 summarised it incorrectly, then he can object.

20 THE CHAIRMAN: I don't think you should be putting
21 transcript evidence from an earlier day in the
22 proceedings to an expert witness.

23 MR PICKFORD: I don't understand --

24 THE CHAIRMAN: He was not necessarily in court to hear it,
25 and you are asking him to absorb it on the hoof, as it

1 were.

2 MR PICKFORD: I am, sir.

3 THE CHAIRMAN: Put the question as a question.

4 MR PICKFORD: Sir, I do contend it is admissible for me to

5 put factual evidence that has -- the point being that we

6 had the factual evidence before the expert evidence that

7 has been heard, in order to elicit the expert's views on

8 that actual evidence.

9 THE CHAIRMAN: He doesn't have the transcript in front of

10 him.

11 MR PICKFORD: Is that correct?

12 THE CHAIRMAN: If we are talking about aids to reading, that

13 is fine.

14 MR PICKFORD: If the transcript could be provided. I am

15 hoping it shouldn't be too controversial when we

16 actually get there. (Handed).

17 Dr Padilla, if you could please take up the

18 transcript bundle for Day 3, do you have that?

19 A. I don't know. I have a bundle. Okay. Tab 3. Okay.

20 Q. Thank you. And turn through tab 3, please, to page 128.

21 A. I am there.

22 Q. Thank you. About two-thirds of the way down page 128,

23 we have a question from -- this was Mr Holmes -- to

24 Mr Petter, and he says:

25 [redacted] xx

1 BT and prevent it from doing that, by refusing to supply
2 the core premium sports channels. That is the vicious
3 circle, isn't it?

4 A. Let's unpack the vicious circle model. What the vicious
5 circle model says is the chances of winning in an
6 auction for content are a function of the size of your
7 subscriber base, for a number of reasons that we didn't
8 discuss this morning and I'm not going to elaborate, but
9 perhaps I will be taken there later.

10 So what it says is that the greater your subscriber
11 base, the more likely you are to win. The smaller you
12 are, the less likely you are to win, and if you don't
13 have the content, then the more likely it is that you
14 won't be an effective competitor and, if you are not an
15 effective competitor, you are not going to be able to
16 grow your subscriber base and that is going to generate
17 a vicious circle. So the vicious circle itself has
18 nothing to do with whether Sky wants to wholesale or
19 not.

20 The second part of the theory says, because there is
21 this vicious circle -- which is what I say that remains
22 today. Because there is this vicious circle, you know,
23 you can see that Sky may have no incentives to wholesale
24 as a way of limiting the subscriber base of BT and
25 therefore undermining its chances of winning.

1 Q. But the implication of your vicious circle theory is
2 that, because Sky understands this, that's why Sky is
3 withholding its content, because it fears that BT will
4 become more powerful if it gets the prime content. That
5 is correct, isn't it?

6 A. Yes, that is correct.

7 [redacted] #####
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2 A. First, I think that, as Mr Chairman said,

3 [redacted] #####

4 #####

5 #####

6 #####

7 #####-- I am an expert witness, I have

8 looked at the market, I believe that the market is

9 characterised by a vicious circle. I believe that I'm

10 not the only one that sees that vicious circle in

11 operation, call it one way or the other, read the 2015

12 Ofcom statement, and I think that the logic of it is

13 that there is an incentive not to wholesale in order to

14 make sure that the advantage that Sky currently enjoys

15 in bidding for content remains.

16 Q. Okay. We will move on to another aspect of Mr Petter's

17 evidence whilst we are there. There is just one other

18 and then we can move on to some other questions. He

19 also said -- page 150 of the transcript, but I can

20 simply quote it to you:

21 [redacted]#####

22 #####

23 #####

24 #####

25 A. Mr Pickford, I would really appreciate if you could

1 point me to the particular paragraph so I have time to
2 read it and consider your question.

3 Q. I completely understand. Go, please, to page 150.

4 A. Thank you.

5 Q. Towards the bottom of that page -- on mine it is
6 line 22.

7 A. Thank you.

8 Q. This is Mr Petter answering a question from the chairman
9 at this point:

10 [redacted]#####
11 #####
12 #####
13 #####

14 That is then picked up in that exchange with
15 Professor Mayer just a few moments later. If you then
16 look at page 154 of the transcript?

17 A. Thank you.

18 Q. Professor Mayer says at line 11 of mine:

19 [redacted]#####
20 #####
21 #####
22 #####
23 #####
24 #####

25 Okay?

1 A. I read that, but I must say that I miss the context when
2 [redacted]#####
3 #####
4 #####
5 #####

6 A. Well, in my understanding of the vicious circle, what
7 matters for BT's chances of winning the content auction
8 is what is the number of subscribers it has access to.
9 It doesn't matter whether those subscribers are based on
10 the BT TV platform or they are based on the DSat
11 platform. [redacted] #####
12 ##### but for the sake of clarity, you
13 know, for me, BT's chances of winning in the content
14 auction are driven by their subscriber base, that
15 includes -- that includes -- subscribers in the DSat
16 platform.

17 THE CHAIRMAN: We have been asked to be very careful about
18 the distinction between subscribers and customers. You
19 do mean subscribers?

20 A. I do mean subscribers.

21 THE CHAIRMAN: Who pay a monthly subscription?

22 A. Correct. I think the reason why I particularly like
23 that terminology is because, for the vicious circle
24 theory, it is important that we are talking about
25 subscribers that are in a sense committed to that

1 provider. That they are -- you know, accessible, that
2 they are regular -- they have a regular relationship
3 with the platform provider. Or the self-retailer.

4 Q. If we can pick up bundle G1, please.

5 THE CHAIRMAN: Have you finished with the transcript?

6 MR PICKFORD: I have, thank you, sir. I am still on the
7 same topic, but I am moving off. We have seen enough of
8 the transcript.

9 Go, please, to tab 19, page 40.

10 A. Which?

11 Q. G1, tab 19. G1, tab 19, is the report that you authored
12 with Mr Dryden, revised on 30 April 2014, entitled
13 "Modelling static and dynamic competition in the retail
14 CPSC market."

15 A. So this is one of the reports --

16 Q. It is one of your earlier reports on which your evidence
17 in these proceedings --

18 A. -- discussed by Cristina Caffarra?

19 Q. This is a report that contains the details of the
20 vicious circle model, isn't it?

21 A. It is one of the many reports that we produced that
22 contains dynamic models, yes.

23 Q. In this particular case, it is the report that deals
24 with the vicious circle model that we have just been
25 discussing, as opposed, for instance, to the investment

1 in technology dynamic model, which we also discussed
2 this morning, but that is not addressed in this report?

3 A. I believe it is also addressed in this report, in
4 page 36 [redacted].

5 Q. I beg your pardon. At any rate, the point I'm going to
6 is [redacted] that begins on page 39.

7 You see at paragraph 5.17, you set out the key five
8 assumptions on which the model relies.

9 A. That's correct.

10 Q. The first of those is:

11 [redacted]#####
12 #####
13 #####
14 #####

15 So it has two choices: retail on its own platform or
16 wholesale to the rival?

17 A. [redacted]#####
18 #####
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14 A. No, Mr Pickford, I think that you are misunderstanding
15 the logic. The point is not about platforms. The point
16 is about subscribers. The point is about having -- the
17 vicious circle theory is about companies that are
18 potential bidders for content having the incentive,
19 having the desire, to build a subscriber base, to build
20 relationships with customers so that, as soon as they
21 win content, they can start monetising that content as
22 opposed to having to spend time to build that subscriber
23 base, time that is wasted, time that is important
24 because these content rights are perishable.

25 Sorry, I think that my English was not very good.

1 Perishable. They die in three years.

2 THE CHAIRMAN: Liable to die in three years.

3 MR PICKFORD: Dr Padilla, I am struck that something that in
4 your client's view is critical as to how the dynamics of
5 the market, which is the availability to self-retail in
6 DTH, is something that you are only now in evidence
7 explaining how it works in the model. It is surprising
8 that you did not seek to elucidate that in your model
9 originally.

10 A. No, I think the logic of the model has always been the
11 same. I think that the logic of the model is the logic
12 that I am putting forward. What Sky can control through
13 its decision of whether or not to grant access to SS1
14 and SS2, is BT's ability to increase its subscriber base
15 on its own platform. But I have never said and, you
16 know, I think that I have never said, that BT would not
17 count on its DTH subscribers as a source of revenue when
18 calculating or when considering how much to bid in the
19 next content auction. So I'm prepared to admit that
20 perhaps, when dealing with this complex model,
21 I simplified and I should have -- like I did in the
22 static model and the self-retailing option, I'm prepared
23 to admit that, but what I cannot admit, because it would
24 be wrong, is to say that including that option
25 fundamentally changes the logic or the results of the

1 model that I presented, because it wouldn't.

2 Q. I think I have put my point on that. I'm not going to
3 deliberate it further.

4 Part of the reasoning that we canvassed at the
5 beginning was you saying that nothing has really changed
6 since 2010, so I would like to start now by going back
7 to the 2010 decision. So I can be very clear to
8 the tribunal, this is not re-litigating 2010, but it is
9 obviously an important part of the context of
10 Dr Padilla's evidence. He says this was the world in
11 2010, this is what it looked like, nothing has changed,
12 therefore the results are the same, and so he chose
13 those steps.

14 THE CHAIRMAN: We can't re-litigate the 2010 decision,
15 Mr Pickford.

16 MR PICKFORD: I know. I was just putting the tribunal at
17 ease, I hope.

18 So the 2010 decision, if we could see firstly what
19 you say about it and then we will come on to the
20 decision. If we go back to your first report which is
21 in bundle N2, tab I, and we go to paragraph 3.2 and
22 following.

23 A. Excuse me, Mr Pickford, which paragraph?

24 Q. Paragraph 3.2. So here in this section of your
25 report -- we don't need to read all of it, but just

1 again for context so we know where we are going, 3.2,
2 you are going through the 2010 statement and setting out
3 your understanding and reasoning in it from 3.2 and
4 following. Yes?

5 A. Yes.

6 Q. Then at 3.10, we come to the critical part: you say,
7 under the title:

8 "Sky is acting on those incentives in limiting
9 distribution of its essential sports channels". Ofcom
10 identified two ways in which Sky limited the
11 distribution of its sports channels: the first was that
12 it withheld supply of its channels; the second was that
13 it wholesaled its channels only on terms that would not
14 allow rival retailers to be an effective competitor.
15 Ofcom therefore found that Sky ... incentive to restrict
16 wholesale supply of its channels. Furthermore, Ofcom
17 concluded that Sky exploited market power ... with the
18 effect of restricting competition from retailers and
19 other platforms. This is prejudicial to fair and
20 effective competition, reducing consumer choice and
21 holding back innovation by companies other than Sky."

22 So just to deconstruct that, there are two issues
23 that you are referring to here, aren't there? First,
24 there are some companies like BT and others who didn't
25 have supply at all?

1 A. Correct. Here, I'm quoting from the 2010 statement. So
2 these are not my assertions. These are quotes from the
3 2010 statement by Ofcom.

4 Q. Yes.

5 A. In inverted commas.

6 Q. Then there was a second aspect, that Virgin did have
7 supply but on terms that Ofcom thought did not allow it
8 to compete.

9 A. Again, these, I am quoting Ofcom, yes.

10 Q. I'm assuming you have chosen to quote these parts
11 because that's what you understand is the essence of
12 Ofcom's reasoning?

13 A. Yes. I think that I described that Ofcom's reasoning
14 was structured in one, two, three, four, five steps, and
15 then I was trying to see whether, you know, the 2015
16 statement, what the 2015 statement had said about each
17 of these five steps, to see whether there was
18 a discrepancy between the logic in the 2015 and in the
19 2010 statements.

20 Q. So let's go and pick up briefly the 2010 statement
21 itself, then and set the background. If we could go,
22 please, that's at G1/1, page 318.

23 A. Which paragraph?

24 Q. Paragraphs 7.1 and 7.2. Here we see again at 7.1:
25 "Our key concerns about restriction of supply ..."

1 Then 7.2:

2 "We also have concerns about the terms of Sky's
3 supply to Virgin, its high prices and restrictive
4 exploitation ..."

5 A. That's correct.

6 Q. So, finally, I apologise that there is a certain amount
7 of context setting to this, but we do then get into the
8 core of it. If we could then please turn to the 2012
9 judgment, which is the next step in terms of what
10 happened along the regulatory way. You will find that
11 in -- I think it made it into the bundles in two places,
12 I am afraid. I am using AB1, tab 4, but I think it is
13 also at H1, tab 5. I'm not quite sure which the
14 tribunal has been --

15 MS POTTER: Mr Pickford, are we going to need the pay TV
16 statement again?

17 MR PICKFORD: I think we can probably put it to one side,
18 thank you. It depends obviously a little bit on some of
19 the answers, but yes, for the time being.

20 So, Dr Padilla, do you have the 2012 judgment?

21 A. I do.

22 Q. If you could go, please, firstly to -- we see at
23 paragraph 22, the tribunal recording the essential
24 theory that it is dealing with, which is the one that
25 I have just taken you to.

1 A. I think that you need to direct me to the tab, because
2 I realise that the tab that I have --

3 Q. I beg your pardon. Tab 4. It depends which bundle you
4 are in. Are you in bundle AB or are you in bundle H?

5 A. I'm in bundle AB, additional bundle.

6 Q. Okay. I am hoping -- but I'm seeing --

7 MR BEARD: I think it is authorities bundle. When you say
8 "AB", do you mean authorities bundle?

9 MS POTTER: We just have an extract from the judgment but
10 not the full text, is that right?

11 MR PICKFORD: In which case we will go to H1/5 and stick
12 with that reference.

13 A. Thank you. And tab number 5?

14 Q. Tab 5.

15 A. Correct.

16 Q. So if you go, please, very briefly we see paragraph 22,
17 the tribunal summarising what it is concerned with,
18 which is again referring back to the paragraphs in
19 effect that we looked at in the 2010 decision. Then it
20 goes on, at paragraphs 27 through to 31, to set out its
21 conclusions in relation to Ofcom's core competition
22 concerns?

23 A. Sorry, what is it in 22? I think you are going a little
24 bit too fast for me.

25 Q. I beg your pardon. If we go on to 27 --

1 A. But do you want me to read 22?

2 Q. I was simply giving it to you out of fairness, so you
3 saw the context of what the tribunal was going on to
4 address. By all means, please read it.

5 A. Thank you very much.

6 Q. It is simply context.

7 A. Okay, I have read 22.

8 Q. Then the tribunal sets out its conclusions at paragraphs
9 27 through to 31 in relation to the issue of restricting
10 supply.

11 Now, I'm going to summarise what I say the tribunal
12 says. By all means, if you wish, you can look at these
13 paragraphs.

14 But in essence, if we see whether we can agree on
15 this, you are aware that what the tribunal said is that
16 contrary to Ofcom's belief that Sky was holding back
17 supply for its own nefarious reasons, in fact the reason
18 why we didn't see any deals in the market was because
19 the counterparties were not as constructive as they
20 might have been and that included BT, which the tribunal
21 made findings had engaged to some extent in some
22 regulatory gaming with a view to avoiding actually
23 reaching a judgment -- sorry, with a view to avoiding
24 reaching a deal. Are you aware of that finding by
25 the tribunal?

1 A. I think so.

2 Q. Now, you don't recognise at any point in your report
3 that key finding by the tribunal in 2012 about the
4 restricted supply of Sky in relation to its CPSCs.
5 Having been set aside by the tribunal?

6 A. No, I don't. And the reason is that in my opinion --
7 and I can explain in greater detail later -- in my
8 opinion that ruling doesn't contradict the existence of
9 the vicious circle.

10 Q. Okay. We will explore that in some more detail. Let's
11 look at what actually happens to the strategic
12 incentives theory. If we go on just a couple of
13 paragraphs in the judgment, if we go to paragraph 37,
14 this is what the tribunal say about strategic
15 incentives, which is in essence the vicious circle
16 theory by another name. Do you understand that?

17 A. I do understand.

18 Q. "Given these conclusions, there is no need for
19 the tribunal to resolve the issues debated before us at
20 some length as to the plausibility or otherwise, as a
21 matter of economic theory, of the alleged strategic
22 incentives on which Sky was said by Ofcom to be acting
23 in its conduct of commercial negotiations. Ofcom's
24 position at the hearing was that its findings relating
25 to the strategic incentives were not essential to the

1 existence of its core competition concern, but that the
2 fact of Sky's acting on these incentives would be
3 revealed when we looked at the empirical evidence of
4 Sky's conduct. However, having examined that evidence
5 with some care, we formed the clear view that Sky was
6 acting for ordinary profit revenue maximising commercial
7 motives and that it cannot reasonably be inferred from
8 the material before us that the alleged incentives were
9 conditioning Sky's conduct."

10 Now, surely that reasoning is correct, isn't it?
11 And therefore, in the light of the tribunal's finding,
12 that causes some problems for whether the vicious circle
13 theory actually tells us anything?

14 A. Well, whether it is correct or not is not for me to
15 decide. There were other instances in this country that
16 would be able to adjudicate on that, but certainly an
17 economist is not capable of doing that.

18 But let's assume that is correct and I have no
19 reason to disagree with the court ruling and their
20 factual investigation. Let us think about what is the
21 implication of that for the existence or not of the
22 vicious circle, for everyone, of the strategic incentive
23 theory. I am afraid I'm going to have to go back to
24 that point in time to particularly characterise or to
25 describe what was the debate, economic debate, at the

1 time.

2 Ofcom, Sky and, so far as I recall, BT did not
3 challenge, certainly I didn't write about, accepted that
4 Sky had static incentives to wholesale. I took no
5 position about whether they were right or wrong, but
6 there was agreement at least between Ofcom and Sky that
7 there were static incentives to wholesale.

8 At the same time, there was no agreement. There was
9 no wholesaling. Ofcom had put forward a theory to
10 rationalise why there was no agreement, and that was the
11 strategic incentive theory which was criticised by Sky's
12 economists as being not cogent and internally
13 inconsistent. My contribution was to elaborate and
14 describe and formalise the strategic incentive theory to
15 show that indeed it was cogent and internally consistent
16 and that, you know, it was a valid theory.

17 The question, however, was, those strategic
18 incentives or dynamic incentives, is that vicious circle
19 strong enough to offset the static incentives to
20 wholesale or not? And there were two positions. One
21 that is the one that I defended, which was that there
22 were reasons to believe that the dynamic incentives were
23 stronger, the dynamic incentives to foreclose or not to
24 wholesale were stronger, more important, more
25 significant, than the static incentives to supply. And

1 there was another alternative theory which was that the
2 reason why we were not observing supply was not because
3 dynamic incentives were greater than the static
4 incentives, but because there was an instance of
5 regulatory gaming. Because of regulatory gaming, static
6 incentives were greater than dynamic incentives, but
7 there were reasons outside all these models that
8 explained what had happened.

9 My understanding is that the court went and accepted
10 the second explanation but not the former. That means
11 what is the logical implication of that? The logical
12 implication of that is that the court considers that
13 either there were no dynamic incentives, no strategic
14 incentives, but it is perfectly consistent with the
15 Court ruling as well that it concluded that the static
16 incentives were greater than the dynamic incentives and
17 that the way to read the evidence was in that way and
18 explain the lack of supply, or blame the lack of supply,
19 or attribute the lack of supply to BT as opposed to Sky.
20 And that's why I mentioned to you before, Mr Pickford
21 that I think that the ruling does not tell me whether or
22 not the vicious circle is valid because this ruling is
23 perfectly consistent with a situation in which Sky was
24 a willing licensee because its static incentives were
25 greater than its dynamic incentives and that's it. But

1 the ruling does not imply logically or otherwise that
2 there were no dynamic incentives, and that's my
3 interpretation of the ruling and its implications.

4 Q. I think we can agree, Dr Padilla, that certainly it was
5 never suggested, I think by Sky in those proceedings,
6 that there could be no dynamic model at all. The whole
7 question in those proceedings -- indeed, we debated this
8 at some length between us before --

9 A. Indeed.

10 Q. -- is whether the dynamic incentives outweighed the
11 static incentives. It was agreed that there were static
12 incentives to supply and the question was you had
13 developed a dynamic model and were the incentives that
14 you saw in that model sufficiently strong to outweigh
15 the static incentives. That was the essence of the
16 debate?

17 A. That's what we debated.

18 Q. Yes?

19 A. And what I'm telling you is that the ruling has no
20 implications for whether or not there are dynamic
21 incentives and I think that is precisely what
22 paragraph 37 of this ruling says:

23 "... there is no need for the tribunal to resolve
24 the issues debated before us at some length as to the
25 plausibility or otherwise, as a matter of economic

1 theory, of the alleged strategic incentives on which Sky
2 was said by Ofcom ..."

3 They did not need to decide whether the vicious
4 circle was correct or not, because what they concluded
5 is that what had happened, or the reason for why there
6 was no supply, was BT playing strategically a regulatory
7 game and that, therefore, there was nothing else to
8 rationalise.

9 All that I'm telling you is that that is what the
10 ruling implies and, as a matter of economics, I thought
11 in 2010 that there was a vicious circle, and I think
12 that in 2015 there was a vicious circle, and I think
13 that there is a vicious circle and, by the way, I think
14 that the logic of the vicious circle is not country
15 specific. I don't think it is even specific to the UK.
16 I think it is an inherent property of the way that these
17 markets work all throughout the world.

18 Q. There is a very important distinction here which I do
19 think we need to get clear, which is that there is
20 a difference between whether the vicious circle theory
21 on its own tells us something or whether the vicious
22 circle theory in combination with the static model tells
23 us something.

24 In particular, the point I'm making is that your
25 evidence was previously that the vicious circle model

1 told us about Sky's behaviour because the dynamic
2 incentives were more powerful than the static incentives
3 and you concluded from that, that because they were more
4 powerful, therefore that explained why Sky was not
5 supplying?

6 A. Correct, that was in 2010.

7 Q. Yes.

8 A. But we are in 2016, and in 2016, we have debated this
9 morning the static incentives not to wholesale. We have
10 developed a series of economic models and we have
11 developed a number of estimations to populate and
12 simulate those economic models and, in the position in
13 which we are now, the question is not whether the
14 dynamic incentives outweigh the static incentives,
15 because we are saying that the static incentives and the
16 dynamic incentives all point in the same direction.

17 THE CHAIRMAN: You are using "we".

18 A. "We", I. Sorry, I think you can take it as a sign of
19 modesty or otherwise.

20 MR PICKFORD: Would you agree with this -- we can go and
21 look at it in more detail -- but we can see whether you
22 agree with it in general terms: when you were analysing
23 the vicious circle theory previously, your model
24 itself -- because we debated this, you said, "Actually,
25 my model on its own, my theoretical model, doesn't

1 really tell you which way you go, because you can
2 calibrate it one way and you discover the incentives are
3 there, and you can calibrate it another way and you
4 discover the incentives are this". So what you said,
5 your previous evidence, was, "I have provided
6 a plausible theoretical explanation, I admit that the
7 model itself doesn't really help us, but what I can tell
8 you helps us is the empirical evidence", and we put the
9 two together and we see the empirical evidence of no
10 supply in conjunction with my theoretical model suggests
11 that I'm right about the direction of my theoretical
12 model. Would you agree with me that is a fair summary
13 of the previous evidence that you gave to this tribunal?
14 A. It is a summary, but it is not very fair. The point is
15 the following. Ofcom and Sky, but let's say Ofcom
16 because it was, after all, what matters, Ofcom had
17 concluded that there were static incentives to supply.
18 And there was no supply. And that generated a puzzle.
19 Why is it that there is no supply if the vertical
20 arithmetic embedded in the static model suggests that
21 there should be supply? The puzzle could be resolved in
22 one of two ways. One was, people are playing regulatory
23 games. We have spoken this morning quite a bit about
24 regulatory games. The other explanation that Ofcom
25 identified was, well, maybe there is something dynamic,

1 strategic, in addition to these static incentives that
2 we are considering.

3 What they did was to formalise the theory that Ofcom
4 had developed, and then we had, indeed, a very lengthy
5 debate as to whether the dynamic incentives that
6 Ofcom had identified and I had formalised, were larger
7 than the static incentives that Ofcom itself had
8 recognised or not. And we had a lengthy debate because
9 the model was very difficult to calibrate and the
10 calibrations were not robust. And you will not be
11 surprised to hear that a group of economists, you know,
12 value certain calibrations pointing one direction more
13 than the other group of economists was thinking that, or
14 arguing that, you know, the right parameter assumptions
15 were different and the calibrations were going in the
16 opposite direction.

17 Because the calibrations were not robust, and
18 I think that we spent quite a bit of time in
19 cross-examination debating this, my position was, well,
20 let's look, there is no supply, I think that if there is
21 no supply, unless you find that indeed there was
22 regulatory gaming, one has to conclude that the dynamic
23 incentives exceed the static incentives.

24 I explained the reasons why at the time and I also
25 clarified, and you can see that in the transcript, based

1 on the limited factual information that I had available
2 that I thought that the explanation was indeed that the
3 dynamic incentives exceeded the static incentives.

4 The court corrected me. The court said that on the
5 basis of the facts, I conclude otherwise, but that
6 conclusion has no implication as to whether or not there
7 was a vicious circle at the time, which I think there
8 was, which I think there is, and which I, as I mentioned
9 before, I think that it is an inherent characteristic of
10 these markets not just in the UK, but also elsewhere.

11 Q. I think we probably disagree on that. But I think
12 I have pursued that sufficiently to put my case to the
13 witness. I don't propose -- I don't think we need to go
14 to the transcript. In fact I'm not clear, Dr Padilla,
15 what aspect of my summary you thought was not fair, but
16 we have your evidence on it and we can move on.

17 Could you, please, pick up in the Sky bundle -- I'm
18 just looking ahead here, we have not reached there yet
19 but there may be a moment during this --

20 THE CHAIRMAN: Are we finished with the judgment?

21 MR PICKFORD: We have, yes. I have put it away myself.

22 I have finished with that one, thank you.

23 We are going to the Sky 1 bundle and just to give
24 an early warning -- I see Mr Beard is very tired --
25 there may be some confidential information that we may

1 get into here, but we have not reached there yet, so I'm
2 giving a pre-warning.

3 THE CHAIRMAN: I was thinking of having a pause at 3.30.
4 How does that fit in?

5 MR PICKFORD: It may, sir. We might get there slightly
6 before that.

7 THE CHAIRMAN: If it is slightly before that, we will pause
8 slightly before that.

9 MR PICKFORD: Thank you.

10 So, if you could please, Dr Padilla, turn to
11 Ms Fyfield's witness statement, which is at tab B of
12 Sky 1.

13 A. Tab B? I'm at tab B.

14 Q. Do you have the witness statement of Rowenna Mai Fyfield
15 there?

16 A. Yes, I do.

17 Q. You are aware, are you not, that she is an extremely
18 high level executive within Sky? She's Sky's chief
19 strategy and commercial officer?

20 A. I'm aware.

21 Q. If there is anyone who would know what Sky's strategy is
22 as regards the distribution of its channels on other
23 platforms in the UK, it would be her?

24 A. I don't disagree with that.

25 Q. So let's see what she says, at paragraph 86, about your

1 theory. She says:

2 "As the person responsible for Sky's strategy for
3 the distribution of Sky Sports channels, I can state
4 categorically that Sky's distribution strategy is not
5 conditioned by concerns that wholesaling Sky Sports to
6 BT for distribution on its ... platform may increase
7 competition for sports rights, nor indeed is this the
8 case in relation to any other platform large or small.
9 This is because Sky does not believe that distribution
10 ... to the particular platform will make the relevant
11 platform operator or retailer a stronger competitor to
12 Sky for sports rights."

13 Now, she could not be clearer, and if she's right,
14 you are wrong?

15 A. If she is -- first, I am not the person that has to say
16 whether she is right or wrong.

17 Q. No, I appreciate that. My question is posed that if she
18 is right in how she approaches things, your theory just
19 does not match the real world?

20 A. No, that is a non sequitur. That is not correct.

21 Q. Just to be clear, are you saying that the chief strategy
22 and commercial officer at Sky does not understand what
23 Sky's own commercial strategy is?

24 A. No, I'm reading what she says. She says:

25 "I can state categorically that the Sky's

1 distribution strategy is not conditioned by concerns
2 that wholesaling Sky Sports to BT for distribution on
3 its YouView platform may increase competition for sports
4 rights."

5 That doesn't undermine the vicious circle. What she
6 is saying is that she is not acting on those incentives,
7 and that may well be true because her actions are
8 conditioned by concerns about regulatory intervention.
9 And I think that that is a very logical concern, one
10 that is identified in Sky's annual report where it talks
11 about potential risks, and how Sky deals with those
12 risks. The annual report of Sky very clearly indicates
13 that they understand that they are subject to regulatory
14 constraints, including competition law and regulatory
15 constraints, and it may well be -- and I have no way to
16 determine exactly what motivates her decision not to act
17 on the vicious circle -- that she is operating under
18 those constraints.

19 But that doesn't tell me that there is no vicious
20 circle, that there are no dynamic incentives, that there
21 is no ability and incentive to operate. It tells me
22 that she is not acting on that ability or acting on
23 those incentives.

24 Q. Absolutely nowhere in her evidence does she suggest that
25 the reason why she's not acting on what you say are

1 incentives is for those regulatory reasons, is there?

2 A. But she's not saying otherwise.

3 Q. Well, she is, Dr Padilla. If you look at the final
4 sentence of paragraph 86, she explains why it is that
5 she doesn't believe in your theory, essentially. She
6 says:

7 "Because Sky does not believe that distribution of
8 its sports channels to a particular platform will make
9 the relevant platform operator or retailer a stronger
10 competitor to Sky for sports rights."

11 A. That's correct.

12 Q. The essence of your theory is that Sky is trying to
13 prevent other retailers, in particular BT, from getting
14 the strength to become a stronger competitor, and she's
15 saying, no, I don't believe that.

16 A. That I find somewhat surprising. Because as I said, the
17 logic of the vicious circle is somewhat trite, that if
18 you are bidding for content, when somebody is bidding
19 for content, it has to do an NPV calculation. It has to
20 think about how much money and profit it is going to
21 make in the three years that it has those rights and
22 compare that with the costs. And one thing that is
23 going to be very important when you are calculating the
24 future cashflows is, when are you going to be able to
25 start monetising those cashflows? And it seems to me

1 pretty obvious that if you have a subscriber base,
2 a subscriber base that is large, the monetising is going
3 to be simpler.

4 Now, it may well be that -- but I think that I'm
5 speculating -- that she thinks that, given the
6 subscriber bases of BT and the other competitors, the
7 impact of wholesaling would be relatively small. But
8 I don't know, I'm in no position to judge. I'm pretty
9 sure that she is sincere in her beliefs, all I'm saying
10 is they do not square with my understanding of how these
11 markets operate.

12 Q. So you are not doubting the sincerity of her beliefs?

13 A. How can I?

14 Q. And you told me earlier that you do not think that she
15 does not understand Sky's business either.

16 A. No, no, I'm not saying that. All that I'm saying is
17 that I'm surprised that the explanation is not
18 regulatory constraints for the reasons that I stated
19 before. Because it seems to me that the logic of the
20 vicious circle is not particularly contrived. It is
21 simply the notion that the more subscribers you have,
22 the easier it is to monetise your investments.

23 I have read her statement and her statement says
24 lots of very interesting and useful things and I think
25 I can learn about the industry by reading her statement.

1 She is saying, you know, that there is value in having
2 access to many customers in order to monetise your
3 investments. That's what the vicious circle is saying.
4 It is saying that the sooner you have access to them,
5 because you have a subscriber base, the sooner you can
6 start monetising and, when you are thinking about
7 content that disappears in three years, time is of the
8 essence and the time to build on a subscriber base is
9 a fundamental drawback.

10 Q. This is the point, isn't it? This goes back to the
11 conversation we had before, because if BT has access to
12 Sky's DTH subscriber base, the whole "time to build
13 a subscriber base" problem is not there. So Sky can't
14 harm BT by denying it access to stop it building up the
15 BT TV proposition because BT can simply get all the
16 subscribers it wants via the DTH platform?

17 A. No, I think that now we are moving from theory to fact.
18 I don't think that that is correct, because I think that
19 in order to win an auction, not only do you have to have
20 a strong subscriber base, you have to have a subscriber
21 base which is similar, closer, not significantly smaller
22 than that of your competitor. What matters is not the
23 absolute size of your subscriber base, what matters is
24 the relative size of your subscriber base.

25 PROFESSOR MAYER: And the nature of the subscriber base?

1 A. And possibly the nature of the subscriber base, but,
2 frankly speaking, in terms of my modelling, it's the
3 number, I haven't complicated the model in that
4 direction.

5 THE CHAIRMAN: I think you are telling us, as I understand
6 it, that actually there is not a lot of difference
7 between a self-retail subscriber customer and an
8 indirect wholesaling customer --

9 A. No, I think the point --

10 THE CHAIRMAN: -- from the point of view of the ability to
11 monetise.

12 A. Excuse me, Mr Chairman, I should not have interrupted.

13 THE CHAIRMAN: Please, no, I had finished. I think I was
14 interrupting you. Go on.

15 A. The point is, what I said is that there is no difference
16 between a subscriber in a DTH platform and a subscriber
17 of BT TV. It is the difference between a subscriber and
18 a customer of BTS which is a subscriber to Sky.

19 THE CHAIRMAN: I have to say -- I am interrupting you now --
20 one of the reasons why I suspect Mr Pickford is
21 hesitating a bit is some of the evidence we've heard
22 earlier would suggest that a [redacted]##### is
23 not so valuable to BT if it is a [redacted]####
24 situation as a subscriber properly put. That idea has
25 been going around.

1 A. That may be what BT thinks, but for the purposes of my
2 analysis, and I'm an independent expert --

3 THE CHAIRMAN: You are an independent expert, thank you.

4 A. -- they are the same in the sense that they are
5 committed customers that you can use to monetise your
6 investment immediately.

7 THE CHAIRMAN: It may be quite significant, I'm not sure.

8 A. The point I was going to make, Mr Chairman, is that we
9 need to come to subscribers. How many subscribers has
10 BT got in the DTH platform? I don't remember from the
11 top of my head, Mr Pickford may correct me.

12 [redacted]

13 MR PICKFORD: I think we can deal with these matters, but we
14 shouldn't be going into --

15 THE CHAIRMAN: Keep the figures out of it.

16 A. I will keep the figures out. Without references to
17 numbers, the point I was going to make is that, even if
18 you count all the subscribers on the DTH platform, the
19 subscriber base of BT is significantly smaller than that
20 of its competitor in the auctions for content, which is
21 Sky.

22 THE CHAIRMAN: I am beginning to agree with Mr Pickford,
23 I think maybe this is a confidential discussion. Shall
24 we pause here for ten minutes?

25 MR PICKFORD: I'm happy with that.

1 THE CHAIRMAN: When we come back, the BT team and Sky
2 team -- unless you want your people to still be here.
3 MR PICKFORD: Sir, I was concerned previously we were going
4 to trespass into some Sky confidential information, but
5 actually, we were also just then trespassing into some
6 of BT's confidential information.
7 THE CHAIRMAN: It is awfully muddling.
8 MR PICKFORD: Perhaps it should be confidential ring only?
9 THE CHAIRMAN: I think it should be confidential ring only
10 while you get this part of your examination out of the
11 way. We will come back in ten minutes.
12 (3.28 pm)
13 (A short break)
14 (3.42 pm)
15 (In camera session)[redacted pages 154-168]
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(Public session)

9

MR PICKFORD: I certainly hope so, sir. I have given

10

extensive thought to (inaudible) to myself anytime I'm

11

about to do something that might be confidential to

12

avoid falling into the traps that I think quite a few

13

people have fallen into so far this week. I can't 100

14

per cent promise --

15

THE CHAIRMAN: Pride cometh before a fall, Mr Pickford.

16

MR PICKFORD: Yes, exactly. It was not so much the pride,

17

it was the warning that I have done my best but I may

18

yet still encounter difficulties.

19

The subject of indirect monetisation. So you say

20

that you extended your vicious circle model to deal with

21

the implications of BT being able to engage in indirect

22

monetisation strategies as well direct monetisation?

23

A. That's correct.

24

Q. And there is a paper which you submitted a couple of

25

weeks after your key paper which you have been currently

1 turning to at tab 19 that explains your model?

2 A. Yes, there is a paper.

3 Q. And that modelling framework allows for the possibility
4 that Sky and BT could indirectly monetise premium sports
5 content by giving it away for free to boost their
6 broadband businesses?

7 A. That's correct.

8 Q. We know, because it is clear from the market, that BT
9 has indeed employed that strategy?

10 A. Yes, indeed.

11 Q. You are not aware from anything that Ms Fyfield has said
12 that Sky has ever employed that strategy, are you?

13 A. I am not aware.

14 Q. You are not aware that Sky actually could employ that
15 strategy, given their market position as a pay TV
16 operator means that their entire brand is associated --
17 or a very important part of their brand I should say --
18 is associated with pay TV and it could therefore be very
19 detrimental to Sky to start giving away pay TV channels?

20 A. I am not aware of them following that strategy.
21 I believe that Sky's strategy is more to give away
22 broadband. But at the same time I think that could
23 they? I think that they could if they differentiated
24 the product that they were giving for free as they are
25 doing by differentiating NOW TV from the product that

1 they sell on their platform.

2 Q. But again, NOW TV is not free. It is not --

3 A. No, no.

4 Q. -- it is not indirect monetisation in that sense?

5 A. All that I was saying was indirect monetisation could
6 make all the difference in the competition for content.
7 That option is available to Sky.

8 Q. Let's assume that I'm correct, that it might actually be
9 problematic for Sky to engage in indirect monetisation
10 that is giving away pay TV for free. If that is correct
11 and that was not available for Sky, again that would
12 make a difference to your model, would it not?

13 Because you assumed equality, that the same options
14 are available for both. But if we make it a strategy
15 that BT could easily employ and it does, and Sky would
16 have some difficulty employing, that would change the
17 dynamics of the model, wouldn't it?

18 A. That would change the dynamics of the model.

19 Q. I would like to look at another topic which is a feature
20 of what you say happens in relation to rights. I don't
21 think any of this is going to be confidential.

22 You say that at the time -- I beg your pardon,
23 I will start again -- at the time of your original
24 report, BT didn't have its own sports channel. That was
25 in 2010?

1 A. Where do I say that?

2 Q. Sorry, you don't. I began my question and it was
3 a badly put question, so I'm putting it again. Erase
4 the previous question and start afresh.

5 At the time of original report, BT did not have its
6 own sports channel?

7 A. That's an assertion.

8 Q. That's an assertion, but it is framing the question that
9 I'm going to address with you.

10 Are you aware that that is true?

11 A. I frankly don't recall.

12 Q. Well, I can say --

13 A. But I take it as an assertion which is a starting point.

14 Q. You can take it from me -- and if Mr Beard wants to tell
15 me I am putting the question on a false premise --
16 BT Sport was launched on 1 August 2013, so it was some
17 time after the initial decision and report that you
18 provided last time around.

19 Now, by comparison, are you aware that Sky -- it
20 doesn't matter about the exact date -- has been in the
21 industry from the early 1990s, so about 25 years, let's
22 say. It really doesn't matter if that is accurate to
23 the year.

24 A. I'm prepared to follow you in that.

25 Q. Now looking at BT, BT currently holds the exclusive

1 rights to the Champions League and that cost BT around
2 about -- again this is public knowledge -- £900 million.
3 You are aware of that?

4 A. Not of the figure, but I understand that it was
5 expensive.

6 Q. And it also currently holds two packs of Premier League
7 rights, again on which it spent the best part of about
8 £1 billion.

9 A. I'm prepared to follow you on that.

10 Q. So on those figures, BT accounts in broad terms for the
11 best part of around £2 billion worth of expenditure in
12 the most recent round of rights for, can we agree, what
13 are the two biggest and most important football
14 competitions on the TV?

15 A. You mean the Premier League?

16 Q. Premier League and --

17 A. -- and the Champions League?

18 Q. -- and the Champions League.

19 A. What I want to say in this respect is that what these
20 rights costs doesn't drive what happens in the
21 marketplace. What happens in the marketplace is what is
22 the value that consumers attribute to those rights.
23 That's what we tested in our choice modelling model: how
24 much these consumers were prepared to pay, or what was
25 the willingness to pay for the BTS product.

1 The choice modelling exercise was conducted before
2 Champions League rights were acquired by BT, and
3 therefore the valuation that we have there doesn't
4 include the value for the Champions League. At the
5 time, the gap between the valuation that was given to
6 BTS by consumers and the valuations for Sky 1 and Sky 2
7 were very, very significant.

8 We don't have valuations so far as I can recall for
9 Champions League. I think that you have to put to BT's
10 experts, BT's business people, whether they think that
11 they would bridge the gap. Based on the information
12 that I have had and the questions that I have asked them
13 and the answers that they have provided to me, I don't
14 think that they bridged the gap. So they may have cost
15 lots of money, but still it appears that the consumers
16 value the proposition that is offered by Sky, SS1 and
17 SS2 let alone SS3, SS4, SS5 and F1, way above what they
18 value BTS.

19 Q. I am sure that is helpful to the tribunal. It was not
20 actually the question I was asking.

21 A. Apologies then.

22 Q. Let's go through the steps --

23 THE CHAIRMAN: You don't always get the answer you asked
24 for.

25 MR PICKFORD: Mine was a very simple question just framing

1 where we are going in the answers.

2 By comparison to BT, we know again from public
3 knowledge that Sky recently spent the best part of
4 around 4 billion on its main football rights, mainly the
5 Premier League. Are you aware of that?

6 A. Again I don't recall the figures precisely, but I know
7 that the cost of those rights has escalated
8 significantly.

9 Q. So if we take my numbers as read -- and deliberately
10 using very broad numbers because the detail doesn't
11 matter -- of the two top competitions, Premier League
12 and Champions League, around one third of the
13 expenditure has been by BT? That's correct?

14 A. I don't know.

15 Q. Okay.

16 A. But according to your figures, it seems that, you know,
17 if I take your figures and I do a back of the envelope
18 calculation, it seems correct.

19 Q. My maths at least runs that far.

20 So all of that investment is not bad for a company,
21 is it, which as at the date of the 2015 decision had
22 only had a sports channel for just over two years, when
23 it is competing against a rival which has been in the
24 market for 25 years?

25 A. All that I can say is that in Padilla 1, I looked at the

1 content gap between the two companies and I found that
2 [redacted]#####
3 #####
4 #####
5 #####

6 And that assessment is, in my opinion, confirmed by
7 [redacted]#####
8 #####
9 #####

10 Q. Now you say, according to your modelling, that you would
11 expect Sky to win except in exceptional circumstances.

12 Given what I have just put to you about the nature
13 of the rights that BT currently holds, you are not
14 really in a position, as an expert economist, to say
15 whether those circumstances are exceptional or not; are
16 you?

17 A. In my report -- in Padilla 1, I recall, maybe Padilla
18 3 -- I considered the experience of [redacted]
19 [redacted]##### and I concluded that it appeared
20 to me [redacted] identified in the model, in
21 the sense that it ended up being [redacted]

22 In other words,
23 [redacted].##### And therefore
24 I concluded that indeed it was of that nature, an
25 exceptional circumstances auction.

1 Why did I focus on Champions League as opposed to
2 others? Because that was the content that was not
3 reflected in my choice modelling estimates and therefore
4 the one that could have made a difference in terms of
5 competition in the market, because it was the content
6 that appeared to be the most significant content
7 acquired for BT in competition with Sky.

8 As to the other content that BT has acquired,
9 I didn't have and still do not have enough information
10 even to know whether there was a competition between BT
11 and Sky, or it was just that BT was bidding for that
12 content.

13 Q. Even in relation to Champions League, you don't have
14 detailed knowledge, do you, about exactly what went on
15 in relation to auctions?

16 A. Very limited, and the one that is described in my
17 report. As to the Premier League, the reason why BT
18 obtained those rights was because of the design of the
19 auction that in a sense reserved certain rights for
20 a competitor and the fact that to the best of my
21 understanding it was the bidder -- the competing bidder
22 at that time. In other words, there were no others.
23 But that's to the best of my understanding.

24 Q. Thank you, Dr Padilla.

25 We are now going to move on to the last major topic

1 but there is quite a lot within it so we are still going
2 to clearly go on into Monday. That is the evidence that
3 you have given about market development. So we have
4 looked at the vicious cycle model but you also gave, in
5 a separate part of your evidence, your views on the
6 nature of competition and how it has evolved since 2010.
7 You are aware of that?

8 A. That's correct.

9 Q. If we can then please pick up your third report which we
10 find in bundle R1 at tab G.

11 I think the G1 bundle does make an appearance again
12 at some point, but probably not for a little bit so
13 I think probably for this afternoon it is touch and go
14 whether we will be getting back to it this afternoon.
15 We might. It depends on how fast we go.

16 If you have managed to turn up tab G, which is your
17 third report, and if you could please go to
18 paragraph 3.3?

19 A. Yes, I am here.

20 Q. You say:

21 "In the 2015 WMO statement Ofcom failed to ... any
22 relevant market as at first down the scope of the
23 analysis to those factors relevant to the product in
24 hand. However in my opinion, and absent any analysis to
25 the contrary, I believe that the relevant products for

1 the purposes of Ofcom's review of the WMO remedy are
2 likely to be based around the wholesale and retail
3 supplied premium sports channels in the UK."

4 A. Correct.

5 Q. Then you go on to address Ms Fyfield's evidence and you
6 say, at 3.4:

7 "Whilst I don't consider every development raised by
8 Ms Fyfield, it is clear that the majority are irrelevant
9 to any assessment of the wholesale and retail markets
10 for premium sports channels."

11 A. Yes, that's what I say.

12 Q. And one of the things you go on to dismiss as irrelevant
13 is Ms Fyfield's evidence on the growing importance of
14 companies such as Netflix and OTT delivery of content
15 via apps, because you say that that is things like
16 movies, in essence?

17 A. So I dismiss Netflix, Amazon, Apple and Google, for
18 example, in 3.5B. And with respect to OTT delivery --
19 and the reason why I dismiss them is because they don't
20 include the sports content -- and with respect to OTT
21 delivery of content of sports content, I think that the
22 most significant development in the market is the entry
23 of NOW TV. But the entry of NOW TV doesn't have an
24 impact on competition to the extent that it is just
25 another product of Sky.

1 Q. I would like to put to you some reasons why I suggest
2 that the OTT developments are more relevant than you
3 say.

4 The first reason is this: you say at paragraph 4.4
5 of this report that we currently have open that one of
6 the primary purposes of the introduction of the WMO
7 remedy was to allow retail pay TV operators to compete
8 effectively to secure access to the most important TV
9 channels?

10 A. Yes.

11 Q. Yes. We have discussed already that at least part of
12 your vicious circle model -- certainly as it was
13 originally formulated -- depended on an assumption that
14 in order to develop an effective pay TV business it is
15 relevant how many premium sports customers you can get
16 on to your own platform?

17 A. Sorry, we debated that point and you know that
18 I disagree. I think that what I said is that what
19 matters is the number of your subscribers. You want to
20 get a subscriber base.

21 Q. Just to be clear, what you are saying now is it really
22 doesn't matter at all whether they are on your own
23 platform or not?

24 A. I don't know what BT's and Sky's views would be on that.
25 All I can tell you is that in the context of the logic

1 of my models, it doesn't matter.

2 Q. In which case I think we can probably cut through that
3 pretty quickly.

4 I think the key point, then, is that I assume you
5 agree that OTT delivery is one of the methods that is
6 available to a retailer to gain subscribers, and it is
7 therefore an important part of their ability to monetise
8 sports rights?

9 A. Yes, but the development in the market -- I fully agree
10 with that, but I think that the development in the
11 market is the following. If we look at, I think it
12 would be NOW TV, the main OTT method of delivery of the
13 sports content, that adds [redacted] subscribers to Sky.
14 So in other words it increases the subscriber base
15 advantage that Sky has over BT.

16 And while I think that BT -- I have means to deliver
17 in an OTT way through its BT app, I don't think that the
18 numbers are comparable at all. So I think that that
19 development in fact entrenches the vicious circle as
20 opposed to undermines the vicious circle.

21 Q. But you recognise, I think, BT also has the opportunity
22 to retail over an OTT basis?

23 A. Yes, I do recognise. But this is the central point of
24 the vicious circle story: that the opportunity is not
25 enough: you need to have content that is sufficiently

1 attractive to grow your subscriber base. If you don't
2 have that content, then you don't develop the subscriber
3 base, that affects your ability in the future to get
4 additional content and that gets you into a trap.

5 Q. One of the themes of Ms Fyfield's evidence is that the
6 audiovisual sector is characterised by rapid and
7 pervasive change. She illustrated that by the fact that
8 Netflix has gone to from zero to 5 million subscribers
9 in just a couple of years.

10 You may feel that you are not able to opine on this,
11 but do you agree with Ms Fyfield that the audiovisual
12 sector is characterised by rapid and pervasive change?

13 A. Yes, I do agree with that proposition. But what I was
14 trying to look at is whether there had been significant
15 developments in the strength of competition in the
16 wholesale and retail markets for sports content. The
17 development of Netflix in that respect is irrelevant --

18 THE CHAIRMAN: It is not a potential cross entrant as they
19 say?

20 A. Not as far as I am aware.

21 And with respect to the other market that we could
22 contemplate, which is the retail pay TV market which is
23 broader than just the retailing of sports channels,
24 I think that I concur with Ofcom's view that Netflix is
25 fundamentally a complement as opposed to a substitute

1 for the traditional pay TV offers.

2 MR PICKFORD: Now, given the agreement that you gave to the
3 question that I asked, it follows, doesn't it, that if
4 you are able to get guaranteed wholesale supply, that is
5 very attractive in a very fast moving market and could
6 well outweigh the more speculative benefits -- given how
7 fast the market moves -- of a strategy that was aimed at
8 hobbling a competitor some years into the future?

9 A. I think that I'm prepared to agree that in an uncertain
10 world if you have long term contracts that is
11 attractive. Again I think I'm going to say something
12 confidential, so --

13 MR PICKFORD: Right, in which case I certainly would not
14 wish to stop you for a moment, so we will have to clear
15 the court if it is necessary.

16 I am afraid I don't know what Dr Padilla is going to
17 refer to. If you are able to describe what you want to
18 refer to in a way that you know is non-confidential,
19 then please do, but if you think that is dangerous in
20 any way --

21 A. I think it is dangerous in any way.

22 THE CHAIRMAN: Where did you receive the information?

23 A. It is in Ms Fyfield's report and it is marked
24 "Confidential".

25 THE CHAIRMAN: So you are going to disclose Sky material to

1 BT?

2 MR PICKFORD: In which case, BT, if they are not in the
3 confidentiality ring, will need to withdraw.

4 THE CHAIRMAN: For ten minutes. Better than making
5 a mistake.

6 A. It is not a very big deal but I don't want to reveal
7 something which is confidential.

8 THE CHAIRMAN: Big deals are made from small deals.

9 (In camera session)[redacted pages-183-188]

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(The hearing adjourned until
Monday, 10 October 2016 at 10.30 am)

Examination-in-chief by MR BEARD107
Cross-examination by MR PICKFORD112

