IN THE COMPETITION APPEAL TRIBUNAL

Case No. 1087/2/3/07

Victoria House,
Bloomsbury Place,
London WC1A 2EB

7 April 2008

Before:
VIVIEN ROSE
(Chairman)
MICHAEL BLAIR QC
PROFESSOR PAUL STONEMAN

Sitting as a Tribunal in England and Wales

BETWEEN:

INDEPENDENT MEDIA SUPPORT LIMITED Appellant

- v -

OFFICE OF COMMUNICATIONS Respondent

- supported by -

RED BEE MEDIA LIMITED

BRITISH BROADCASTING CORPORATION Interveners

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HEARING – DAY ONE

APPEARANCES

Mr. Stephen Hornsby (Partner, Davenport Lyons) appeared for the Appellant.

Mr. Rupert Anderson QC and Mr. Alan Bates (instructed by the Office of Communications) appeared for the Respondent.

Mr. Nicholas Green QC and Miss Jemima Stratford (instructed by Travers Smith) appeared for the Intervener, Red Bee.

Miss Lesley Farrell (Partner, S.J. Berwin LLP) appeared for the Intervener BBC.

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THE CHAIRMAN: Good morning, ladies and gentlemen. A couple matters the Tribunal wishes to raise on an introductory basis; first, a couple of points of clarification as to where we are now with the issues that we have to decide. We would welcome clarification as to exactly what the abuse, or abuses, were that were being alleged by IMS as having been committed by Red Bee and, further, whether it is IMS' argument that the nature of the abuse, or abuses, alleged have any effect on the time period over which IMS say Ofcom should have assessed the existence of dominance.

Secondly, to clarify whether it is agreed that the issues for the Tribunal are now as set out in para. 2 of Ofcom's skeleton argument, or whether they are as set out in para. 2 of IMS's skeleton argument - and, again, in particular, whether IMS is arguing only that the contract falls within Article 81(1) and the Chapter I prohibition after 1st January, 2007. It seems to us at the moment that the logic of two of IMS' arguments really go to whether the vertical agreements/block exemption applied at all - namely, whether it was right to exclude in-house supply from the total size of the market and hence from Red Bee's market share; secondly, whether the duration of the exclusivity is properly to be treated as eight years or five years depending on the characterisation of the cost reimbursement fee. So far as that cost reimbursement fee is concerned, we know now that it represented about 3 percent of the total expected revenue over the renewal period. What the tribunal needs to know though in order to assess the economic effect of it is whether in order to avoid paying the CRF, Channel 4 would have to renew the contract at the same prices as prevailed over the preceding five years, or whether there was a re-negotiation of the price at the point at which the option is exercised, because our preliminary view is that in a market where prices are falling, we can see that the CRF has less effect from an economic point of view if the price has to stay the same under the contract than if the price can be reduced on renewal.

Similarly, whether in order to avoid paying the CRF Channel 4 have to renew the whole of the contract, or whether they can renew part of it, taking part of the services for the subsequent three years from Red Bee, or whether, in order to avoid paying the CRF they have to renew all aspects of the contract with Red Bee.

There are a couple of small factual points also which we would be grateful if someone could help us with at some point. First, there seems to be an inconsistency in the decision between the figures for market shares in Tables 6 and Table 7. They seem to us to be supposed to be saying the same thing. However, there is an inconsistency there in some of the market share figures. The second factual point is in relation to Wordwave. Para. 5.70 of the decision mentions Wordwave entering into a joint venture with ITC. IMS say in para. 14 of their

skeleton that Wordwave failed and exited the market, and we note also in para. 24 of the IMS skeleton that there is a reference there to an attempt to enter, not having succeeded in recent years, and there having been a major exit from the market. We assume that the major exit referred to is Intelfax, although, if we are wrong on that, please tell us. But, it would also be helpful to know if the failed entry that is referred to there is Wordwave or is something else.

Those are points that we would like to be addressed on at some point during the proceedings - not necessarily at the outset. Mr. Hornsby, I think it is probably for you to kick off.

MR. HORNSBY: Thank you very much. If I could just perhaps deal with the first of your questions to at least get that one out of the way? Your question was: What were the abuses that IMS alleged took place in the course of conduct, if you can call it that? The abuses were that the price at which BBC won the Channel 4 contract was beneath marginal cost with a predatory price; the second was that price discrimination took place in that the price that was charged to Channel 4, in our estimate, was a price that was subsidised by the revenues derived from the BBC contract. That is the second limb, if you like, of the pricing complaint. The second complaint was in relation to the duration of the exclusive contract entered into by BBCB, as it was then described, and Channel 4. At the time it was a five year contract as far as we knew. Subsequently, we discovered that it was a five year contract with an option to renew. The option to renew had a fee arrangement which you have already referred to attached to it.

The second question that you asked was in relation to the relief sought. I think, if I understand you correctly, what you said is that the logic of the position that we are adopting -- that IMS is adopting in relation to the Channel 4 contract should mean that the contract always was in breach of Article 81 and that it did not need the protection of the block exemption for that issue to arise. Our point is simply this: we are not concerned in seeking a remedy from the Tribunal in relation to events that are now quite some distance in the past. Our concern is simply to show that from 2007 the agreement did not have the benefit of the block exemption, and fell within Article 81(1), we say. That was the decision that we are attacking. We are not looking at 81(3).

THE CHAIRMAN: So, you are saying that although your arguments may go to the question of the application for block exemption at all, in fact your interest is only in challenging the position post 1st January.

MR. HORNSBY: Indeed, yes. The factual questions, to a certain extent, I think can be dealt with by Ofcom. There was one more, but I have already forgotten it ----

THE CHAIRMAN: It was the question of whether the nature of the abuse, or abuses, alleged has any effect on the period at which Ofcom ought to have assessed -----

MR. HORNSBY: It is absolutely fundamental. It is the most important issue in our perception of it. We believe that these hypothetical abuses - because Ofcom never went into the pricing one because it did not have to, according to its logic -- We believe, ex hypothesi, these abuses are continuing. The pricing, although we do not know this to be the case, continues to be one which is beneath our average variable costs, or one that is subsidised by the BBC revenues. Ofcom would surely agree with us that to the extent that our complaint is in relation to a contract of five years' duration, that contract is continuing to this day. It is operating actually at the moment. So, when we actually come to look at this point in some detail, what we will be saying is that if the time for infringement is really the time you make your assessment of market power, then at the time that the decision was taken in June 2007, analysis should have been made of market power at that point or a little time before then. We also say that the fact that Ofcom had to actually do an analysis for 2007, because at that point the block exemption had run out, the transitional period had expired, shows that really when you take a decision under Articles 82 and 81 you have to use the same time frame, but Ofcom's case is essentially based upon when an infringement first occurs – not when the infringement actually occurs – the infringement is continuing. What Ofcom is saying is that you analyse market power at the point the infringement first occurs i.e. either when a predatory bid is made, or an exclusive contract is entered into. That is very much I think the difference between our two approaches, and we will come on to it in more detail.

THE CHAIRMAN: What I was trying to get at is whether, in relation to those types of abuses – the pricing abuse and the exclusivity abuse – you are arguing that they potentially focus on different periods of time. I quite understand that you say that in relation to both of them you should look at the whole period of the contract and Ofcom say in relation to both of them you should look just at the moment when the contract is entered into or shortly before. But is part of your argument at least to differentiate between those two abuses in any way and say if the Tribunal is against you on one of them might it still be open to us say in relation to, say, the exclusivity point then you look at the whole period, even if we find that ----

MR.HORNSBY: I understand, yes. We would say, I think, that they stand and fall together really. I do not think there should be any disagreement between Ofcom and ourselves that on any view the hypothetical abuse that is constituted by the exclusive contract is a continuing infringement – if infringement it is.

THE CHAIRMAN: Thank you.

MR.HORNSBY: Would it be helpful if I started off by just saying what I take to be common ground between IMS ----

THE CHAIRMAN: I think that would be very helpful.

MR.HORNSBY: IMS and Ofcom agree on the definition of the market, the service market, that is contained in the decision. We also agree with Ofcom in relation to the geographical scope of that market, we believe it is a national market – a UK market – and in a sense that is defined by the statutory provisions which require these services to be provided to a certain extent. It is also supported by the lack of development of other markets for the provision of these services in Europe although not in the United States.

The second point that we agree with Ofcom is in relation to the treatment of in-house sales. We agree with Ofcom that when a company is openly bidding for business, other than self-provision then its market share needs to be taken into account in doing an assessment of market power.

THE CHAIRMAN: Could you repeat that?

MR.HORNSBY: We agree with Ofcom that the treatment of in-house sales for the purpose of Article 82 depends upon whether the company in question is openly bidding for other contracts in the ----

THE CHAIRMAN: Whether its in-house supplier people are bidding for outside work as well?

MR.HORNSBY: Yes, so when they are bidding for outside work as well they have the capacity to meet demand outside their in-house requirements, in those circumstances their market share needs to be taken into account globally.

ITFC, the in-house supplier of these services to the ITV channels also have other customers apart from the in-house purchaser (ITV) and they were properly taken into account by Ofcom for that reason. They are in the same situation as the BBC, they are openly bidding for business, ITFC, outside their protected market, if you like, that was provided by the requirements of ITV.

We have a disagreement in relation to the treatment of Sky, however; Sky was never in this category in our view. Plainly, as a matter of fact, it did not actually pitch for any business. It did supply some of the services in-house but it did not pitch for business outside, therefore its market share is something of a misnomer, it does not have one. That is a factual disagreement; the analytical analysis is one we share with Ofcom. You distinguish the two treatments based upon whether there are attempts to win business other than your captive customer.

THE CHAIRMAN: And that is the important thing, rather than whether there was ever – or ever would be – a competition between the in-house suppliers and others for the business of the undertaking which has in-house supply, "the protected business" as you called it a moment ago?

MR.HORNSBY: Yes, but sometimes a company may wish, as Channel 4 did, it had an in-house supplier called Intelfax and decided it wanted a competition for the provision of that business and BBC won that business and IMS did not succeed in its bid. The other area of agreement that we have at a high level is, if you like, that bidding markets could be a relevant consideration in assessing this particular market. We say that there is not yet a bidding market, there may one day be one. Clearly countervailing power is highly relevant in an analysis of market power, it is the power of the purchasers and that includes the power to sponsor new entry or force down prices.

New entry from outside is obviously a relevant consideration. We differ in our analysis of what the facts show. We say actually no one has entered this market – there have been a couple of exchanges of ownership. Wordwave did try and enter the market independently, but it did not succeed in winning any business independently to a significant extent – it got something like 1 or 2 per cent.

THE CHAIRMAN: You mean outside the joint venture ----

MR.HORNSBY: Outside the joint venture. Then we say in response to that it had to go into a joint venture to actually get off the ground at all in the United Kingdom. So we agree that these are factors that you look at, we just disagree with the conclusions you draw from the factual record.

We also agree that above a market share of 50 per cent there is a presumption of dominance, the proposition for that is the *AKZO* case. We say, in distinction to Ofcom that we are in a situation where at the relevant time, and I do not go into that at the moment because I say it goes up until June 2007, Red Bee now has a market share of over 50 per cent. Where you have a market share of over 50 per cent the weight that you need to give to the elements that help to discount a finding of market power – dominance – the weight must be much greater, you must have really strong arguments to demonstrate that the presumption must be rebutted. We say simply that we are in presumption territory at the relevant time, the presumption was there and that what Ofcom ought to have done is look critically at the evidence that its investigations had unearthed, and said actually this evidence is too weak to rebut the presumption of dominance, 50 per cent plus dominance creates. Our fundamental difference with Ofcom though relates to the time for assessing market power. Ofcom

believes that the time for assessing market power must be closely related to the time of the infringements. We say that to the extent that they have adopted a consistent position on this point, that it is wrong in principle. We believe, ex hypothesi, the infringements are continuing infringements; they were continuing to the date of the decision. On any view, if the exclusive contract amounted to an infringement of Article 82, it was continuing, and continues to this day, but we are not seeking any remedy in respect of any period of time beyond June 2007, which I will come on to explain in a second.

The final area of disagreement is, if you like, in relation to the analysis of the Channel 4 contract post January 1st, 2007. We say the block exemption runs out at that point and that in circumstances like that it is very difficult to justify a minimum three year tie, we say, of more than 10 percent. We also say in relation to (shall we call it) the CRF contract renewal fee that that effectively is a serious impediment to anyone wishing to enter the market at that point and makes it even more difficult to reach the conclusion that Article 81 is not infringed.

That is really where we are. The issues before the Tribunal are, firstly, in relation to the question of dominance. Is Ofcom right or are we? The second, again, is a question of whether Article 81 is available. If we are right on the first, and that Ofcom was incorrect in saying that BBCB was not dominant -- if Ofcom was wrong on that point and we are right, we believe it is much harder to reach the conclusion that Article 81(1) is not infringed because it is much more difficult for a company in a dominant position to enter into exclusive agreements of any period more than one year without it falling within Article 81(1), subject to their being efficiency justifications for that agreement which are not contained in the decision. The decision does not have anything which says, "This is efficient" - it just says, "The effect is not appreciable". We say, "If the company is in a dominant position, that is hard to get away with". You are in Article 81(3) territory there, and nothing has been put forward, we say, to justify the substantial elimination of competition that is collectively, if you like, created by an agreement added to the BBC internal agreement.

The intervener, Red Bee, has raised some points about the remedies that we are seeking. I thought perhaps we would just go to those. If we go to the documents bundle at Tab 16, p.2, para. 7 of the Red Bee skeleton, you will see that Red Bee is basically saying that IMS is asking the Tribunal -- or criticising Ofcom for not carrying out an exercise which it cannot do because it is looking too far in the future. Our point in relation to this we believe is

satisfactorily dealt with by turning to the authorities bundle at Tab 37, which is the extract from **Bellamy & Child**, at para. 10.018.

> "Because a finding of dominance involves assessment of these elements in the circumstances prevailing at the time ..."

that point is quite interesting; it is a rather ambiguous phrase, which we will come back to.

> "... it is not binding for the future. Therefore a determination by the Commission of dominance, without a finding of abuse, cannot in itself be the subject of an appeal since it does not produce legal effects, although it will probably have a practical effect on the commercial conduct of the undertaking concerned, given the 'special responsibility' imposed on dominant firms by EC competition low. Should a subsequent allegation of abuse be made, an analysis to determine dominance would have to be conducted afresh".

This is not a telecoms market, obviously. But, what we are saying is simply this: we believe that at the time the decision was taken Ofcom should have looked at prevailing market conditions at that point. At that point Intelfax was long gone; the market share was over 50 percent; the elements to discount market power were insufficient to overcome the presumption of dominance. Therefore, we are not seeking by these proceedings any form of declaration in respect of the future; that battle will have to be fought at some future date if it ahs to be fought at all, but of course Article 82 creates a prohibition that is not necessarily the result of a decision; Article 82 has effects without a decision taking place. So what we would say is that a decision in relation to Article 82, as of 2007 could not be ignored by a dominant company going forward because of the special responsibility attaching to dominant firms, it would have to have regard to the possibility that if it were to repeat behaviour which we say has taken place in these proceedings it might abuse that dominant position

THE CHAIRMAN: I understand that you say that they should look at the position in the market as at the date they take the decision, but is that as well as or instead of looking at the position in the market as at the date that the contract was concluded? If it is decided that Red Bee was not dominant at the time that the contract was concluded – you have referred to these as "continuing infringements" but I am not sure whether you accept that it is a necessary step for Ofcom to have decided that there was dominance at the time the contract was entered into, or whether it is your case that it is enough that at some point during the application of the contract; the implementation of the contract, that a dominant position arose?

MR.HORNSBY: We say that both at the time that the contract was entered into and at the time that the decision was taken BBCB/Red Bee was in a dominant position. There was a 40 per cent market share at the time that the contract was bid for, that became a 50 per cent plus market share when the contract was awarded; that market share continued until 2007. We say that in making a decision based upon events that took place in the past Ofcom misdirected itself. It should in 2007 have not taken into account the market share of a company that had gone out of business some two years previously, it should have updated the analysis and looked at the conditions of competition at the time that it took the decision. Had it done so, we say, it would have inevitably reached the conclusion that a presumption of dominance had been created.

THE CHAIRMAN: I am still not entirely clear though, Mr. Hornsby, whether you accept or not that it was important for Ofcom also to assess the question of dominance as at the beginning of 2004; was that a necessary thing that they did, and is it essential for there to have been a finding of abuse in this case that there was a determination that there had been dominance at that stage?

MR.HORNSBY: Well we believe that the period of time over which you should examine whether or not a dominant position exists is far longer than the six month period that Ofcom seems to have chosen. Whether it was the bidding that was the time that you look at market power, or whether it was the actual achieving of the contract, the winning of the contract, we believe that the authorities that we will come on to now demonstrate that that period of time is far too short. You should look at the period 2004 – 2007.

PROFESSOR STONEMAN: Before you move on, I have in front of me **here**, the original Ofcom determination which lays out the IMS complaint. I do not know what paper it is of yours, but according to this your original complaint was submitted on 6th June 2005. Are you arguing that on 6th June 2005 that IMS should have undertaken a determination of the situation as it would be in 2007?

MR.HORNSBY: No, because we never knew when a decision was going to actually be handed down, but what we would have expected to have been carried out by Ofcom was an analysis of market power that was not based upon the situation, the snapshot in 2004, whether it was early in 2004 or later in 2004; we would have expected a period of at least three years to have been examined properly before a decision was reached as to whether BBCB had a dominant position.

PROFESSOR STONEMAN: But you put in your complaint in June 2005 with respect to a contract signed on 14th July 2004, which was an 11 month period, so you did not follow that rule yourself?

MR.HORNSBY: Well we had no option. We were asked first of all to complain to the BBC governors about our complaint, and we did so and that took a certain amount of time to resolve. We then put together the complaint and in our complaint we said that BBCB enjoyed market power at that particular point and that we were putting the complaint in.

PROFESSOR STONEMAN: But you made that complaint in July 2004, which was exactly days after the contract was signed, so you had no idea how the market was working out and whether or not the market was being abused at that time?

MR.HORNSBY: Well it was difficult at the time that the original complaint was made to the BBC; it was difficult to do a proper market analysis, that is always the situation of the complainant. At that point the major thrust of the complaint was that here was a Body in receipt of the licence fee competing on terms which were perceived to be unfair, not just by IMS but by Intelfax, and when Intelfax lost the contract there were a large number of complaints made, many of them to MPs, along the lines of here was an unlawful, unreasonable and unfair use of public subsidy to put out of business another company which, of course, actually in receipt of public subsidy itself.

PROFESSOR STONEMAN: Let me explain to you why I am being a bit awkward about this. Basically your original complaints were framed in terms of the contract, the signing of the c contract, the terms of the contract, and that was, I gather from the original complaint, what Ofcom was to look at. But now what you are saying to us is that the complaint is not about the contract, it is really about the operation of the market in the post-contract period, that in the post-contract period to at least 2007 (and maybe later) a dominant position was being abused. Now, I cannot understand how you can originate a complaint in 2004/2005 with respect to abusive behaviour in 2006, 2007, and 2008, unless it is just the contract itself that you are concerned about.

MR.HORNSBY: It is the contract and the price.

PROFESSOR STONEMAN: The price is in the contract.

MR.HORNSBY: The price is in the contract that is absolutely true, but the contract is an exclusive contract and that is a separate ground for abuse. There were three grounds of abuse, if you remember. There was the pricing one which had two limbs: first, beneath average variable cost, secondly there was a cross-subsidy and therefore discriminatory, and then the second limb of the complaint was in relation to the duration of the contract and we

made those complaints about the market at that point. Obviously as we moved on and the proceeding left the BBC governors and passed over to Ofcom, and we had the transfer of ownership from BBCB to Red Bee, and obviously there are some change of circumstances, but we believe that what Ofcom should have done is to look back from the time that it took its decision in 2007 and say: "How has this market performed? How has it developed since the time the complaint was made?" They are perfectly entitled to look into events that took place before 2004. For example, if Wordwave had tried independently to enter the market in 2003 certainly Ofcom was entitled to take that into account, and it did so in its decision. We say that by the time it came to take its formal decision in 2007 in relation to dominance and the Channel 4 contract, it had plenty of material to look back on. It had been able to see the evolution of the market, and had it looked properly, we say, and had it not looked at and taken into account the existence of a company that had gone bust two years previously it would have reached a different conclusion from the one that it reached.

THE CHAIRMAN: I am not sure now whether your case is that in deciding whether, when it entered into the contract in 2004 Red Bee was dominant, Ofcom ought to have looked at a longer period including the whole of the period up to 2007 but still addressing its mind to the existence of dominance in 2004, or whether you say that regardless of whether they were dominant in 2004, looking at the position in 2007 they were dominant and therefore this contract is an abuse of that dominance.

MR. HORNSBY: We say that it was an abuse of a dominant position when the contract was entered into. We also say that looking at market power you analyse a market based on a longer period of time than Ofcom took. You look at the period before the contract was entered into, and you also look into the period after the contract was entered into. If you looked into the period when the contract was entered into, you will have seen that there was an exit from the market - that was Intelfax - and that is something that you ought properly to have taken into account when you took a decision in 2007. Had they properly taken the exit of Intelfax into account in 2007, our case is that they would have reached a different conclusion -- they would have had to have reached a different conclusion.

We say it was both dominant at the time we made the complaint and subsequently. There were changes of ownership, and that meant that there have been some difficulties about the analysis, about the in-house sales, about whether the Article 81 guidelines can be applied to in-house sales. But, apart from that, we say that there is a continuum of market power demonstrated by an analysis of the position of BBC Red Bee from the period 2004 until the

period 2007. I think somewhere it is actually accepted in one of the skeletons that that is the analysis that we want. It is in relation to 2004 to 2007.

I hope that deals with the issues of the remedies, which is an important issue.

Could we now go on to a chronology? We seem already to have got on to a chronology. It might be of some assistance to just go through it. (After a pause): It is not in the court bundle - it came rather late. This chronology was agreed, not without some difficulty, between all the parties. It contains events which I think are incontrovertible. Just pausing at (3), we would like to stress that we complained to the BBC governors about the five year contract not being one with a three year option, and we had no knowledge at that point in time of the CRF. Clearly, the governors were aware of those things. Nevertheless, we felt that there was an issue. So, we had no option but to complain to Ofcom at that point.

In early 2005 Intelfax staff transferred to BBC Broadcast. That pre-dated the rejection, we think, of the complaint by the BBC governors. But, we are not entirely sure when the transfer took place.

After (7) when Ofcom opens its investigation into the Channel 4 contract, we have an event which will be discussed later. The event is November 2005 when there was a management presentation by Red Bee. We will come on to discuss the significance of that presentation later on.

The other events are non-controversial really. They simply recite what took place, when. We have decision on 4th June, 2007. What we say, obviously, is that it was a decision which was issued on 4th June, 2007 which ought not to have taken into account the existence of a company whose staff had transferred to BBCB some considerable time earlier - over two years earlier.

We now go on to the parties' position on the time for assessing market power. I think we can go through that quite quickly. Ofcom's position, in its decision, at any rate, is to be found in the court bundle at 1.16. That is in Tab 3. This document deals solely with Ofcom's consideration of the BBC 4 contract at the time it was entered into by the BBC subsidiary.

THE CHAIRMAN: The Channel 4 contract.

MR. HORNSBY: I am sorry. The Channel 4 contract. Since the decision was taken Ofcom has modified its position slightly on when the time for assessing the Channel 4 contract was - partly in response to questions from the Tribunal. The position it adopts in its defence now is that it was either when the contract was entered into or when it was bid for. They say it does not really matter which it really is -market positions were pretty much the same at that

point. Our first point about this is really that it is insufficient in a decision to leave your options open in this way. The decision actually says when the assessments for the Channel 4 contract took place. It is quite clear in 1.6 of the Channel 4 decision and that is when it was concluded. We cannot speculate on why it is that Ofcom has modified its position and now says that it is really very likely that it occurred when the contract was bid for. One possible explanation for this approach is that at that particular time it might be more reasonably said that Intelfax had a future. It still was not clear whether Intelfax would depart from the market. On the other hand, when the contract was concluded, it being reasonably well-known, that Channel 4 was Intelfax's major, if not sole, client, that at that point Intelfax was moribund. It took some while, obviously, for Intelfax to finally depart the scene, because the contract had a few more months to run and it did not conclude until January, which was effectively six months later. Our point on that is really that whichever date is chosen, the whole concept is wrong -whether it is when the contract was bid for, or whether it was the time it was concluded. Either of those, or both of those -- It is just too short a time to make a proper assessment of market power, and the market power issue must be carried on, and that when the decision is actually you look at the market; you take a decision, generally speaking, on the conditions of the market prevailing at the time that decision is taken.

THE CHAIRMAN: I think you are conflating two different points there, which are points that I am trying to tease out. What is the decision that Ofcom actually has to take as regards when dominance exists? That is one question. The second question is: in deciding that Red Bee is, or is not, dominant at that time, what period should they look at? Now, the period of time at which they have to decide whether it was dominant or not is a moment of time. That would be what they say. But, they are not saying, "Well, you just look at the situation on that day". They accept that you look at some period of time. You look at the period of time in order to decide, "At that moment were they dominant?" You say that the period of time they looked at was too short and that it was only prior to the contract, and not after the contract. I can understand that point. But, do you nonetheless say that they were right to understand that their task was to determine whether Red Bee was dominant at a particular date being when they entered into the contract or when they bid for the contract - whichever - but that in looking at that question they erred in taking account of too short a period? Or, do you not accept that they should focus on a particular time which it is necessary to establish, however you do it, that Red Bee is dominant?

MR.HORNSBY: We say that it should be 2007 looking backwards for at least three years. One of the elements that you look at obviously therefore covers the period of time when the

contract was entered into and it was bid for. But we say you do not shut off the analysis at that point. Our complaint about Ofcom's decision is at the point – whether it was when the contract was bid for, or when it was concluded, Ofcom if you like pulled up sticks and said "That's it. We look at things from that particular point in time going backwards a few years to see the evolution of the market and so on and so forth, and we do not take into account events that took place subsequently, such as the change of ownership and the demise of one of the four competitors in this market." It will become clearer as we go through the authorities.

THE CHAIRMAN: Mr. Blair has a question.

MR. BLAIR: I have another way of slicing this onion. In the chronology very helpfully supplied and agreed, item 9 (see Docs bundle B, Tab 6, pages 81-82) says: "On 22nd March 06 IMS wrote to Ofcom arguing that the analysis about dominance should be updated". I have not found - maybe it is somewhere in the decision – the reaction that Ofcom took to that request. I do not think it is the one in footnote 146 – can you tell us whether that suggestion of yours, about updating the analysis was rejected in the decision?

MR.HORNSBY: Implicitly rejected in the decision.

MR. BLAIR: Implicitly only?

MR.HORNSBY: Implicitly only.

MR. BLAIR: Thank you.

MR.HORNSBY: We objected quite strongly, we felt that this was just a way of not getting into the issue of the pricing. We thought that this was, if you like, an exercise in logic chopping, it did not correspond with the realities of the market; that to look simply at the situation at the time the contract was entered into and not to take a longer period taking into account the change of ownership which would have an impact on how in-house sales were to be assessed, we thought that that was completely wrong. Now, we told Ofcom about that and we had a meeting with Ofcom about that, and the note of the meeting is supplied in the bundle (see Docs bundle B, Tab 9), but it was quite clear afterwards that argument had really fallen on deaf ears, that they were determined to carry on with the decision based upon what they perceived as the time for making the analysis, which was a time which we said had long gone.

We say that the proper test is the one that BBCB and Red Bee put forward, whether jointly or severally. It is recorded in the decision, file A, tab 3, p.41, at 7.5:

"The BBC on behalf of itself and BBC Broadcast argued that at the time it bid for the Channel 4 contract, BBC Broadcast was not (and continues not to be) dominant in the supply of UK television access services because:

(i) 'its market share [excluding self-supply] was, and is, not large enough to give rise to a presumption of dominance;

(ii) in any event market shares are not very meaningful in a bidding market'."

We say that is the correct test, the essence of it is captured by the words "continues to be". What the BBC was basically saying was: "In prevailing market conditions we are not dominant; no presumption of dominance can be derived from our market share, we are not therefore dominant – even if we are, perhaps bidding markets and other factors mean that that market share is not as important as it would otherwise be."

We say that Ofcom's position is inconsistent, it is too short and I just want to take us briefly to some authorities on the point of too short. If you go to A36 – authorities bundle tab 36.

PROFESSOR STONEMAN: Just before we go there, could I take you back, you are implying that the continuation of the dominance is an important point in the BBC's viewpoint.

MR.HORNSBY: Yes.

PROFESSOR STONEMAN: What was Ofcom's attitude to that? It looked to me as if in 7.9 it did not take any notice of it – we are appealing Ofcom's decision and not BBC's view.

MR.HORNSBY: That is absolutely right, yes, Ofcom did not seem to think that it was necessary to take a position on the argument. It thought that it was sufficient that it was not dominant at the time the contract was entered into.

PROFESSOR STONEMAN: That is very much taking a position; that is not ignoring the position.

MR.HORNSBY: I agree, yes, I agree. In the decision itself, to be fair to Ofcom, I think in one of the footnotes it does record IMS's view about the proper time for the assessment of market power, but we never succeeded in the administrative proceedings in actually eliciting from Ofcom why it was that this particular cut-off existed and it has only become clear what Ofcom's position is, although it is we say, still inconsistent and unclear, only since we have appealed this have we been aware precisely what has gone through its mind so to speak.

MR. ANDERSON: The Tribunal might find it helpful just to note at that point footnote 104, which essentially sets out Ofcom's response to those positions.

MR.HORNSBY: Yes, that is absolutely true, I am indebted to Mr. Anderson for pointing that out. But if you get half way down that particular footnote, what you get to is this concept of

the time of the infringement. It contains a latent ambiguity – what is the time of the first infringement? We now know, because the skeleton has made it very clear, that it is the time of the first infringement that Ofcom believes is the appropriate time for the assessment of market power, it is not the time of the infringement. Infringements can be carrying on until the crack of doom, what matters for Ofcom is the market position at the time that an infringement occurs. We are going to come on to say that this position is wrong in principle and that, if correct, it would deprive Article 82 of its effectiveness as a means of dealing with abuses of dominant position. But before we get to that particular point, could I just go back to the point that I was making, referring to the guidelines – A 35 in the authorities' bundle.

THE CHAIRMAN: That is the DG Competition Discussion Paper?

MR.HORNSBY: That is right. The bottom of p.9 –

> "Market power is the power to influence market prices, output, innovation, the variety and quality of goods and services, and other parameters of competition on the market for a significant period of time."

If you turn over and go to p.11, just look at para.29:

> "If market shares have fluctuated significantly over time it is an indication of effective competition."

If we go to para.31, and this quotes *Hoffmann-La-Roche* and we do not need to go there unless Ofcom insists, and I think it accurately describes what is said there. Paragraph 31:

> "It is very likely that very high market shares, which have been held for some time, indicate a dominant position."

These guidelines make it clear that the object of the exercise – looking at market share and the rest is to see what is happening in a market, and what is likely to happen in a market – the period of time is quite significant, it cannot be a short period of time. It should be a long period of time and we say that period of time should have included 2004 to 2007.

Can we have a brief look at the *Michelin* decision, it is at tab 8. *Michelin* is a very important decision under Article 82 in relation to rebates and *quasi* exclusive agreements entered into by a dominant company. If you would go to p.23, para.33:

> "In its decision the Commission relied upon the fact that from 1975 to 1980 Michelin NV's share of the market was …"

whatever it was. That decision was taken a couple of years later. If you go to the front, you will see that the decision was taken on 7th October, 1981. So, a decision taken in relation to on-going practices in 1981. A period relied on for looking at market power -

1975 - 1980. I am sure the Commission would say they were a bit slow to get it out, but the principle that is being illustrated there is quite a clear one: when you have ongoing behaviour a decision speaks of the market conditions that prevail at the time.

If you go to the end of that decision, at p.32, at para. 110 -- As far as the duration of the infringement is concerned it is common ground that the system at issue was applied during the period from no later than 1975 to 1980. There was a period when they did not apply it, and they did not get fined for that period. But, for the period in question, which was a period in the five years up to the point when the decision was taken, Michelin both had a dominant position and, by virtue of its quasi-exclusive contracts, abused that dominant position.

THE CHAIRMAN: What was the abuse that they were looking at there then? That was a discount system.

MR. HORNSBY: Quantity discounts on dealers which had the effect of foreclosing the tyre market.

THE CHAIRMAN: I suppose they were contractually bound to continue that discount system once they entered into a contract, unless and until it was declared unlawful.

MR. HORNSBY: Absolutely. One of the features of the fines was that Michelin said, "Well, actually the Commission has been a bit slow on this one. Had it told us earlier, then we would have brought these infringements to an end and the fine would be less". So, you get the flavour that it was an ongoing infringement. There was a contract there. The period of investigation was five years up until the moment when the decision took place. The decision did not come out as quickly as it perhaps ideally ought to have done, but, nevertheless, you do not see the great hiatus that typifies Ofcom's decision in this case.

There is more on this which I can take you to. There is the *Coca-Cola* decision. *Coca-Cola* was a merger decision.

THE CHAIRMAN: That was the underlying authority for that paragraph in **Bellamy & Child** which you took us to.

MR. HORNSBY: Yes. That basically says that the decisions are based on market conditions prevailing at the time. There is some ambiguity about what that time is. We say that time is when the decision actually takes place. So, we do not need to go there.

BSkyB. That is quite interesting because the *BSkyB* case was one in which the abuses were pricing abuses, and also they were abuses in relation to foreclosure. So, in many ways it is quite similar to the matters under consideration in this complaint. If we could just skip through *BSkyB*, the decision of the Office of Fair Trading, in the authorities bundle at Tab

26, you will see that there are certain important features in relation to the period under investigation. It is a decision, incidentally, where there was a finding of dominance but no abuse. It is quite interesting, and obviously of practical importance, as I imagine the hypothetical abuses are still matters of some complaint to the cable companies who did make this complaint in 2003. If you look at p.4 of the *BSkyB* decision, para. 17, the period investigated was from 1st March, 2000 until 30th June, 2001. This was in a decision that was handed down in December 2002. What the Office of Fair Trading did was look at the effect on competition of the practices complained of in that period - 1st March, 2000 to 30th June, 2001. If you go to p.7, para. 26, that is made quite clear.

> "This decision relates to conduct within the period from 1st March, 2000 until 30th June inclusive".

When you come up to the analysis of market shares, however -- If you go to p.68, there is a little table - market shares in the supply of premium films by subscription volume rather than value. You will see it is the three years prior to the decision effectively that market shares were examined. So, you have the Office of Fair Trading identifying a time when it looks at the effect on competition, and then identifying a longer period of time when it looks at the market shares and market power - both of those in ongoing practices and Sky continues to do mixed bundling, as far as I know, even now. As far as ongoing practice is concerned, the decision states the position at the date of the decision on the basis of an analysis of dominance in the three years leading up to the decision. It could have gone back further if the market had existed, but it was a relatively new market and it stopped I think in 1998.

That is Sky. I think there is just one more. It is not an authority, but it is one more matter that I just want to bring to your attention. That is in the authorities bundle. It is the modernisation regulation at Tab 32. Article 7 refers to findings of infringement and termination of infringements. It says,

> "Where the Commission, acting on a complaint or on its own initiative, finds that there is an infringement of Article 81 or 82 of the Treaty, it may by decision require the undertakings and associations of undertakings concerned to bring such infringement to an end."

There is an important final sentence in that.

> "If the Commission has a legitimate interest in doing so, it may also find that an infringement has been committed in the past".

We say that what that very strongly suggests is that when the Commission takes a decision it is taking decisions, unless it says otherwise, based upon conditions of the market or contracts which are ongoing at the time that the decision is taken. I want to just take you finally on this point to two examples where a historic decision was taken - historic in the sense that it addressed events that had passed. The first of those I do not want to take you to in any great detail - it is the Dutch oil case. That case looked at the issue of whether there was a dominant position in a situation of economic crisis where there was a shortage of supply. The Commission, perhaps because it wanted to be involved in energy policy, or something, was anxious to demonstrate that in a very short period of time the oil companies were collectively in a dominant position. That decision was appealed to the European Court of Justice and no finding was necessary on the point as it actually happened that the Advocate General doubted that a period so small as that under consideration was sufficient for a finding of dominance.

So, that is the sort of historic decision you can have where the market changes but you nevertheless want to establish a legal principle which gives you some power to intervene in the future.

The same sort of historic decision was taken in *Tetra I*, the BTG license decision. Tab 21 in the authorities bundle. (After a pause) That case involved the acquisition of an exclusive licence, and you probably do not need to have me repeat it.

If you go towards the end of the decision – this was an historic decision because Tetra renounced exclusivity. The Commission nevertheless said that it had had an interest because of the development of its case law to establish that a company in a dominant position could acquire an exclusive licence and abuse that dominant position for so long as it was exclusive, irrespective of the fact that the licence agreement itself fell within a block exemption. A very important case, and we say that this demonstrates that generally speaking the conditions of the market, at the time a decision takes place are the ones that matter, although in some exceptional circumstances decisions can take place in relation to historic events.

THE CHAIRMAN: But in this decision what was the point at which it was important that Tetra Pak was dominant – when it entered into the patent licence, or only subsequently? Where does it say what they decided as regards dominance?

MR.HORNSBY: It is in the annex, it is based on cartons sold in 1985. There was no reason to believe that the market shares had fluctuated to any significant degree, Tetra's position being super dominant, although that concept I do not think had been invented at that time.

So the relevant market is defined on p.7. The abuse was committed when it purchased Liquipak and Liquipak had this exclusive licence with BTG.

The analysis of dominance is rather sketchy – it starts at the bottom of p.12 and over to p.13:

> "91.8% of the EC market for machines capable of filling cartons by aseptic process with UHT-treated liquids."

THE CHAIRMAN: Yes they do not seem to tie it to any particular time, although at the beginning of para.45 they say:

> "Tetra committed an abuse of its dominant position when, through the purchase of the Liquipak Group, it acquired the exclusive licence from BTG"

MR. GREEN: (no microphone) … paragraphs 60 and 61.

THE CHAIRMAN: Yes.

MR.HORNSBY: "The abuse lasted until Tetra renounced all claims to this exclusivity", because at the time of the acquisition it occupied a dominant position.

PROFESSOR STONEMAN: Mr. Hornsby, just before you move on from that, are you saying that that translates into this case?

MR.HORNSBY: No, what I am saying is that that decision is an example of a decision based upon behaviour that is no longer being carried on at the time the decision is taken. That is, if you like, an historic decision.

THE CHAIRMAN: Yes, but it is relevant to this case in that, as with this case, it was looking at a particular contract, whereas it could be said in relation to *Michelin* and *BSkyB* it was looking at courses of conduct which might include entering into contracts, but continuing courses of conduct which do not start and end at a particular time, although the individual contracts entered into as part of that course of conduct do. But here, as in our case, they were looking at one particular agreement, and the exclusivity in that agreement.

MR.HORNSBY: Yes.

PROFESSOR STONEMAN: The point I wanted to raise was more to do with the fact that Tetra Pak was dominant at that point in time, and we have not established the fact yet that Red Bee was dominant at that point in time. There is a difference between abusing dominance and creating dominance, I think.

MR.HORNSBY: Yes, that is right, although actually we will come to that point, it is a very interesting and important point, and perhaps the point is now when we should come to it. If we go to Ofcom's skeleton now ----

THE CHAIRMAN: Before you leave *Tetra Pak* I just want to see what they said in relation to the Article 85, as it then was. (After a pause) Yes.

MR.HORNSBY: If we go to the skeleton argument of Ofcom, tab 15, para. 10, second sentence:

> "Whether or not BBCB became dominant partly as a consequence of its alleged abusive conduct is irrelevant to whether BBCB was dominant at the time when that conduct occurred."

There is quite a lot of meat in this sentence: "when that conduct occurred" contains again this latent ambiguity about whether it is the time that the conduct first occurs, or whether it is the time that the conduct is continuing to occur. What is basically being said, as I understand it, is for the sake of, for example let us suppose someone acquires a dominant position – and this is your point - if he is not dominant when he acquires that dominant position that is okay. This can be tested against the following hypothetical example: suppose a bus company with a small market share in a city – Edinburgh – wants to enter the market and expel the existing incumbent operators what it does is to lay on a lot of services, because that is what you do, that is predatory pricing in the bus market. It lays on a lot of services in competition with the incumbent. These services are at prices that in no way cover its costs. As a result of that activity the incumbent leaves the market. Those service levels are maintained for years. Attempts are made to enter the market by other bus companies; they fail. Mr. Anderson's argument would mean, if it were correct, that in that particular circumstance it would not be an abuse of a dominant position to have laid on these extra services beneath cost, because at the time of laying on those extra services beneath costs the company doing it was not in a dominant position. Now, that is not our case because we say that already BBCB had a position of dominance, which was 40 per cent, and it got the Channel 4 contract we say – or we said in our complaint – unlawfully by the cross-subsidy.

But Mr. Anderson's argument, taken to its logical conclusion, is that you have, if you like, a grandfathering of abuses. There are some abuses which can be attacked, and then there are other abuses which cannot be attacked because at the time you committed them you were not in a dominant position, you did not have the special responsibility that is incumbent upon dominant companies and therefore you were able to enter into practices which are perfectly legitimate for non-dominant companies.

There are a couple of problems with this. The first of these is that abuse of dominance is not just the abuse of a dominant position when you have that dominant position, it can change, it can fluctuate. Behaviour that was non-abusive when you were not in a dominant

position can become abusive when you are in a dominant position. So in the example that I have just given what you would say, properly analysed we say, is that the maintenance of prices beneath marginal cost, which is reflected by the service levels which make no kind of recovery, was an abuse of a dominant position. A dominant position was being maintained by abusive practices.

We say that that cannot be right – simply that cannot be right – that Article 82 creates an obligation of special responsibility on dominant companies, which ebbs and wanes; sometimes a company may be in a dominant position, sometimes it may not be. If it is not in a dominant position at a given moment then it can enter into practices or agreements with equanimity if not impunity. But that only lasts as long as it is not in a dominant position and the time that it is in a dominant position it is subject to Article 82, and the obligation not to abuse that dominant position by maintaining practices which restrict competition.

THE CHAIRMAN: So what does that mean then in relation to contractually binding terms? You say even if they were not dominant at the time that they entered into the Channel 4 contract – of course you say they were, but even if they were not – the prices set by that contract were predatory, and although that would not have been an abuse when they were not dominant when they concluded the contract, at some point during the currency of the contract they become dominant, and therefore they have to not charge those prices any more. But what does that do then as between the parties, because if they were to go back to Channel 4 and say: "I am terribly sorry, this great bargain that we have given you now that we are dominant we are going to have to double our price so that it is not predatory any more". Channel 4 might not be very happy about that. I can see it working when the prices are excessive and they are brought down. But, how does that work contractually then?

MR. HORNSBY: It works extremely unsatisfactorily from a contractual point of view. But, that is the consequence of the case law. One of the things that happens when companies buy other companies is that warranties are sought in relation to contracts that are currently held by the company that is acquired with a view to establishing whether there will be a problem with, for example, exclusivity when there is a change of ownership. So, after the *Tetra I* decision, for example, lawyers dealing in this particular area would have been advising their clients to establish that if they were purchasing a company that had an exclusive agreement attached to it, and the acquiring company had a strong, or dominant, position, that following *Tetra Pak* what it might have to do is to renounce that exclusivity or run the risk that it would be subject to the kind of procedure that the Commission took in the *Tetra I* decision.

This is the same kind of process that happens in Article 81. Above the 30 percent threshold things change. We will come on to that when we look, if you like, at Part 2. However, our case in relation to Part 1 is that not only is this wrong - the choosing of this short period - but it could never be right. It could never be right because, in principle you could not have a situation in which contracts were continued by dominant companies which were an abuse of that dominant position, but in this argument were not abuses because at the time they were entered into the company was not a dominant company.

Now, if you spin it the other way around, you can see that there are also problems with the proposition advanced by Ofcom and Mr. Anderson. If you go to the IMS skeleton at para. 17,

> "The fundamental error of Ofcom's choice of the relevant period of time can be demonstrated in a different way by hypothesising what the regulatory outcome would have been had BBCB been held to be dominant somewhere in the first part of 2004 and further hypothesising that abuses were held to have been committed by predatory and discriminatory pricing and the non-compete contained in the Channel 4 contract. In this scenario, the duration of the abusive infringements would have had to have been considered by Ofcom. It is axiomatic that there can be no abuse without a dominant position having been established; it therefore follows that if Ofcom were to be right in its selection of so short a period of time but reached a different conclusion the hypothetical abuses could only have had a duration of six months irrespective of the fact that pricing may have continued (and the non-compete did continue) way beyond that point. We say the absurdity of the logical consequence demonstrates the flaw in Ofcom's approach".

You simply cannot take the position that Ofcom is taking here. Ofcom hamstrung itself by choosing this short period of time. It was a process with only one outcome. Had it decided that there actually was a dominant position in 2004, it would not have been able to take a decision in 2007 that could have stood up. The interveners would have been able to say, with some justification, and Channel 4 as well, that "Then was then. Now is now". There was only a dominant position in relation to this contract at that particular point, and therefore there can be no remedy now based upon the need to comply with the decision in 2007. There just is not a dominant position at that point.

So, to answer that, Ofcom would have had to have gone back and taken another decision, and they would have had to have updated the analysis in respect of the Channel 4 contract, and it would have had to have reached the point where it said, "As of now, right here, right

now [either in 2007 or in 2008] a dominant position is enjoyed by Red Bee. This contract constitutes an abuse of it. We wish this infringement to be brought to an end".

MR. BLAIR: That is the very decision you seem to be seeking out of them, is it not? Your argument is about a timing period -- a choice of a period of time. But, actually, if you compare your skeleton with the Ofcom skeleton what you are actually wanting to have is a decision that in 2007 they were by then dominant and therefore were abusing the position they had obtained in 2004. You are actually asking for a different decision from the one that was actually made.

MR. HORNSBY: We are saying that the decision in relation to dominance -- There should have been the updating that happened in relation to the Article 81 analysis. Ofcom, when looking at the Channel 4 contract under Article 81, could no longer refer to market conditions at the time the contract was entered into because subsequent to then the situation had changed and on any view Red Bee had a market position of more than 35 percent such that it could not take advantage of the block exemption any more.

What we are saying is that consistent with that analysis there should have been an updating in relation to Article 82. There is some authority on that which I would just like to come to.

THE CHAIRMAN: What you are saying really amounts to saying that Ofcom mis-characterised the abuse in that the abuse was not really entering into a contract at which prices were set at a predatory level, or at which there was exclusivity, but rather that it was charging prices which were predatory, or having an exclusive agreement with Channel 4 - practices which continued throughout the duration of the contract - and that if at some point Red Bee becomes dominant over the period of that contract then those practices become something which, as an undertaking with a special responsibility, it must discontinue.

MR. HORNSBY: Yes. We are asking for nothing in these proceedings in relation to abuses.

What we are simply saying is that in relation to dominance ----

THE CHAIRMAN: Yes, but how you look at dominance has to depend on the way in which ----

MR. HORNSBY: Sometimes it does, but we say that the two do not go hand in glove in the same way that Ofcom think that it does. Ofcom says, "You just look at the dominant position at the time the alleged abuses happened." We say that there is a reason why you need to look at the market over a longer period of time than that, and that what you should do is to take decisions that reflect prevailing market conditions at the time the decision is taken, and unless you are taking specifically historical decisions where you wish to establish a precedent.

It is the nature of this area of law that the analysis of a contract depends upon the market share and the companies that are parties to it. That may change in the course of time. When we look at the Article 81 analysis we will see why it was no longer appropriate to rely on the block exemption and the *de minimis* notice. The reason that we drew attention to the fact that the first time round Ofcom did not take this into account was not merely to point out that Ofcom got it wrong, but it is to actually establish the nature of the exercise that you must do. If an abusive practice is continuing, when you take a decision in respect of that you cannot just cut off your analysis of the dominant position and say, "Beyond 2004 [whenever it is] we are not looking at it any more". You have to roll it forward to the point where you actually take that decision and the *Sky* and the *Michelin* decisions demonstrate that quite clearly. They look over a long period of time at these particular contracts, and they make an analysis of the market share, and they make their findings of abuse. In the *Sky* case there was no abuse, and so the practices continue. In the *Michelin* case the practices were held to be abuses. The infringement decision was taken. A fine was imposed based upon an abuse of a dominant position within the period that there was a dominant position. The argument offered by Ofcom does not really allow that to happen in a situation where there is no pre-existing dominant position. That creates a legal hiatus, if you like. There is a gap. There are lots of cases on the maintenance of a dominant position by abusive behaviour. Those cases would no longer be able to be brought because a company under investigation would say, "Well, actually, I started this. I was not dominant at the time. I may well have got a dominant position as a result of that, but at the time of the infringement I was not dominant". That, we say, is a clear fallacy.

My final point now is really in relation to consistency with Article 81.

MR. BLAIR: Before we go there, we were looking at the Ofcom skeleton. Can I take you to para. 4 of the Ofcom skeleton? "For the purposes of determining IMS' appeal --" It says, "-- the alleged infringement". So, this is the infringement alleged by IMS. The infringement was that 'BBCB had infringed the Chapter II prohibition by securing the Channel 4 contract'. Now, do you say that was not the alleged infringement because the emphasis there is on securing the contract? You could have had an alleged infringement that says, "The alleged infringement was the charging of prices post 2005 that were predatory", or whatever. Do you accept, or do you not accept, this Ofcom version of what the alleged infringement was?

MR. HORNSBY: I do not accept it. We say that it secured the contract by predatory pricing. The offer was very, very low - beneath marginal costs. But, we also say that as a result of it

being an exclusive contract it not only secured the contract, but it maintains, and continues to maintain, we say, that contract and that is an abuse of a dominant position.

MR. BLAIR: I just want to get it clear. It is very important, this point. You are saying that the alleged infringement was in fact in two parts - one was securing the contract at these prices that are too low -- predatory -- or whatever; the other one is by operating the contract at those prices after it has been secured.

MR. HORNSBY: Yes - and also on an exclusive basis.

MR. BLAIR: On an exclusive basis.

MR. HORNSBY: On an exclusive basis, yes. The contract is ongoing as we speak.

MR. BLAIR: Yes We are very well aware of that. We will leave it at that point because that clarifies your stance. Thank you.

THE CHAIRMAN: Let me just push that a tiny bit further. Therefore, you say that even if it is the case that they have to be dominant for the securing of the contract point at the time they secure the contract, as far as the continuing aspect of the infringement is concerned it is enough if they become dominant at some point. Now, whether it matters that they become dominant because of this contract or through other changes in the market may well not matter to you.

MR. HORNSBY: That is correct. That is how I would characterise it. You can also turn it the other way around: a company, for example, which is dominant as a result of the possession of patents may decide, because it has special responsibility not to impede competition -- it may decide that it does not want to enter into exclusive agreements. Now, next year the patents come to an end. All kinds of new entry to the market - say it is drugs. The generics can come in and take away a large proportion of the market share of the dominant company. At that point, if you are advising a dominant company, you can say to the management, "You are now no longer dominant because your patent protection, which gives you the market power, has gone. You can now start entering into different sorts of contracts from those that you were able to enter into when you had the special responsibility because the special responsibility has gone". So, you go up and down with the tide - sometimes you are dominant and you cannot behave in a certain way; other times you are no longer dominant and at that point you become free to act in certain ways. It is the same with Article 81. You can be absolutely certain that if you are underneath 30 percent of the relevant market share, that unless you have some clauses in like re-sale price maintenance, or something like that, which are so-called black clauses -- you can enter into non-compete agreements or exclusive agreements. Those are block exempt. But, once you go beyond 30 percent, you

can no longer have that security. You have to do a full market analysis, and in some circumstances it may be the case that you are actually not entitled to carry on with those particular agreements. I quoted *Tetra* because that was an example. Now, had the exclusive contract been acquired by another company that did not have a dominant position then there would not have been an issue; because it did not have a dominant position it could have an exclusive contract that fell within the block exemption without any problems, but because it was Tetra, a super dominant company, and had been dominant for years, and had all the technological advantages and all the rest of it, and was likely to have those advantages for a considerable amount of time, that contract was not one that the Commission was able to say fell outside Article 82 as it then was. Even though it fell within the block exemption it prohibited that contract, and it prohibited that contract even though there had been a renunciation of exclusivity.

We say that 82, as put together by Ofcom is not a legal instrument which it was intended to be, and the final point will be that the interpretation of Ofcom will not be consistent with Article 81, and for that I just need to go back to *Tetra* again, please.

MR. BLAIR: I was just going to say, you were talking about going up and down with the tide, but your argument is much more extreme than even the *Tetra 1* case, because you are saying that they have to go up and down with the next tide but two, and it might well be a much higher tide. In other words, you enter into a contract which is perfectly okay at the time, and the legal adviser ought to say – on your case – "You must not enter into this contract, it is far too good from your point of view. There is a risk that you will be dominant during the life of this contract and you may not be able to get out of it, so you had better not enter into it now". Is that really what you are saying?

MR.HORNSBY: No, I am not saying that because I do not think any legal adviser would carry any conviction with his client if he said that some years down the line you might be dominant, and therefore you will have to look at this one again. I think what clients want to know is what the situation is now and in the foreseeable future, and what the block exemptions do is to give you some guidance about that. They give you some legal safe harbour. Now, I think Ofcom does accept that the Channel 4 contract does not take the benefit of the legal safe harbour and it does so as a result of the change in ownership, and the fact that the in-house sales are now no longer in-house sales, but have to be taken into account.

When Red Bee acquired BCCB I imagine its advisers would have looked at the contracts that BCCB had and one of the things I would have expected them to say, and one of the

things I would certainly have said if I had been in their position, would be that the Channel 4 contract will not take advantage of the block exemption in a couple of years' time. You would not say at that point: "Well actually you should be cancelled now". What you would say is that there would have to be a full analysis done as to whether that contract fell within Article 81(1) or not; you have to start generating some justifications for that contract. If you felt that that contract did not have such justifications what you would consider doing is raising the issue with your partner as to whether it could continue to be exclusive or whether it should not in fact revert to being non-exclusive. That is the nature of competition law advice, you advise your clients based upon the situation at the time, but you also warn them that when their market share changes, so the analysis of it may change. As I said, you can do this in two particular ways. A client can say: "Well, my patent protection comes to an end in two years' time, can I do X or Y?" Currently you are in a dominant position and the answer is that you ought to be very careful, but in two years' time all these generic products will flood into the market and at that point you are free, you no longer have the special responsibility. So the going up and down with the tide is a function of how these legislative provisions work.

The final point is more or less covered, but if we could just go to *Tetra* again. I think the best way of doing that will actually be to go to A.37, which is the **Bellamy & Child** extract, it is p.913, para.10.006.

> "Articles [81] and [82] are complementary inasmuch as they pursue a common general objective set out in Article 3[1][g] of the Treaty, which provides that the activities of the Community are to include ' the institution of a system ensuring that competition in the common market is not distorted'. But they none the less constitute, in the scheme of the Treaty, two independent legal instruments addressing different situations."

We say that if Ofcom is right in its analysis you have quite an extraordinary outcome. The complaint that IMS originally made about the Channel 4 contract was both under Article 82 and under Article 81. The exclusive nature of the contract we considered to be an abuse under Article 82, we had to do that because there was the argument, of course, about in-house sales, and therefore if in-house sales could not be taken into account under Article 81 we needed some way of demonstrating that it was nevertheless an infringement of competition, so we put in a complaint in relation to Article 82 as well.

If Ofcom is right, you do an analysis of market power. On the same facts you do an analysis of market power in relation to the Article 82 issue at the time the contract was

entered into or when it was bid for, but if some way down the track Article 81, if you like, raises its ugly head because a block exemption is no longer available, and an individual exemption has to be considered, looking at the market at that particular point in time you have to reach a conclusion on the same contract, so you actually shoot off in two different directions, and that, we say, is what Ofcom has done here. It has done an analysis of Article 82, based upon one period of time, and has had necessarily to do a different analysis of the same contract under Article 81 based on the conditions of competition in 2007. We say that is simply nonsense; it cannot be done when Articles 81 and 82 have the same function, although they are, of course, different legal provisions.

Now why does all this matter? We say it matters a great deal. It matters because if you do the analysis over the correct period of time the market share enjoyed by now Red Bee is over 50 per cent and growing. When you are in that area there is a presumption of dominance, and at that point you must be absolutely convinced that the evidence that you adduce to rebutting that presumption is sound. We say the inclusion of Intelfax by this – what might be a device, but it might not be – of looking at the situation in 2004 actually distorts the analysis and the analysis is wrong as a result. Ofcom misdirected itself on what it needed to do to examine whether a position of dominance existed in the market. Clearly, it is for IMS to show that there is a position of dominance, but the management presentation in 2005 on Red Bee's website in our view clearly demonstrates that, as of November 2005 (and for the foreseeable future), it is not something that is likely to change a great deal, was a strong one.

THE CHAIRMAN: But are you saying that they were wrong to include Intelfax even insofar as they were looking at the position before the contract was entered into? Or only insofar as they ought to have looked at the market position subsequent to that?

MR.HORNSBY: Well the inclusion of Intelfax has some kind of logic before the contract was entered into but at that particular point in time no one would know whether Intelfax was actually going to carry on or not; there was nothing to suggest at that point that his future was menaced. But once the contract had been won at that point it was quite clear that Intelfax had to find something else to do or go out of business.

THE CHAIRMAN: But you are not saying that even if they had won the Channel 4 contract they would still have gone out of business?

MR.HORNSBY: Oh no, the complaint is only directed towards the fact that Intelfax lost, and we say it lost as a result of an abuse of a dominant position, and that is not something we are pursuing in these proceedings. What we are simply seeking to establish is that the material

time, which we say is the time when the decision was taken, Red Bee or BBCB was in a dominant position, and that has consequences in relation to the Article 81 analysis going forward, which should have been taken into account but were not – we say – in the analysis under Article 81. The Channel 4 contract should have taken into account – we say – that there was a 50 per cent plus market share, and in circumstances like that the maintenance of exclusivity – the maintenance of exclusivity – is something which restricts competition within the meaning of Article 81(1).

We say that this mistake, this error flows through the whole analysis, and the correctness of our analysis, we say, is demonstrated by the fact that when you look at the Article 81 situation as from 2007 you have to do an update. We will come on probably this afternoon as to why the update was itself wrong. But nevertheless, Articles 81 and 82 have a similar goal, and it is absurd that in analysing the same contract under Articles 82 and 81, you look under 82 at a period of three years prior to the period you look at that same contract under Article 81; it does not make any sense at all – quite apart from the other issues of principle which we say are raised by this idea that you can acquire a dominant position by abusive behaviour but so long as you are not actually dominant at the time you acquire it then there is nothing that can be done. We say that demonstrates why the analysis is wrong as well.

So our problems with the decision are both general and particular. We think that the wrong period of time has been chosen and that feeds through to the whole analysis. What you have is the existence of a fourth competitor embedded in this decision, when that competitor went out of business three years ago; that in fact the market is one where there are three suppliers not four, and one where there has been no entry since then on an independent basis. There has been this joint venture with Wordwave, but there has been nothing else.

Therefore we say the structural analysis on which Ofcom based its decision is wrong. It started from an incorrect perception of what its duty was when it took its decision. What it should have done is analysed the conditions of competition prevailing at the time it took a decision, not go back four years, avert its eyes to the disappearance of Intelfax and reach a conclusion then, it should have reached the proper conclusion in 2007, and that conclusion, had it reached it, would have been very similar to the picture painted by Red Bee itself when it made its management presentation in November 2005 - a market share of 53 percent at that point by volume. That only included actually three months of sales from Channel 4. So, probably erring on the side of caution there.

On burden of proof the *Freeserve* test - you are aware of it - we believe we have discharged it. For the reasons we have said, we do not believe the decision to Article 82 can stand.

There are many reasons why it should not stand. It would be very dangerous, we believe, if it were to stand.

THE CHAIRMAN: Have you come to the end of your submissions?

MR. HORNSBY: Only in relation to the first part.

THE CHAIRMAN: What are you coming on to next then, Mr. Hornsby?

MR. HORNSBY: The analysis of the Channel 4 contract post 2007. The second part of the relief that we sought. The first was to establish that from 2004 to 2007 - the time when it took the decision that BBC Red Bee occupied a dominant position; the second point was to contest and seek a contrary declaration in respect of the finding that Article 81(1) was not infringed by the Channel 4 contract, and is not infringed by the Channel 4 contract.

THE CHAIRMAN: The point about the inclusion or exclusion of the in-house supply ----

MR. HORNSBY: That has now gone. If we are looking at the Channel 4 contract from 2007 it is the fact that they are now no longer in-house that means that the block exemption and the *de minimis* notice do not apply any more.

THE CHAIRMAN: Looking at the question of dominance for Article 82, doesn't the question whether Red Bee was dominant in the first part of 2004 depend on whether you include or exclude in-house supply?

MR. ANDERSON: Madam Chairman, we looked at dominance in 2004 on both bases - both including and excluding in-house supplies, and concluding that even if you included the in-house supplies, with a market share of 30 to 40 percent (whatever it was) they were still not dominant.

THE CHAIRMAN: Thank you.

MR. BLAIR: Perhaps I could follow that up. You have been arguing that those market shares should have been evaluated in a three/four year period - not just for 2004. Do you have any evidence that if Ofcom had looked back to 2001 that they would have found that there was dominance?

MR. HORNSBY: That would have depended upon obviously the market shares at that particular point. I think that what can be said about the BBC broadcast is that coming up to the time when it put itself out for sale it had not been very successful in gaining any business other than that of the BBC. That is specifically recorded in the decision. So, it may well have been the case that at that point the market share was slightly less. Also, in the past my understanding is that BBCB did not have -- The agreements were not exclusive. So, for example, IMS has, in the past, supplied these services to the BBC.

MR. BLAIR: So, although you have these arguments that we should look over, say, a three or four year period, you have no evidence to show that the 2004 result would have been changed as a result of not looking over that period.

MR. HORNSBY: No.

In relation to the Channel 4 analysis under Article 81, if we could go to the vertical restraint guidelines which is in the authorities bundle at Tab 30 -- Just looking at the table of contents for a moment, p.2 of the table of contents -- If we look at 1.4.2 it says, "Relevant factors for the assessment under Article 81(3)". Those paragraphs are 137 to 229. It is common ground, I believe, with Ofcom now that the block exemption does not apply any more to the Channel 4 agreement and that the *de minimis* notice does not apply either. Ofcom has not been specific on what it thinks the market share enjoyed by Red Bee is, but it says that it is more than 35 percent in the decision.

If you could now turn to para. 135 of the vertical restraints guidelines -- This is a sort of introductory paragraph before going on to discuss Article 81(3) considerations.

"The last criterion of elimination of competition for a substantial part of the products in question is related to the question of dominance. Where an undertaking is dominant or becoming dominant as a consequence of the vertical agreement, a vertical restraint that has appreciable anti-competitive effects can in principle not be exempted. The vertical agreement may however fall outside Article 81(1) if there is an objective justification, for instance, if it is necessary for the protection of relationship-specific investments or for the transfer of substantial know-how without which the supply or purchase of certain goods or services would not take place".

What we say is really quite simple on this point: we say that Red Bee is dominant, or is approaching dominance even if we are wrong on whether it is dominant or not. Therefore, unless there are any efficiency justifications contained in the decision you cannot hold that this decision is one that is an Article 81(1) negative clearance, in effect, in the old language. In these particular circumstances you have to go on to look and see whether the Article 81(3) criteria are satisfied. The decision does not contain any Article 81(3) analysis because it does not have to in its own terms. All based on Article 81(1).

We did think in the course of the administrative proceedings that there would be some efficiency justification put forward for the Channel 4 contract. At one of the meetings Ofcom did say, "Oh, well, a very long term contract - fifteen years, for example, which is investment-specific - can fall outside Article 81(1) even though it is very long term". But, none of that actually fed through into the decision itself. The decision itself - and it could

not do anything else actually because Ofcom was at this point on the hook really -- It had to take a decision that Article 81(1) was not infringed because it was all geared up to take this decision in relation to Article 82. The drafts were circulated ----

THE CHAIRMAN: We cannot really speculate as to the background.

MR. HORNSBY: No. I am just saying why the decision has to be on the basis of Article 81(1).

THE CHAIRMAN: We need to look at the reasoning in the decision and see whether that stands up.

MR. HORNSBY: Shall we now do that? If we go to the documents bundle and look at the version of the decision at Tab 3.3 -----

MR. ANDERSON: This has been a constant theme of Mr. Hornsby's submissions. The relevant decision under appeal is the one at 3.1 - not the version at 3.2 (which is a draft decision) or 3.3 (which is his highlighted comparison of the two).

MR. HORNSBY: Yes. In relation to that, the decision is in fact no different in 3.3. What you have is underlining which is actually, I believe, quite helpful and not really contested. That demonstrates what was new, if you like. If it is a problem, I will go back to the decision as published. But, if you look at the version at 3.3 what it does demonstrate is before and after, if you like - the decision that Ofcom envisaged taking and the decisions it had to take when it apprehended that the analysis that it needed to do was in 2007. I do not make anything of it. I just find it helpful to look at the underlined passages because they show what analysis Ofcom then did.

THE CHAIRMAN: Let us go through the actual published version, and if there is something that you feel you need to take us to in the other versions, then we will deal with that if and when it arises.

MR. HORNSBY: If you go to 8.16. This was dealt with in some detail in the skeleton.

THE CHAIRMAN: This is a paragraph starting, "Ofcom's analysis ----"

MR. HORNSBY: That is right, yes. Ofcom repeats, if you like, the analysis of the market that it has made in the decision. It says that there are at least three access service providers. Actually there are only three. This is the Intelfax point. It says that buyers have a significant degree of countervailing power at their disposal. The contracts are awarded infrequently. It goes on to conclude,

> "Taking into account the nature of the products and services in question and the duration of the remaining non-compete obligation after the contract loses the benefit of the block exemption has concluded that the remaining term of the non-compete obligation would be unlikely to have the effect of appreciably restricting

> competition in the relevant market. Any cumulative impact of the agreements would not alter this conclusion".

The same point is made in the skeleton of Ofcom. They basically say three years -- We will come on to the issue of whether it really is three years. Three years is a bagatelle. It does not matter. The duration is just really too short. The importance of the contract is really too little.

Ofcom does not cite any authority for the proposition that a contract of three years' duration which counts for 10 percent of the market does not appreciably restrict competition.

But, there is a relevant case which I would like to draw the Tribunal's attention to. That is the Finnish petrol station case. That can be found at Tab 17. This was a case where there were a large number of contracts which had collectively a foreclosing effect on the market. But, some contracts had to be distinguished in treatment because they were slightly different from the large majority of the contracts that created this foreclosing effect. If you go to para. A35 -- This is the Advocate General. It is a 177 case (or whatever they are called now) - a reference from the national court. The judgment is not particularly full -- Well, it is not full. It is pretty concise. If you look at A35 I think you can spell out what the rationale was for the decision that was taken.

> "In summary, I am satisfied, at least in respect of exclusive purchasing agreement sin the service station sector, where it is common ground that competition is essentially limited to inter-brand price competition and where it is also clear, unlike, for example, in the beer and ice-cream markets, that there is little or only insignificant brand loyalty among consumers, that an agreement concluded by a supplier which may be terminated by the reseller at any time simply by giving one year's notice is not similar to other fixed-term agreements which tie the reseller to the supplier for significantly longer periods of time. Such agreements, where they constitute a small minority of that supplier's network of agreements and where they genuinely permit the reseller readily to switch suppliers, should be assessed separately by national courts".

So, when it actually came to it the argument of the Advocate General was accepted by the court and they held in the sense that the Advocate General had indicated.

What is interesting though there about the finding that those particular contracts - accounting as they did for a small part of the total number of contracts in the station market - did not fall within Article 81(1) - was that this was a market where there was insignificant

brand loyalty among consumers. Now, what Ofcom's decision makes absolutely clear is that brand loyalty and reputation is extremely important in this particular market.

THE CHAIRMAN: The point they were making there was that because there was no brand loyalty it was realistic to think that parties might actually exercise the option of terminating after a year. That was why these were different from longer term contracts.

MR. HORNSBY: Absolutely. Absolutely. The notice period was twelve months. We have a situation here where the Channel 4 contract is, on any view, of a duration of three years, where Ofcom has found that brand loyalty is a significant factor with new entrants finding it difficult to get into because there is this reputational barrier that has to be overcome according to Ofcom. So, that is a fact which has been found in the decision.

So, this decision is as far as the law has gone on Article 81(1) not being infringed by an agreement that falls outside the block exemption, or where there is a high market share enjoyed by the operator. That is a situation where you have twelve months' notice to go, and where there is no brand loyalty.

So, we say that it is simply not sufficient on the basis of binding authority to say that there is a three year agreement and no notice before then may be given, which accounts for 10 percent of the relevant market, and where there is significant brand loyalty or reputational barrier to entry. We think that that is clearly within Article 81(1) unless there is an efficiency justification for it. The decision contains no efficiency justification for it, and therefore the decision cannot stand.

THE CHAIRMAN: I think that probably is a convenient moment to break, Mr. Hornsby.

(Adjourned for a short time)

MR.HORNSBY: I had just finished dealing with the issue of whether Article 81 applied to an agreement in these circumstances which was of a three year duration, and we are now, as far as IMS at least is concerned, going to enter rather difficult territory because we are addressing now the issue of whether the agreement is actually three years or whether it is a longer period than three years, or is likely to be a longer period than three years. We are trying to deal with the issue of whether there is a material disincentive to terminate something and we have obviously not had an opportunity to see this arrangement and therefore it is extremely difficult for us to really make any meaningful submissions in respect of this, which I am sure you will appreciate.

I would say one thing to begin with, it must be – surely – common ground between the parties that the existence of this arrangement does make it more difficult than would otherwise be the case for IMS or ITFC to get the business, and therefore more likely

perhaps that, all things being equal, Channel 4 will retain it. Were it not to exist there would be certainly a level playing field. The extent to which it is not level is something that we do not really have an answer to. As I have said to you, we have already submitted that three years is too long, but if we are to consider the CRF we are working on the hypothesis – and it can only be a hypothesis – that it is more difficult for us to get that business for the option period.

Before I get on to the point that you raised about the falling market, at a general level our case against the original contract was that it was an extremely low price and that that price was maintained by higher prices enjoyed internally. If that were to be the case, and that were to be the case going forward, and even in the last year of the contract therefore the Channel 4 price were to be a very low price, it would be, in our submission potentially fatal to any attempt of IMS or ITFC to get that business, the fact that the contract renewal fee was between 3 and 5 per cent; it could be the difference between making any margin at all, and not covering our costs. So we have made that as a general submission, we do not know for sure what the price is, we suspect that it is a very low price – 3 per cent of a very low price if we are to win. It could mean that, assuming equal efficiency, that IMS would be put in a position where it could match and therefore stand a chance of winning this contract, or it could put us into a loss.

Rather more specifically you raised the issue of this is going to be less of an obstacle in a market where the price is falling. Well, just let us pause there for a second. First, I think it is too broad a brush to say that the market price is falling. I think we certainly know that the free market price is falling, that is reflected in the Ofcom skeleton in which one of the footnotes refers to the fact that a major customer managed to renew the contract at a very much lower price than previously existed. So I think we can say in the free market that prices have fallen principally as a result of the level at which BBC Broadcast obtained the Channel 4 business, but whether they are actually falling across the board is another matter altogether, we do not have any information on the internal prices being charged by Red Bee to the BBC, and part of our complaint related to that.

As specific as perhaps we can be, just looking at the scenario (which is not one we think is likely) that the Channel 4 price is, in its last year, much higher than the market price. Let us see how that would work through. The figure that we are talking about is based on the last year that is expected. So assume that the price for the last year of the Channel 4 contract is £200 per hour – just assume that for a second – and assume that the market price at that point is £100 per hour. For IMS and ITFC to be on an equal footing with Red Bee in

respect of this extra three years of business which is potentially up for grabs what we would have to do, and what ITFC would have to do, is offer more than 3 per cent (or something like 3 per cent) of 200, that is the price in the last year. Now, if we are having to offer that price then on our calculations Red Bee to retain the business can actually charge £95 an hour and when it charges that level it will be in a position where Channel 4 would be worse off going with us than it would be with Red Bee. It is not automatically the case that the falling market results in it being easy for IMS to win the business if you take those figures that I have just given.

THE CHAIRMAN: But does that not depend on what price prevails after renewal. If the contract price is £200 and the market price is now £100, then if the contract says that the option to renew is at the £200 price then it is an easy decision for Channel 4 to take, they say "Well clearly we do not want to continue paying £200 for the next three years, we will pay the £3, or whatever it is, to get out of this contract, and tender it and get a further three years at £100." So there it is very easy for IMS to compete, to beat the fee. The problem is whether the Channel 4 contract says; "There is a renegotiation" and everybody offers £100, and so we get in all these offers of £100 including one from Red Bee. But we know if we go to somebody else other than Red Bee we have to pay Red Bee the £3, and in that case Red Bee can bid £100 an hour and everybody else has to bid £97 an hour because they have to compensate for the fact that if they win the contract Channel 4 has to pay the £3 to Red Bee. So it does seem to me crucial whether the renewal of the contract, the price at which the contract is renewed, is the old price, or whether it is a renegotiated price going forward, because if it is the old price then the amount of the fee is, in a falling market, not going to be sufficient to make it beneficial to stick with that price rather than go with somebody else's better price. It is a bit unfair to ask you, I know, because you do not know what the terms of the contract are, but that perhaps just expresses our thought at the moment. Perhaps you make what submissions you wish and then of course you will have a chance t o come back once we have heard from the other parties who may clarify.

MR.HORNSBY: Yes, I think all we can say is that between 3 and 5 per cent might make an awful lot of difference.

THE CHAIRMAN: Certainly if you are right that this is a very low price, although the price now might be, say, 70, even though the market is now 100 and then of course there is the incentive – it is difficult for other companies to match that price, partly because it is a very low price and partly because of the fee.

MR.HORNSBY: Also partly because Red Bee will be at that point, on any view, retaining the benefit of the BBC business; that contract goes on until at least 2012, so that contract gives it the opportunity to spread the costs in a way that is not available to those who do not have that advantage.

THE CHAIRMAN: Can I just clarify something? You referred to the "free market price" as falling, what do you mean by the "free market price"?

MR.HORNSBY: By the "free market" I mean simply what the likes of Sky and Channel 5 are paying.

THE CHAIRMAN: And are those publicly known?

MR.HORNSBY: They are not publicly known, but Ofcom in the course of its investigation – and I will refer you to the section of the skeleton ----

THE CHAIRMAN: And did I understand that you were saying that those prices were influenced by the price that is paid by Channel 4 under this contract that we are considering?

MR.HORNSBY: In my client's view, yes, it was as night follows day in effect, Sky obviously, as a very strong negotiator, was able to point to this contract and definitely the word in the market place was that BBCB had won this business at a low price and that became, if you like, the index of prices available, or the ball park prices that were payable thereafter, obviously having a major impact on the profitability of IMS which, of course, is not a relevant consideration for the Tribunal.

If I could just perhaps refer the Tribunal to the relevant footnote ----

MR. BLAIR: Are you going to the Ofcom skeleton?

MR.HORNSBY: Yes, it is tab 15, footnote 8 on p.7. …. (pause) Referring to it, there are indications that the market price for those services has fallen in recent years were expected to fall further. You go to (viii) and it says,

> "The indications were drawn from the information provided to Ofcom. At least two broadcasters on one access service provider - see the Channel 4 decision. In addition, Ofcom was also aware at the time of the decision that at least one UK broadcaster had been able to re-negotiate the price for certain access services provided by an existing supplier, thereby achieving a very significant reduction in price".

I do not think there is any point in me referring to the sections in the guidelines which deal with the issue of loan. We do not know what we are shooting at. So, until we do, or if we ever do, I do not think we have got very much to add there.

THE CHAIRMAN: You refer to it as a contract renewal fee. However, in para. 14 it is referred to as the cost reimbursement fee. Is there a settled industry, "It is just whatever anybody wants to call it, and then abbreviate?"

MR. HORNSBY: I think we just got it wrong.

THE CHAIRMAN: It is the cost reimbursement fee issue generally, is it?

MR. HORNSBY: Yes.

THE CHAIRMAN: Thank you.

MR. HORNSBY: Madam, unless there is anything that I can assist you with further, those are our submissions.

THE CHAIRMAN: Mr. Anderson, are you going next?

MR. ANDERSON: I am entirely in your hands. I was planning to as primary respondent. But it is entirely as you wish.

We have served a very comprehensive defence with quite a full skeleton argument. I am not proposing to repeat everything in those. But, of course, we rely upon the contents of those documents. I hope that means I do not need to take up too much of the Tribunal's time. I propose to deal with matters in the order in which my friend, Mr. Hornsby, has dealt with them - first, the Chapter II decision; then the Chapter I decision.

The preliminary point to make in relation to the Chapter II aspect of the case is that in fact IMS are not seeking any relevant relief in relation to Article 82, the Chapter II prohibition. They are simply seeking a general declaration that Red Bee are dominant in a period between 2004 and -- I am not sure whether it stops at 2007 or continues to the present day. In reliance on the authority he himself took the Tribunal to, that is not an appealable matter. In essence that would be a sufficient basis to dispose of this aspect of the case altogether.

Now, turning then to the substance of what Mr. Hornsby says ----

THE CHAIRMAN: Wait a minute, Mr. Anderson. There is a non-infringement decision here. Everybody accepts that. The infringement in question at the moment is: Was there an infringement of Article 82? To that, Ofcom answered, "No, there is not because there was not dominance, and therefore we are not going to look at the question of abuse because it does not arise because there was not dominance".

MR. ANDERSON: Yes.

THE CHAIRMAN: Now, that non-infringement decision has been appealed. As far as I can tell Mr. Hornsby's case is, well, we can look at that and see whether you got it right or wrong, and if we decide that you got it wrong, then we can either remit the matter back to you for

you to look at it again, or we can decide the matter ourselves. Do you thus far disagree with any of that?

MR. ANDERSON: I disagree with the very end bit, because if all he is seeking is a freestanding decision that Red Bee is dominant, then that is not a decision that is in substitution for the decision we took. We took a decision that they were not dominant in 2004. Now, if that is wrong, that can be set aside. But, what it cannot be replaced with is a freestanding decision that Red Bee are dominant.

THE CHAIRMAN: But what if our view were, "Well you asked yourselves the wrong question". It now seems that Mr. Hornsby is saying not that you should have found they were dominant in 2004, but that you wrongly restricted yourselves to that question and that actually what their complaint raised was something wider than that - namely, that at some point during the duration of this contract Red Bee became dominant and you ought to have looked at the whole duration of the contract to see whether at any point during that time the exclusivity or the potentially predatory pricing could have been an abuse because dominance arose at some point, and that you did not deal with that. Now, perhaps I will pause there -----

MR. ANDERSON: All I am saying is that however he puts it, what cannot happen is that it stops with a single declaration that Red Bee is dominant. You can say we got it wrong, and send it back to us. You can go on and take an infringement/non-infringement decision yourself. You cannot simply declare that Red Bee are dominant.

THE CHAIRMAN: But we could say, "Well, we think you got it wrong as at 2004 and there is enough in the papers for us to decide for ourselves that Red Bee was dominant". Then I suppose we would remit it to you to consider the question of abuse. Is that what you are saying?

MR. ANDERSON: That is all I am saying. It cannot simply end with a declaration of dominance.

As was clear from IMS' skeleton and, indeed, the submissions today, IMS' essential complaint is that Ofcom consider too short a time when assessing dominance and should have taken account of the rise in BBCB, or Red Bee's market share after winning the Channel 4 contract. He confirmed that he had no evidence about whether, looking at the period before that would have made any difference. In fact, our position is that there were no relevant changes in the preceding periods. In our submission the essential fallacy, or flaw, in that approach is that the abuse that we were looking at was the entering into the Channel 4 contract. That happened in 2004, either at the time at which the bid was put in, or

at the time that the contract was concluded. That was 2004. That was the relevant point in time at which to ascertain documents. It is an entirely separate question to consider over what sort of period of time should be have been looking at the evidence in order to determine whether in fact there was dominance. But, the relevant point of time in which to determine dominance was, in our submission, when the Channel 4 contract was awarded. Taking account of subsequent changes in market share we say would be entirely irrelevant. Now, the complaints identified in relation to the Channel 4 contract award are that the price bid was too low; that there was some form of cross-subsidy from the BBC license fee; that there was exclusivity. But, what we say in answer to those points is that clearly the price at which the contract was bid - whether or not a predatory bid was put in - occurred at the time at which the bid was submitted. Whether or not there was cross-subsidy from the BBC license fee -- Clearly whether or not there was, there cannot now be because the BBC no longer owns Red Bee. Then there is the question of the exclusivity.

We submit that none of those are a continuing abuse; that the relevant abuse in this case is the entering into, or the bidding for, the Channel 4 contract - because after that, after the contract had been awarded, the BBC had no choice as to what price it was paid by Channel 4; the exclusivity was part of the terms of the contract; there is no provision for varying or unilaterally altering those terms. That was therefore the contract that was entered into at the time and that, we say, is the relevant abuse.

The proposition that somehow those facts can change because the market share of Red Bee may have increased after that time, we say simply does not, as a matter of law, alter the situation. There is certainly no authority cited, and we are not aware of any authority, where a contract that was legitimately entered into at the time when a company was not dominant somehow becomes abusive simply because the company's market share increases. That is a proposition of law - a submission which we say can find no support in any of the authorities.

So, that is essentially why we say Ofcom was right to look at where the BBC was dominant in 2004. It is not, we would say, a fair allegation to submit that that was only looking at a snapshot of the BBC's position. What would have been possibly relevant was the question of market share prior to the first half of 2004, and there is simply no evidence that that would have made any difference.

It is quite clear from the submissions we have heard today that IMS are submitting that the relevant period should have been a period post 2004. They make a number of points - for example, they contend that one should not have included Intelfax in the market share

calculations. We say, "Well, quite clearly, since Intelfax did not leave the market until 2005, it was quite right to include their market share when looking at the position in 2004". For Ofcom to have ignored Intelfax's market share would have been to shut its eyes to what the market conditions actually were at the time when the BBC submitted its bid for the Channel 4 contract, and the BBC's small share of the contestable market at that time. What is quite interesting is that at that relevant time the market share of IMS was 60 to 70 percent of the contestable market - the BBC's was down at around 10 percent.

So, it is perhaps not surprising that IMS would rather focus on a period at some later point in time. In fact, at paras. 8 to 21 of its skeleton it seems to go so far as to argue that you should be looking at what Red Bee's market share is now. You see that from their quote from para. 21 - that,

> "RB, in its communication to investors in its communication to investors in November 2005 explains the market situation in an up-to-date manner".

So, we have no problem with the notion that in assessing whether an undertaking is dominant one should look at the position over a period of time. One can see that from *Hoffmann La Roche*, for example, which can be found in the authorities bundle at Tab 7. That makes the point that if one needs to consider whether market share has remained persistently high over a period of time. The same point emerges from the case that IMS has cited and, just for the record, the relevant cases are the *AKZO* case, which is at authorities' bundle tab 10, the relevant paragraph number is 59. There is the *Virgin/ BA* Commission decision of 1999 which can be found at bundle B of the authorities at tab 23, and the relevant paragraphs are 88 and 93. The OFT Guidelines and Assessment of Market Power, that is authorities' bundle B at 34, paras 211 to 212.

The other cases relied on were firstly *Michelin* which, in our submission, does not assist, because that was quite clearly an ongoing system of discounts and rebates, and if I can just invite you to open that briefly, it is at tab 8. If one turns to p.4 of 33 it gives an idea of how the Commission identified the abuse.

> "During the period between 1975 and 1980 [Michelin] infringed Article 86 of the Treaty establishing the European Economic Community by:
>
> (a) binding tyre dealers in the Netherlands to itself through the grant of selective discounts on an individual basis conditional upon sales 'targets' and discount percentages which were not clearly confirmed in writing and by applying to them dissimilar conditions in respect of equivalent transactions; and

(b) granting an extra annual bonus in 1977 on purchases of tyres for lorries, buses and the like and on purchases of car tyres, which was conditional upon the attainment of a 'target' in respect of car tyre purchases.

Then if one looks at the bottom of the next page: "The discount system", one can see that the abuse consisted of a series of actions and some of the key points over the page, p.6. You will see in the third paragraph down:

"… [the discount system] comprised of variable component consisting mainly of the annual bonus …"

The next paragraph:

"The level of the variable annual bonus component was established individually for each dealer in accordance with his efforts."

At the beginning of the next paragraph:

"On a number of occasions the advance bonus and the monthly bonus were paid on the basis of expected annual sales."

Two paragraphs further down:

"A comparison of the customer files shows that dealers purchasing very different quantities often received the same bonuses and vice versa."

So essentially the point is that it was a variety of practices that cannot really be compared with the conclusion of a single contract, such as we are dealing with in this case.

THE CHAIRMAN: Well except that these are all within the context of contracts, and presumably once Michelin enters into a contract with the dealer I suppose the dealer is then entitled to that, but there is not in this case – and I do not think I am aware of any case where there is – a discussion about saying: "This is an abuse in relation to those contracts if you are dominant at the time you actually signed up that dealer, but not if you were not". The same clauses are not abusive if you were not dominant at the time you signed up; it is just not dealt with.

MR. ANDERSON: No, well two points. Yes, Michelin was dominant throughout – point 1, point 2: one of the aspects of the abusive conduct was the discriminatory and arbitrary nature in which the discounts and rebates were paid. It was not a case where Michelin had entered into a clear contract – whether it is with one or several suppliers – which sets the terms, and either side could then know what was going be paid by the one to the other. It was a series of rather arbitrary, discriminatory, discounts, and rebates. So it was a continuing practice, rather than a single contract that had been entered into; that was the only point I am making.

Sky, of course – it does not really assist – the relevant point there is the period that was being investigated for determining Sky's dominance was the period leading up to the abuse, not the period following the abuse.

Similarly, we would say that the *Tetra 1* case (tab 21) does not really assist. What happened in that case was the relevant abuse was the first act that Tetra engaged in. As a dominant undertaking it purchased effectively a company with the benefit of an exclusive contract. It is quite clear from para.65 I think it is, that the relevant abuse was the acquisition at the outset by the dominant undertaking of that exclusive licence. That is a very different position to the position that we have today. It is simply not open to Red Bee to turn to Channel 4 and say: "Now that we are dominant we have to put the prices up and you have to put some of the business out to third parties". It is simply not feasible, and it is not permissible, and that is why we say this is a very different case to the *Tetra* case.

In the *Coca-Cola* case, which is tab 16 in the bundle, and in particular paras. 81 and 82:

> "[81] Secondly, a finding of a dominant position buy the Commission, even if likely in practice to influence and future commercial strategy of the undertaking is concerned, does not have binding legal effects as referred to in the IBM judgment. Such a finding is the outcome of an analysis of the structure of the market and of competition prevailing at the time the Commission adopts each decision. The conduct which the undertaking held to be in a dominant position subsequently comes to adopt in order to prevent a possible infringement of Article 86 of the Treaty is thus shaped by the parameters which reflect the conditions of competition …"
>
> [82] Moreover, in the course of any decision applying Article 86 of the Treaty, the Commission must define the relevant market again and make a fresh analysis of the conditions of competition which will not necessarily be based on the same consideration as those underlying the previous finding of a dominant position."

What we say that shows is that a dominant finding in relation to one period of time cannot conclude that an undertaking is or was dominant, let alone abusing its dominance at another period of time.

In the skeleton Mr. Hornsby refers to various merger decisions, but in our submission those cannot assist. You are clearly looking, in a merger decision case, at the likely future effects of an action or a state of affairs in contrast to considering whether there has been in the past an abuse.

Turning now to the Chapter I non-infringement decision ----

THE CHAIRMAN: Wait a minute, Mr. Anderson.

MR. BLAIR: I think what you are saying is that the right moment you were looking at was 2004?

MR. ANDERSON: Yes.

MR. BLAIR: But the case against you may be – it has not been very clearly expressed – that what you ought to have done on the facts before you was to have seen whether relying on the contract in 2006 or 2007 was itself an abuse of Article 86.

MR. ANDERSON: To which our answer is: there is no authority for the proposition that a contract legitimately entered into becomes abusive, without any other change, simply because somebody becomes dominant. The contract has been concluded, the parties have rights under it and we say it is not, as a matter of law, legitimate to contend that simply that contract unaltered can become an abuse. That would be going considerably further than any authority.

THE CHAIRMAN: Even though it does seem clear, which you are no doubt coming to, that under Article 81 exactly that can happen?

MR. ANDERSON: Not by reason of acquiring a dominant position.

THE CHAIRMAN: No, but by reason of an increase in market share.

MR. ANDERSON: Yes, it can have, but that is a consequence of the guidelines and the nature of the two animals; they are different, and we did conduct a proper and full, we say, analysis under Article 81, which has not really been effectively challenged in submissions today. There are no conceptual reasons why those positions are inconsistent.

THE CHAIRMAN: Well they are in the sense that you put forward the argument: well, it cannot be right that the agreement, which was not an abuse at the time, becomes abusive because you cannot expect Red Bee to go back to Channel 4 and say "Sorry, we can't have an exclusive agreement with you because of our increase in market share, therefore you must put this out to other people". But could Article 81 not operate in such a way that they have to do exactly that, they would say that we would have to go back to Channel 4 and say "We were in the block exemption beforehand, but now our market share is over 30 per cent and we have assessed whether 81(1) and 81(3) apply to us and decided that they do, and decided that this exclusivity now is unlawful and you must go out to the market."

MR. ANDERSON: I come back to the point that we say the relevant abuse – the relevant infringement – was the entering into the contract. When one is then looking, over a period of time as to whether or not an existing agreement benefits from the block exemption, and if at some point it no longer benefits from the block exemption does it infringe Article 81, one has to look at the conditions in the market over time. That is the essential difference.

THE CHAIRMAN: Yes, I am sorry, Mr. Anderson, I took you out of your order.

MR. ANDERSON: Not at all. I want to move on now to the Chapter I non-infringement decision. In setting out its case IMS identify two main issues between itself and Ofcom. The first is whether the Channel 4 contract is in reality an eight year contract rather than a five year contract because of the option to extend, and the second one is whether Chapter I is infringed from 1st January 2007 by virtue simply of the fact that from then it at least falls outside the vertical block exemption.

The second issue, at least so far as the skeleton is concerned, seems to be little more than a number of narrow criticisms of Ofcom's reasoning, not many of which were developed today. But we say that IMS has not made out any convincing case for finding that Ofcom's conclusion in the decision was wrong, and that the Channel 4 contract prevents, restricts or distorts competition.

I will address each of those in turn but before I do so it is worth reminding ourselves of what IMS's complaint was on Chapter I. The broad position is that the Channel 4 contract being of potentially eight years' duration effectively foreclosed the market, or in other words that the Channel 4 contract contributed to a market situation where it was difficult for a newcomer to enter the market, or for an existing operator to increase its market share.

In seeking to justify that what IMS is essentially saying is that since the Channel 4 contract is exclusive in the sense that Red Bee is contracted to provide all the services during the duration of the contract, they effectively excluded other potential suppliers from supplying to Channel 4 - in other words, that the contract effectively should have been re-tendered in January 2007 when it no longer had the benefit of the block exemption.

We say that is not a sufficient basis for impugning Ofcom's decision. Of course we acknowledge that a feature of the market for access services is that major UK broadcasters choose to meet their requirements for such services by awarding contracts for periods of five years or more. That is a feature of the market that is driven by the requirements of the broadcasters - such as Channel 4 - who choose to invite tenders to provide them with access services at a pre-determined price over a period of years. Of course, not all those contracts are held by Red Bee. For example, IMS holds the Sky contract. While one can argue whether, as a technical matter, particular contracts are exclusive or non-exclusive the facts are that each of the major UK broadcasters chooses to engage particular access services for all their service needs, or at least all their needs of a particular category, or a particular channel for a number of years at a time. It is entirely understandable why they do that. They need to acquit themselves with security of supply of access services so that they can

be sure of meeting their regulatory obligations because these access services are regulatory obligations. Also, they want, by tendering out a contract for a number of years, to attract the interests of a reasonable number of credible bidders who may need to make some form of up-front investment.

None of this necessarily means that the market is foreclosed in the sense that by reason of the Channel 4 contract it is difficult for competitors to enter or expand. Indeed, contracts for a number of years' duration are sometimes a good thing as far as competition is concerned because suppliers of access services will almost certainly need to make some form of up-front investment in order to be in a position to meet, for example, Channel 4 needs.

If the contractor re-tendered every year that would clearly favour the incumbent provider who would have already made those investments and would therefore be better placed to submit a competitive priced bid. So, our contract of a number of years' duration clearly makes it easier for others to bid against the incumbent over price since the initial investments could be spread over a number of years.

Further, as we have explained in the decision - and this is at paras. 7.44 to 7.72 - this is a market in which we found that it was the broadcasters who called the shots. Those buyers are well-informed, experienced purchasers of access services, and they determine the terms and durations of the contracts into which they entered.

Broadcasters have been able to drive keen prices in a market where prices have fallen, and are expected by broadcasters to fall further. We also say that this is a market which exhibited some of the characteristics of a bidding market. That is dealt with in the decision at paras. 7.17 to 7.26 and in Annexe 4. When I say 'with the characteristics of a bidding market', relatively few large contracts, open contests with an opportunity for all to participate and no significant capacity constraints. Not all the characteristics of a bidding market ... reputation we did find to be important in this market. It is also a market in which shares can change rapidly as a result of a contract being won or lost over time. That is one of the reasons why simply concentrating on market share when assessing dominance is inappropriate.

At least three of the existing suppliers were regarded as credible bidders, and with the major broadcasters able to sponsor new entry if their needs were not being met. It is also a market that is closely related to other markets - for example, the provision of sub-titles for TV advertisements; DVDs or foreign language movies. Those are activities which IMS itself is

engaged in, and one can see that from the extracts from their website in Tab 18 of the core bundle. We say that is relevant because it clearly makes entry easier.

THE CHAIRMAN: So, there is a degree of supply substitutability there, although it might not be part of the same relevant market. It operates as a constraint on the exercise of market power.

MR. ANDERSON: Yes. All these are points that are made in our decision where we took the view that the important thing to do was to undertake an investigation of the actual effects of the agreement in the context of the market, having regard to the various issues and points made in the vertical restraints guidelines of the Commission.

THE CHAIRMAN: Do you say then that if it were right to look at the position in 2006 or 2007, that these points are sufficient to rebut any presumption of dominance that might arise simply from the existence of a 50 percent market share at any particular point?

MR. ANDERSON: No, that is not the way we put the case. The way we put the case in the decision, and in the defence and the skeleton is that when we were looking at it under Article 81, prior to January 2007 they benefited from the relevant block exemption because their market share was below the threshold. One knows from the vertical block exemption itself that one excludes in-house supply when calculating the relevant market share. That is expressly set out in that block exemption. That is why we did that.

THE CHAIRMAN: In the block exemption or in the guidelines?

MR. ANDERSON: Sorry. It is in para. 98 of the guidelines. I am sorry. But, for the purposes of applying the vertical block exemption. So, that is why we did that. We therefore reached the view that this five year agreement by a company that was below the relevant market share threshold benefited from the block exemption. Now, there came a point, of course, where the in-house supply became out-house supply. Therefore the benefit of the block exemption was lost. But, it did not follow from that that it was necessarily the case that this contract, because it no longer benefited from the block exemption, necessarily infringed Article 81. So, what we then did was an investigation of the effects of this contract in the relevant context in the market. That involved looking at various features and aspects identified in the vertical restraint guidelines.

THE CHAIRMAN: The increase in market share though which caused the block exemption no longer to apply occurred as soon as the in-house supply became external ----

MR. ANDERSON: That came after winning the Channel 4 contract. That came on the BBC selling its own in-house supplier to Red Bee.

THE CHAIRMAN: Right. But then they benefited from the transitional period of another year.

MR. ANDERSON: Yes, and that is why there was only the run for the contract left, which was what we then looked at. We could not assume, simply because they had lost the benefit of the block exemption, that it necessarily infringed Article 81. So, we then embarked on a pretty full investigation of the actual effects of this contract in the context of the market.

THE CHAIRMAN: But, had there been any other relevant changes in market share data other than that move of the in-house supply to being the external supply once you came to have a look at it post-January 2007?

MR. ANDERSON: There had not, but the point was that the features that I have been identifying - the bidding market, and all those sorts of things - were relevant features in considering that the mere fact that there had been an increase in market share was not enough to assume there had been a foreclosing effect, or that this contract continued to have a foreclosing effect. That is why I am going quickly through this list of the very features of the market we investigated, and why we concluded that the agreement did not appreciably foreclose competition in the market.

Now, what we say is that IMS has not begun to undermine – they have not even addressed these features of the market. They have not begun to undermine the analysis undertaken by Ofcom in its decision. They have confined themselves to two points - one is that the contract is really eight years; the other is that once the block exemption no longer applied, it necessarily followed that Article 81 was infringed. That is where we say they fail totally in this appeal.

THE CHAIRMAN: I do not think they say that. I think they say that once the block exemption does not apply because of the increase in market share, that increase in market share is so high that it creates a presumption of market power (to put it in a neutral sense) which then requires to be rebutted. What I was asking you before was whether approaching it now - because that is the point that is put to you - do you say that these features that you have listed rebut any such presumption?

MR. ANDERSON: We would not accept there is necessarily a presumption because of the characteristics of the market. One has got to recall that essentially changes in market share happen very significantly because of single contracts. This single Channel 4 contract is what makes all the difference. That contract, we know, is no longer of concern to you. It was won. It is there. It is not going to be contested until it expires. It was simply artificial to say that because the market share is now - whatever it is - 50 percent, it necessarily follows that you have any more market share, or market power, in relation to bidding for other contracts than you had beforehand. So, simple reliance on increase in market share is mis-placed.

One needs to look at all these other features. We looked at all these other features and concluded that there was not a material foreclosing effect.

MR. BLAIR: Can I just pick that up? I just want to clarify what I understood IMS were saying this morning. They were referring to para. 135 of the guidelines on vertical restraints. Basically they were arguing that once the block exemption is lifted, then any vertical agreement such as this has to be justified under Article 81(3). Article 81(3) is in terms of efficiency, innovation -- You can probably quote it much better than I can. I think the point made is that none of those aspects are addressed in the decision. The decision addresses issues of competition, but not issues of efficiency or innovation, or other things. That is the area where Ofcom should have addressed, if it was going to pass this agreement through Article 81(3).

MR. ANDERSON: Two points. (1) We did not rely on para. 135 of the guidelines, which does apply to exemptions effectively. What we relied on was the next section in the vertical restraint guidelines - para. 137 onwards - which is a section addressed to whether or not, in a position where the block exemption does not apply, you necessarily infringe Article 81. So, what we concentrated on was whether or not Article 81 was infringed. We went through all the factors in paras. 137 through to 160 and concluded that in this particular case, given the characteristics of this market, given the strength of buyers' power, the fact that it is the buyers who determine the terms and so on, there are single large contracts and market share changes rapidly over time, the contract did not infringe Article 81; we never got on to considering Article 81(3).

PROFESSOR STONEMAN: But that implies that 135 and 137 are alternatives; it is not both, it is either/or is it?

MR. ANDERSON: Well it is a different section of the guidelines, yes. We did not rely on attempting to justify the contract under Article 81(3), we considered whether or not it infringed Article 81(1) in the first place.

THE CHAIRMAN: You nailed your colours to that mast in the sense that you did not then go on to say "And even if we are wrong on that, then looking at 81(3) we think there is a justification". The decision was that it did not fall within 81(1).

MR. ANDERSON: Yes, that was the decision. So some of the other characteristics, just to complete the picture, the next issue is when will the Channel 4 contract next be contestable? We submit that the appropriate date is towards the end of 2009 and not three years' later as IMS submit.

THE CHAIRMAN: Can you just remind us what was said in the decision about this fee?

MR. ANDERSON: Yes, it is dealt with at in section 8.22 to 8.24, and then of course it is also explained in a rather horrendously long footnote somewhere in our skeleton, which you will find tucked away in the middle of it the answer to your question about contract price renewal.

THE CHAIRMAN: So what paragraph was it in the decision, sorry?

MR. ANDERSON: 8.22, 8.21. I am told it might, just for completeness, be best to start at 8.18.

THE CHAIRMAN: (Pause for reading) Right.

MR. ANDERSON: I am sure I can give you the reference where it is dealt with in our defence and skeleton as well.

THE CHAIRMAN: Yes.

MR. ANDERSON: IMS submit that Ofcom's analysis was flawed because the contract was in fact of eight years' duration, and essentially the argument is that because it might not be terminated until 2012 – not that it will not be, but it might not be. The reasons I will now go on to outline. We say that argument is incorrect. We say that the relevant question to ask in considering whether a contract forecloses the market is not how long the contract might last, but how long it will last until the buyer can terminate the contract, if he can get a better deal from somebody else – that is the critical point.

When one goes on to consider: does the cost, reimbursement fee affect that, the relevant point is in 2009 not 2012 is the point at which competitors will be able to come along and say, or Channel 4 will be able to go to the market and say: "Let us see if we can get a better deal from you", so that is why we considered it was relevant to consider that first question and not "it might go on to 2012 and therefore that is the relevant time to consider."

We accept that it is possible that the contract might remain operative for eight years, but we say it is equally, we would expect, common ground that subject only to the payment of the CRF that Channel 4 is not obliged to take up the option of extending the operative life of the contract. So the issue between Ofcom and IMS is which date is relevant for the purposes of analysing of whether the Channel 4 contract forecloses the market.

This was a question expressly considered by Mr. Justice Park in the *Crehan* case, which one can find in the authorities' bundle – the first one – at tab 20. He was considering the point in the context of investigating the second limb of *Delimitis* in the context of the Finnish *Neste* Petrol Station case which you were taken to this morning. You will remember in that case the ECJ was taking the view that contracts that could be terminated on short term – a year – did not have a foreclosing effect, even in the context of a market where there were other contracts that did. It was at tab 20, and I am sure, at least Madam Chairman will be

familiar with the *Crehan* case, it is all about pub ties. The relevant paragraph is 179, p.44 of 74.

> "Before leaving loan ties I should mention the ECJ decision in *Neste Markkinointi*. The decision was given after the Commission's decision in Whitbread. The case concerned a contract for the supply of petrol to a filling station n Finland. The filing station was tied to purchase all of its supplies from t he supplier, but the contract was terminable on 12 months' notice. The ECJ held that, because of the relatively short notice period, the contract did not make a significant contribution to any sealing-off or foreclosing effect so far as the market for supplying petrol to retail outlets was concerned. The case was concerned directly with the Delimitis condition 2, whereas at this point in my judgment I am considering condition 1. Nevertheless it seems to me that the Commission's view in Whitbread that loan ties which were terminable at three months' notice could have foreclosing effects cannot stand with the *Neste* decision. I note for example that in para. [32] of the decision the ECJ says: '… duration is the decisive factor in the market-sealing effect'."

And it is the next sentence that is the material one:

> "It is clear that what the court means by 'duration' is the period during which the agreement cannot be terminated, not the period for which it is in practice likely to last without termination."

MR. BLAIR: Pausing there, is it the f act that that bit of Mr. Justice Park's decision was not disturbed in the subsequent proceedings above?

MR. ANDERSON: It was not.

MR. BLAIR: Thank you.

MR. ANDERSON: Indeed, in any event, the House of Lords reinstated Mr. Justice Park's decision. So the significant point there is the date at which this agreement cannot be terminated is the initial period to 2009. The fact that it has an option to extend is not relevant for current purposes.

THE CHAIRMAN: Though it is strange there that they do not refer to the distinction that we saw the Advocate General drew between beer and ice cream on the one hand, and petrol on the other hand, as indicating that in a beer supply agreement, because there is more brand loyalty people are presumably less likely to exercise the option to make a change, than they are in relation to a product where the main driver of competition is price.

MR. ANDERSON: Yes, save that the point he is making is when one is considering duration, how do you measure it? Do you measure it by how long the contract might last? Or do you just look at the period that it is bound to last, and the answer is the latter, therefore the relevant period in this case is 2009 and not 2012.

PROFESSOR STONEMAN: But can we actually decide the period in which it is bound to last without knowing the size of the penalty? I mean if the penalty is huge it is bound to continue, if the penalty is minimal then it may continue. I went back to this long footnote, which I do not think actually answers any of the Chairman's questions at all ----

MR. ANDERSON: I think it is the bit in parenthesis in the very middle.

PROFESSOR STONEMAN: Is this that the whole of the contract has to continue, and it has to continue at current prices; what bit are you saying is in that footnote?

MR. ANDERSON: It was the answer to the first of those two questions. I am a bit reluctant to get into the detail of it because this is a very sensitive area and it may be more appropriate for Mr. Green to address the detail of that question. But as I understand the section in the middle of the footnote the actual fees payable remain, subject to an inflation factor upwards.

PROFESSOR STONEMAN: Well is Mr. Green going to answer these questions?

MR. GREEN: I am just making some inquiries to see whether we can provide you with the contract because it seems to me that would be the easiest solution, but it does have some confidential data in it, we would need to redact, for example, some rates and financials out of it, but then you would be able to see the full extent of clause 4. It is, in fact, the same price, which is increased by reference to a compounded RPI, but I think it is better that you see the relevant terms. We need to just clear that with C4 though.

THE CHAIRMAN: Right, continue with your point and then we will see.

MR. ANDERSON: Subject to that point, clearly one could hypothesise that if the CRF was worth 50 per cent of the contract price, which was already very low then that would have so significant an impact that it would be unrealistic to say the contract is bound to end in 2009. But we explored that issue, we dealt with it in the decision, we see that it was worth 3 per cent of a contract which Red Bee would not on renewal be entitled to reduce, and we concluded that that was not a material impediment to Channel 4 seriously being able to put the matter out to tender in 2009. That is the conclusion we reached, and we say that was a legitimate and reasonable conclusion properly researched and properly considered.

I accept that footnote 12 is a little impenetrable, and if we can provide any clarification; it may be that provision of the contract answers the problems, but as may be apparent from footnote 12 the contract itself might be equally impenetrable. One of the points was it was

not an exact science; there are a number of variables, such as what Channel 4's requirement will be at the time, and so on. What we calculated was that the value of the CRF relative to those contract prices was just 3 percent. Therefore we conclude that that was not a material impediment similar to the point made in the vertical restraint guidelines about the loan. One has to consider whether the effect of a loan, and repaying the loan, acts as a real impediment to terminating a tie, or not. That is the conclusion we came to.

It is, of course, material that this is a market in which broadcasters expect to see prices coming down - broadcasters and access service providers. On that point, if I can invite you to look at the decision at para. 7.59 -- One of the difficulties with the evidence on this particular point is confidentiality. Interviews were conducted by IAMCO with a number of participants in the market. We reached the view that the consensus was that prices were coming down.

> -- broadcasters generally consider the prices of a downward trend. For example, Sky stated: '[we] think that with technology development prices will drop. Providers can now cover with fewer people, which means lower prices'. ITV stated: 'we expect a price decrease over the next few years".

Of course, the technology continues to develop. For example, annexed to IMS' skeleton at Tab 14 are pp.5 and 11 -- You need to be able to turn it on its side in order to see the page numbers. For example, the move from the old linear system of broadcasting to the new tape-less and presumably digital will result in if it is expecting falling prices. One sees on p.11, in the little box, the pioneering use of speech recognition technology and assisted sub-titling to drive greater efficiencies.

The IMS report is in the core bundle at Tab 21.

THE CHAIRMAN: We were looking at the annexe to the IMS skeleton at Tab 14 of Bundle 6.

MR. ANDERSON: The core bundle, yes.

THE CHAIRMAN: You took us to pp.5 and 11.

MR. ANDERSON: Yes. Now, I am asking you to move on to Tab 21 of the same bundle. This is an IMS financial statement. The third paragraph under 'Market & Business Development'.

> "Additionally, unit production costs in IMS' key business areas have also been reduced as a result of this cost review and additionally as a result of the introduction of speech recognition technology for live sub-titling. IMS is proud to note that it is the first major sub-titling company in the world to produce its entire live sub-titling output using this technology and the board envisages that its application in international markets could bear fruit in the future".

We believe it was legitimate for us to conclude that there was every reason to think that Channel 4 will, towards the end of 2009, review its access service requirements to see if it can get a better deal. That does not of course necessarily mean that one of Red Bee's competitors will win that business, but the important point is that it means that that is the point at which it will become testable.

So, taking everything in the round, Ofcom saw no reason to consider that Channel 4's access service requirements were likely to be un-contestable until 2012.

In our submission it would be wrong for the Tribunal to conclude that IMS' analysis that the Channel 4 contract should simply be regarded as an eight year deal is correct.

I said I would give you the references to where else we dealt with the CRF before you. That is in the defence at paras. 54 to 56, and in our skeleton at paras. 19 to 22.

Turning now to the second ground on which IMS challenge ----

MR. BLAIR: Just before you leave it, the last question on the CRF -- Is it standard in the industry to have the CRF in the contract, or is there something special about the Red Bee contract that differentiates it from all others?

MR. ANDERSON: I do not know the answer to that. We can perhaps find that out and let you know, but I do not know the answer.

MR. BLAIR: It would be useful.

MR. ANDERSON: We will investigate it and let you know in writing.

MR. GREEN: We will deal with that in due course.

MR. ANDERSON: Thank you. The second ground was whether the Chapter I is infringed from 1st January, 2007, simply by virtue of the agreement falling outside of the vertical block exemption. The first point to make in our submission is that IMS have simply not put forward any credible case as to why our analysis of the actual effects of the agreement once it no longer had the benefit of the block exemption are erroneous or wrong, but based on a full analysis of all the relevant characteristics of the market and the reasons are fully set out in s.8, and cross-referring back to relevant aspects of s.7, which was the section dealing with market characteristics.

In the skeleton this is dealt with by IMS at paras. 30 to 37. They advance a number of specific criticisms. The first is that Ofcom did not fail to take account of the relative size of competing suppliers. What we say is that it is quite clear from reading the decision that Ofcom had well in mind the market positions of the various participants in the market and the long-term contracts which each of them had with the major broadcasters. Of course, it is true a lot of those details are confidential. So, we have not set them out at great length. But,

IMS is fully aware of the nature of the inquiries we undertook through the s.26 notices, and therefore were well aware of the position of the other suppliers in the market.

It is, of course, relevant also, as noted in para. 8.16, that Red Bee was one of three relevant access service providers - the other two being ITFC and IMS - who all had the reputations to be able credibly to compete for the large contracts. That being so, the relative size of those suppliers - and their market shares also depend upon which contracts they happen to win - is not very material to an assessment. If they can compete for the jobs, they can compete for the jobs. That is what is relevant in terms of the competition.

Secondly, IMS in fact criticise Ofcom for having regard - and this is in their skeleton at para. 31 - to the various factors set out in paras. 137 to 160 of the BRG. As I say, that seems to be based on the fact that we should have been looking at the matter under Article 81(3). The suggestion seems to be, if one did not have the benefit of a block exemption you necessarily could not then find that the agreement did not infringe Article 81(1). We say that that is just based on a misunderstanding of the relationship between the vertical block exemption and the vertical restraint guidelines. If you no longer have the benefit of the block exemption, you necessarily have to then go on and consider what the effect of the agreement not having the benefit of that block exemption is, and that is precisely what paras. 137 onwards of the vertical restraint guidelines provide guidance on what to look for.

THE CHAIRMAN: Mr. Hornsby?

MR. HORNSBY: As Mr. Anderson keeps on coming back to this point, could I remind the Tribunal that para. 137 is actually in a section devoted to Article 81(3). That is demonstrated by looking at the table of contents that I drew your attention to this morning.

THE CHAIRMAN: You drew our attention to that, and I noted that actually the table of contents did not seem to coincide completely with what is actually -----

MR. HORNSBY: Not entirely. There is one ----

THE CHAIRMAN: It seemed to me that whether or not it is the case - which it seems to me it is not that - that it automatically falls within Article 81(1) if it exceeds the market share threshold, nonetheless the point that I thought that IMS were making is, “Look! Then you are looking at an agreement with a party that has a market share in excess of 30 percent, with an exclusivity that is going to last at least for three years, in a contract that relates to 10 percent of the market, and there was no sufficient reasoning as to why a contract which has those features should not fall within Article 81(1)”. I think that was what was being put to you.

MR. HORNSBY: Yes. That was what was being put. If I can go back to it, I would say that we are not saying that because it is outside the block exemption it is automatically within Article 81(1). We do not say that at all. We say that you need to show some efficiency justification, and para. 135 is relevant to that. S.137, and particularly s.141, make it really quite clear that when a strong market position exists, the duration of a contract, where it is more than on year, gives rise to serious questions and those questions have to be addressed under Article 81(3) and not under Article 81(1). On any view, this contract is more than one year duration. That is our point.

THE CHAIRMAN: That is the point that is put against you, Mr. Anderson.

MR. ANDERSON: We say that is a misunderstanding of, firstly, the vertical restraints guidelines. I think my friend is only able to say what he says because something has gone wrong with the paragraph numbering and the table of contents. But, the first section - Enforcement Policy in Individual Cases - the framework of analysis clearly ends at para. 142 with relevant factors for the assessment under Article 81(3). Then, the section beginning, "Analysis of specific vertical restraints" is factors relevant to considering whether or not there is an infringement of Article 81(1). That is how the scheme of the guidelines operate. They are dealing both with Article 81(1) and 81(3), and in our submission, if you no longer have the benefit of the block exemption, the starting point is to consider whether or not there is an infringement of Article 81(1), and it is only if you conclude that there is an infringement that you need to go on and consider Article 81(3). We undertook an investigation under Article 81(1) and for the reasons I have been explaining - and I set out fully in our decision - we took the view that in the circumstances of this case, and given the characteristics of the market, and given the three year period, given the fact that market shares vary as a result of success in winning individual contracts, one could not conclude that this Channel 4 contract had the foreclosing effect that IMS was contending. We say that was a perfectly legitimate and correct approach, and the Tribunal has not been provided with any credible case as to where we went wrong in that analysis. Just to reiterate the reiterate the relevant characteristics, major broadcasters are large, well-informed undertakings who are experienced and knowledgeable purchasers. The major broadcasters are choosing to meet their access service requirements by periodic tendering, and they determine the terms and durations. Broadcasters had a choice of access services. The need for an established reputation was the only significant barrier entry. Entry costs were relatively low (see Annexe 2). Essentially for those reasons we submit that we got it right.

One final point - a point made by IMS at para. 36 of their skeleton, that Ofcom failed to have proper regard to the points in paras. 141 and 145 of the vertical restraint guidelines -- It may be worth taking you to those now. (After a pause): What IMS say in their skeleton at para. 36 is,

> "As to the proper analysis of the Channel 4 contract, IMS refers the Tribunal to paras. 141 and 145 of the vertical restraint guidelines which make it clear that non-dominant companies whose market shares exceed 30%t need to justify non-compete agreements of more than one year. This justification must take place in the context of Article 81(3)".

We considered Points 141 and 145. You will see those on p.29. It is the second part of 141.

> "Non-compete obligations between one and five years entered into by non-dominant companies 'usually require a proper balancing of pro and anti-competitive effects'.

So, it is not a question of justification. It is a question of balancing. Then, of course, Point 145:

> " …'Countervailing power' is relevant, as powerful buyers will not easily allow themselves to be cut off from the supply of competing goods or services. Foreclosure, which is not based on efficiency and which has harmful effects on ultimate consumers is therefore mainly a risk in the case of dispersed buyers. However, where non-compete agreements are concluded with major buyers this may have a strong foreclosure effect".

So, we were right to have a look at countervailing power amongst the many other features that the guidelines suggest we should have investigated.

In conclusion, in our submission, IMS has failed to establish that their appeal on either the Article 82 or Article 81 features of the case.

Madam, unless I can assist the Tribunal further, those are our submissions.

THE CHAIRMAN: Thank you very much, Mr. Anderson.

MR. GREEN: Madam, I would like to start just by identifying what is, or what should be, the proper scope of IMS' appeal. It is trite that an appeal is governed by the notice of appeal -- the notice of application - Schedule 8(3). What we have heard today is an attempt by IMS to formulate a case - not necessarily the case that is in the notice of appeal. The notice of appeal identifies a number of issues and it also identifies things which are not in issue, but which, as per the submissions made to the Tribunal today now appear to be coming into

issue. So, it is very important to start by identifying what is the proper scope of the appeal, and, accordingly, the jurisdiction of the Tribunal.

I would like to start with IMS' notice of appeal, and to identify some issues which I think will be helpful in clarifying what is, or should be, the scope of the dispute.

The notice of appeal which is in the main bundle at Tab 2 deals with the dominance issue and the five or eight year issue in a total of five pages and nineteen paragraphs (or there, or thereabouts). If you turn to p.18 of the internal numbering of the amended notice, s.6, we find a mere two and a half pages on whether the C4 contract infringes the prohibitions. In relation to Article 81(3) there are two paragraphs, and then in relation to dominance there are, again, two and a half pages - eleven paragraphs. It is trite that IMS cannot trespass outside the confines of its notice of appeal. I would like to just pick up a number of points that are in the notice of appeal and not in the notice of appeal because I think it is important to try and work out what IMS' real objection is.

In that regard I think it is important to work out what IMS says the counter-factual is - in other words, if you were to grant relief, what they say the perfect market, shorn of any anti-competitive conduct would look like. In that regard IMS is quite unequivocal that a number of features can thrive in an untainted market. They accept that a dominant undertaking can enter an exclusive arrangement pursuant to a tender, and that the period of time can be set by the broadcaster. They have no objection whatsoever to any of those things. It is important to understand that because it helps us identify that the real objection is to the means by which the contracts were entered - namely, the pricing at the point in time of acquiring the contract.

I would you to have a look at para. 7.2 of the notice of appeal. At p.21 of the internal number IMS says as follows as to relief,

> "It follows the Tribunal should order the C4 contract to be brought to an end. The impermissible exclusivity goes to the heart of the contract and is not severable under English law. This will mean that the contract should be re-tendered. Provided that this re-tender takes place at the same time as the SLA and providing that RB is correctly held to be dominant in the relevant market for the reasons given below in s.8, it should not be possible for the cross-subsidy enjoyed by RB to be continued if it is to be re-appointed. As a result, the rest of the market will not be at RB's mercy, even if it retains the SLA and the C4 business on an exclusive basis".

So, there is no objection *per se*, even if RB were *ex hypothesi* dominant, to it retaining any of these contracts on an exclusive basis. As to the duration, on the last sentence IMS says as follows,

> "The duration of the contracts can be determined by the broadcasters since the relief will actually create a bidding market which will generate efficiencies where none currently exist".

They make a similar point in para. 1.7 in the summary section of the notice, on p.2 of the internal numbering:

> "For details of IMS' objections to the SLA and the C4 contracts' exclusivity, duration, and pricing the Tribunal is referred to the Complaint. In case there should be any doubt, IMS's case is not the opportunistic action of a competitor invoking competition law for commercial advantage. If the Tribunal grants IMS the relief it is seeking, there is no guarantee whatsoever that RB will not retain all of BBC's and C4's business. IMS may therefore gain no business at all. However, should RB retain the contracts, IMS hopes that it will not be on the current basis whereby the high revenues it obtains from the SLA could enable it to leverage a relevant market share that Ofcom acknowledges to be between 60 and 70 percent in the CCD as opposed to 60% & 80% in the CCD. Already, since the draft CCD was communicated to RB, it has gained a significant contract from ITFC with a low bid. Unless the Tribunal grants the relief IMS is seeking, RB, using its high revenues from the SLA, could easily eliminate all competition in a market which, - as Ofcom's detailed investigation demonstrates - has proved to be extremely difficult to enter. Such an outcome would be highly desirable as it is estimated that the relevant market will double in value in the next few years".

So, the text in the middle makes it clear that IMS does not believe it is acting opportunistically because it accepts RB could retain the contracts even if dominant, even if it had market shares of 60, 70, and 80 percent on an exclusive basis and its objection here is said to be some form of unsubstantiated cross-subsidisation from the BBC contract into the C4 contract. That is important because it highlights the point that the nub of IMS' objection is one of pricing at the point of entry into the contract. There is no allegation anywhere in the notice of appeal to suggest that if Red Bee is not dominant at the point of entering into the contract and it were subsequently to become the contract, that is in any way dominant -- it was in any way wrong, or abusive, or Ofcom's decision is to be subject to criticism in that regard. One finds that in s.8 of the notice of appeal, p.22 of the internal numbering.

IMS again was clear in this part of the document that the only point in time at which it is alleging dominance is the point in time of the entering of the contract. The alleged infringement in this is the pricing. Mr. Hornsby accepted this morning in response to the Tribunal's question ----

THE CHAIRMAN: Where are you reading from?

MR. GREEN: I am just about to start at 8.3.

> "For the reasons set out in its original complaint, IMS is convinced the C4 contract is, and continues to be, beneath average cost and is discriminatory".

Again, that highlights that the bid which was put in pursuant to the invitation to tender was alleged to be predatory and/or discriminatory, which focuses attention upon the point at which the bid was made. That is the alleged infringement.

In 8.6 the allegation is made in the following terms:

> "At the time of the alleged infringement, in IMS' view, BBCB's relevant market share (including in-house supply) was over 50 percent, thus exceeding the 40 percent threshold. What is more, the in-house element was not contestable. This gave BCCB the power to act independently of its competitors, which is the hallmark of dominance".

That is at the time of the alleged infringement, which is the time of entering into the contract with the allegedly predatory and discriminatory pricing and in para.8.8 IMS says:

> "It follows to the extent that it is material at the precise moment when BBCB won the C4 contract it enjoyed a dominant position in the relevant market and in IMS's view both the pricing of the contract and its eight year duration infringed Article 82 and Chapter II on Ofcom's own analysis properly corrected, unless they could be objectively justified."

There was nothing in s.8 which says that if there was no dominance at the time of the entering into of the contract that somehow dominance acquired through the evolution of market share subsequently gives rise to a separate criticism which is before the Tribunal. Now, we have not prepared on that basis – although there is a clear answer to the point which I will come to later – and nor has Ofcom.

In relation to the allegation which is, at least one understands, the core of this case, it is extremely difficult to know what the objection is and can I just take you through a number of paragraphs in which the core objection is actually formulated. If I could go back to 1.7, towards the bottom of that paragraph one sees the allegation, and this is the conduct which IMS is inviting the Tribunal to stamp on in a new tender process, which is "… using its high

revenues from the SLA", I understand that to be an assertion of some form of cross-subsidisation from the BBC contract into the C4 contract. We do not understand what that means. "Cross-subsidising" means you are less profitable on one contract by virtue of another, it is certainly not abusive; it is hard to know precisely what is meant. There is no assertion of predation there, we have been told on the basis of tittle-tattle ----

THE CHAIRMAN: Well no one has gone into abuses, I think it is generally accepted that we are not considering that.

MR. GREEN: And that is right, but it is also informative to work out precisely what the allegation is because the allegation is conduct at the time of the C4 ITT, the initiation to tender, it is variously described, or alluded to as being some form of cross-subsidy, elsewhere it is referred to as "discrimination", para.1.10 for example. At 8.1 they just use the words " a very low price", and at 8.2 they do say: "prices which do not cover variable cost", but the Tribunal is absolutely right nowhere is there a shred or a scintilla of evidence as to the actual pricing, of whether or not there is even a prayer of a case advanced that at the time of the contract there was ever any abuse.

THE CHAIRMAN: That, with respect, Mr. Green is not really something which IMS has access to the information that they would need in order to do that. What they would say is "That would be something for Ofcom to investigate.

MR. GREEN: I understand that.

THE CHAIRMAN: I do not think one can really criticise them for not knowing what all the pricing is and how it relates to your costs; that is information that is within your knowledge, not within their knowledge.

MR. GREEN: I understand that and I am not suggesting that this case turns upon that, but it is very important that one identifies, given a note of the arguments advanced today, precisely at what point in time the allegation is being made and what the nature of the allegation is, because I think one can analyse it this way: that if *ex hypothesi* Red Bee had engaged in some form of predatory pricing in order to secure a contract, then the fruits of that contract, the exclusivity, would be, if you like, unlawful benefits, but that highlights the fact that even if they were not in and of themselves abusive, there may be benefits which would have to be unravelled if the original conduct was abusive. If you acquire those rights on an abusive basis when you would not otherwise have gained them, then it may be said that you had unravelled the contract. But that is the allegation which is made against us that at the time of the contract those benefits, but for the unlawful pricing, would be lawful – they accept that and that is a fundamental part of their case, but for that the contract would be all

right. So that does focus attention upon the fact that it can only be at the inception of the contract that Ofcom was required to examine dominance, because there is no suggestion that anything that happens otherwise is abusive, and I will show you the case law.

THE CHAIRMAN: Well except the continued payment of the very low prices. It is not a situation where they were saying when they entered into the contract there was a one-off payment, or discount, and thereafter the prices were fine.

MR. GREEN: I accept that.

THE CHAIRMAN: It is the prices throughout the duration of the contract that they are complaining about.

MR. GREEN: That brings me to the second point, which is to analyse the alternative, which is assume for the sake of argument they are not dominant at the point of entering into the contract and that, let us say, two years' later they for whatever reason become dominant. Could it ever be said that the prices entered into in a competitive tender process absent dominance, could become dominance simply because you acquire a greater market share. That is highly improbable because the definition of something which is abusive is something which is abnormal, which is outside the scope of competitive, normal conduct. But by definition on this hypothesis, when the contract was entered into, we were dealing with a pure Article 81 situation, a normal competitive market shorn of dominance. So there is no dominance then but the only question is you acquire dominance two years' later does the original pricing become abusive? It is almost impossible to see how it could become so, because you have won that contract in competitive circumstances, whatever the price may be; it was a competitive price. If there is then a dominant company you then engage in a tender at a sub-cost price – below average variable cost for example – then of course that might be entirely different. But again, there is nothing in this appeal which puts on the Tribunal's table that latter issue, it just is not an issue which emanates from the notice of appeal. If they do not succeed before the Tribunal in establishing dominance in 2004 there is no alternative hypothesis. You questioned Mr. Hornsby this morning on precisely what his case was, and he came up with at least three different formulations of what his case was but he is not entitled to depart from his notice of appeal, and his notice of appeal makes it clear that it is 2004 and the position of market power then, which is the issue for the Tribunal. That is the issue which we are addressing. Nobody has addressed the other issue, and certainly so far as we were concerned, reading the notice of appeal in terms of preparing our statements of intervention to our skeletons it had not occurred to us we would have to address this alternative hypothesis, and since the statute makes it clear that the

appeal is determined by reference to the notice of appeal it seems to us to be right that this is the essential starting point. It really does not do for Mr. Hornsby to stand up and start inventing a case at this late stage. It is just not open to him to do that. So that, in our submission, is the starting point ----

THE CHAIRMAN: It was always clear that Mr. Hornsby was saying that Ofcom should have investigated the market position of Red Bee throughout the period 2004 to 2007, what was not clear was whether he was saying that they should have done that in order to identify whether, as at 2004, Red Bee was dominant, or whether he was saying that the question of dominance arises throughout the contract.

MR. GREEN: I agree, yes, I understand that, and that is right. That is why my starting point, of course, throws that issue into sharp relief. If the question is: was Red Bee dominant in 2004, even if you are looking at it from the perspective of a decision to be adopted two years' later, then you are looking at it as of 2004, and to look at the position in 2007 really gives you very little assistance, if any, and none has been pointed to by Mr. Hornsby, as to what the position is retrospectively in 2004. If it is a continuing matter then it may be different, so I accept the analysis, but that is why identifying what the proper framework for the analysis is very important as a starting point because it sheds light on that very question, and that is why we submit that Ofcom's analysis of looking at the market in 2004 and the period prior to it, and to the extent they took account of those factors is the correct one. There is nothing which happened after 2004 which retrospectively sheds light on that *a priori* question. Indeed, the only fact which changed was that in 2005 the BBC cast off its access division purchased by the Macquarie Group and then changed its name a year later to Red Bee from BBC Broadcasting. It did not actually change the BBC's internal capacity, it was still supplying itself after 2004 with the services, and then the same capacity, the same personnel were still supplying the BBC, it was simply pursuant to a transitional contract to get the business under way; that is all that changed in the market place. But the key question is were they dominant in 2004? Ofcom's analysis focuses, we submit, entirely logically on 2004 because that is the date of the abuse, and it is not an abuse arising in 2005, or 6 or 7. Had it been, then Ofcom might have been required to analyse the situation subsequently because that would be analysing the coincidence of the abuse with the market power, but that is not this case, so I accept that that is the right question.

PROFESSOR STONEMAN: Are you extending that argument to both the 82 and the 81 case, or are you just talking about the Article 82 here?

MR. GREEN: I am talking about Article 82, because we are looking at dominance for the purpose of deciding ----

PROFESSOR STONEMAN: I just want to make clear that you are not trying to extend it to Article 81.

MR. GREEN: No.

PROFESSOR STONEMAN: Fine.

MR. GREEN: No, the Article 81 point is a different issue altogether. In that regard, I think it is important to look at precisely what the decision actually said, and Mr. Anderson has summarised it in some detail, but I would like to pick up a number of important factors about the market, and what I was proposing to do was to summarise what we say are the relevant findings of fact – none of which are challenged – in the decision. When I say "none are challenged" there are astray assertions that some are correct, e.g. it is asserted that this is not a proper bidding market, that there is not a shred of evidence put forward by IMS to counter any of the facts relied upon by Ofcom. I want to set out what the facts are and I will give you the relevant paragraph numbers that we rely upon and then I will take you to some of the key ones. The relevant facts to us appear to be as follows: first, that Ofcom found that most broadcasters wanted medium term exclusive contracts and Ofcom set that out in some detail in the following paragraphs: 5.23.2, 7.23, and annex 4, A.4.2 to A.4.4. In those paragraphs Ofcom gives as the reasons for broadcasters wishing to conclude contracts on the basis of exclusivity as follows – and all of this, I should add, comes from evidence provided to Ofcom by the broadcasters and, indeed, by the access service providers, but these were the reasons given by Ofcom. First, the need for software and hardware systems to be integrated and kept connected between suppliers' and purchasers' sites. Secondly, reduction of procurement costs, thirdly minimisation and control of risk, since broadcasters tended to require their suppliers to be responsible for compliance with the Ofcom code and they did not want to duplicate the number of suppliers who were responsible for their regulatory risk; thirdly, reduced management costs, fourthly reduced prices because having exclusivity led to lower prices overall, and finally increased efficiency since broadcasters would give material so that the access services could be inserted into them to only one supplier. Now for all those reasons, which are classic efficiency reasons, broadcasters in this market seek to obtain contract services on the grounds of exclusivity. IMS does not challenge any of those reasons, they are all accepted as factually correct.

THE CHAIRMAN: What is the relevance of those legally though, because we know from *Hoffmann La Roche* and *British Plasterboard* that an exclusivity term or a loyalty rebate is

still an abuse of Article 82 even if it is with the agreement or at the request of the customer, because the anti-competitive effect is not to the detriment of the customer, but because of the foreclosure of the market to competitors.

MR. GREEN: One distinguishes between the cost and the efficiencies, when the Court of Justice in *Michelin* and other cases was recording that if a purchaser asks for a discount that is not an excuse, because the consequence is foreclosure nonetheless, they were not saying that if a discount is given and it is justified and normal because of efficiency reasons, that is somehow sufficient somehow to render it restrictive or abusive. So these are not cost related reasons, these are not the buyers saying: "We want you to give us a discount and we will give you long term exclusivity". These are customers saying: "For efficiency reasons, one of which is it stimulates the greatest possible price competition, we want exclusivity". So exclusivity is the key to achieving price competition and administrative and other efficiencies. I think it is quite different from the classic *Michelin* or *Hoffmann La Roche* situation, whereby the customer says: "It is a jolly good deal I am getting and I am not going to object. I like it because I am getting a very low price.

The second factual characteristic that we rely upon to show that Ofcom addressed its mind to all the correct issues was that the market had characteristics of a bidding market, and this plainly is a question of fact and degree in each case, but Ofcom sets out in very considerable detail its conclusions on this, in particular for your note para.7.17 to 7.26 and annex 4, a lengthy section pp. 76 to 82 of the decision itself. Importantly, in such a market Ofcom explains that market share is of limited value in assessing market power, and I would like to show you a small number of paragraphs, first, 7.9(i), p.42 of the internal numbering of the decision. It starts with these words:

> "In assessing whether BBC Broadcast was dominant at the time of the alleged contravention Ofcom has considered the following factors:
>
> > i) Existing competition – an undertaking is unlikely to possess market power if alternative sources of supply are present in the market, to which a consumer could switch if that undertaking attempts to act anti-competitively. Therefore, the market shares of firms in the market, both in absolute terms and relative to each other, can give an indication of the potential extent of a firm's market power. However, as is well recognised, a firm with a large market share will not always be dominant, since other features of the market may affect a firm's ability to exercise any potential market power. It is thus necessary to take into account both the competitive conditions at the time of

> the alleged abuse and those subsequent to it. Ofcom's consideration of market shares and other factors is set out above in section 6 and in paragraphs 7.10 to 7.26."

Just to pause there, Ofcom is here saying that even if you have very substantial market share that is not necessarily co-relative to market power because in a bidding market you need to take account of other factors, and it goes on in particular para.7.20 onwards, to talk about the relevance and significance of bidding markets; in fact, the section starts at 7.17 on p.44. In 7.17, just to summarise the point, Ofcom says that high market shares at one point may not be a permanent feature, and material market share changes can occur rapidly albeit at infrequent intervals. Consequently Ofcom's analysis of dominance relies more heavily on criteria such as barriers to entry, expansion, countervailing buyer power and less on market shares. They then refer to the Competition Commission's report in the *Arcelor/Corus* Group in which they identify four factors which they say may be relevant to a bidding market, relatively few large contests to supply customers which, they come to the conclusion later on, is applicable in this case; open contests with the opportunity for all suppliers to compete in each contest, and again they conclude that that is the case here, and you will recollect in relation to that what they said was that there were at least three main suppliers who met all broadcasters' requirements for quality and reputation, and thereafter what was significant was not so much those quality or reputational factors but price. Then they said no significant capacity constraints, which is another factor coming from the Competition Commission report; again they find as a fact there are no significant capacity constraints, indeed, there is excess capacity. Then they say brand image and other factors that are likely to be reinforced by repeated sales, for example, cost of switching between suppliers for customers should play no part. Again they address their mind to this and although they identified reputational factors, brand images, creating at least to some degree a barrier to entry, those companies who were in the market already they identified – having analysed the situation – there were no material switching costs between those who had the relevant reputation and there were a sufficient number of those.

Then they cite further in 7.19 and 7.20 from the Competition Commission's report, and then 7.21:

> "In a bidding market, if competition at the bidding stage is effective, having a high share of sales over a period of time may not be indicative of market power because most or all sales could be lost to a competitor in the next bidding round.

"7.22 The "winner takes all' aspect to a bidding market is an important factor in an assessment of competitive constraints. In the market for access services Ofcom has observed that in general television access services are either supplied in-house (for example ITV or, before the sale of BBC Broadcast, the BBC), as a result of a negotiated procurement (for example, Sky) or a competitive tender (for example Channel 4 or Five, Flextech and Disney). In the future it is likely that an increasing number of new but much smaller contracts will become available as more television broadcasters are required to offer more access services under the Ofcom Code."

Again, just pausing there, it is relevant that they found that this was an expanding market and, indeed, it is common ground, I think, between IMS, between Red Bee and Ofcom that the market is effectively doubling every year or two years because of Ofcom's statutory requirements. The Red Bee presentation, attached to IMS's skeleton refers to the market was doubling on a 12 monthly basis. In any event, we do not have very detailed information on that but it is rapidly expanding.

They then say:

"7.23 Ofcom has observed in para. 5.23.2 that most UK broadcasters prefer not to have more than one provider of all access services (i.e. they prefer to award exclusive contracts). This exclusivity means that most significant orders in the access services market are likely to be large enough to induce all capable suppliers to want to participate in each available tender."

Then in para.7.24 they say that their assessment of this market is set out in Annex 4, but they provide some conclusions: first, the majority of the market is characterised by a few large contracts, even excluding the BBC and ITV contracts.

"These large contracts are likely to be large enough to encourage capable suppliers to want to participate in each available tender.

ii) The tenders are, however, not completely open in that not all suppliers are invited to tender or regarded as suitably qualified bidders, although there are usually three or four suppliers which participate in each competitive tendering process;

iii) there are no significant capacity constraints; and

iv) in this market a well-established brand (akin to reputation) is likely to be favoured over another less established one. Broadcasters generally stated that they require their access service providers to have a certain minimum

level of reputation and experience and that at least three suppliers meet that threshold. Once this reputational pre-condition has been met, selection of a supplier then comes down to price which means that switching could and does occur. Thus although switching costs exist they do not in general preclude customers from switching provider."

The relevance of this is that market share is, in the peculiar circumstances of this market, treated by Ofcom as largely irrelevant, plainly not wholly irrelevant, but because of the structure of the market the precise level of market share is not at a premium, and this is because this is a competitive bidding market, and there is no challenge to the underlying facts which has led to Ofcom's conclusion.

These facts are then elaborated at considerable length in Annex 4, and I will not take you to everything in Annex 4, but I would like you to just see the extent of the work which Ofcom carried out so that they can be confident of their conclusions about the characteristics of the bidding market – this runs from p.76 through to p.82. They address here all of the various headings – you will see on p.77: "Few large contracts", "Open contests", "Capacity constraints"; on p.78: "Brand image and other factors which may reinforce repeat sales". They then deal with IMS's comments on bidding markets, so it cannot be said that their submissions were ignored and they set out their responses to it.

Their conclusion at A4.34:

"In summary, Ofcom considers that at the time of the alleged infringement the market for the supply of access services to broadcasters in the UK was characterised by a few large contracts, the absence of significant capacity constraints, some reputational effects akin to brand image and the selection of suppliers that satisfy the reputational criteria by way of open contests. Ofcom therefore considers that the relevant market, at that time, exhibited at least some of the characteristics of a bidding market."

Now, both the European Commission and the OFT in their guidance documents recognise in markets with such characteristics market share is less important. If you would please go to tab 35 in the authorities' bundle. This is the Commission's – DG Comps' – discussion paper of December 2005 at para. 32. The Commission here are making what I would submit is an obvious point, which is that market share is not in and of itself sufficient, and often nowhere near so. They say in para.32:

"The strength of any indication based on market share depends on the facts of each individual case. Market share is only a proxy for market power, which is the

> decisive factor. It is therefore necessary to extend the dominance analysis beyond market shares, especially when taking into account the difficulty of defining relevant markets in Article 82 cases, cf. section 3 above."

So market share is a proxy for market power, market power is the decisive factor in a bidding market, as Ofcom comprehensively explains, market power is limited by the characteristics of the bidding market, and again Ofcom is balanced, it does not say that the bidding market in issue is perfect in every respect, but they have analysed it thoroughly, they have not overlooked any particular facts, and they have come to conclusions which are not challenged.

If you jump back in the same bundle to tab 34, the OFT's assessment of market power, on p.12 there is section "Bidding markets", under the heading "Market shares and market power" on the previous page. Paragraph 4.4 on p.11 starts with this sentence:

> "Nevertheless, market shares alone might not be a reliable guide to market power, both as a result of potential shortcomings with the data (discussed in the next section) and for the following reasons:"

Then the second bullet point headed "Bidding markets":

> "Sometimes buyers choose their suppliers through procurement auctions or tenders. In these circumstances, even if there are only a few suppliers …"

and again we are talking there about suppliers with 20, 30,40 per cent of the market:

> "… competition might be intense. This is more likely to be the case where tenders are large and infrequent (so that suppliers are more likely to bid), where suppliers are not subject to capacity constraints (so that all suppliers are likely to place competitive b ids), and where suppliers are not differentiated (so that for any particular bid, all suppliers are equally placed to win the contract). IN these types of markets, an undertaking might have a high market share at a single point in time. However, if competition at the bidding stage is effective, this currently high market share would not necessarily reflect market power."

I rely on that simply to show that Ofcom's analysis is an orthodox one, it has applied the OFT guidelines, there is nothing untoward or unusual and importantly it has not been criticised by IMS, by adducing any evidence to show that the underlying facts are incorrect, or that the inferences drawn about those facts, about different aspects of the bidding market are incorrect.

There are a number of other points over and above the pure characteristics of the bidding market which Ofcom took into account: (1) that the market is expanding. I think it is

probably helpful just to pick up one or two points because in an expanding market plainly there are more opportunities coming forward. Ofcom said that it was not just this phalanx of large irregular contracts -- there are in fact a significant number of smaller contracts which sort of underpin this layer of large contracts. Perhaps it is sufficient to just give you the references: at 5.43 and footnote 64 on p.28 in the decision; para. 7.23; and in IMS' notice of appeal at paras. 1.7 and 8.2. IMS says in their notice of appeal, "The relevant market will double in value in the next few years". Indeed, you will see from the presentation attached to IMS' skeleton that they also talk about the market doubling in the next year or so.

The second point I would just like to throw into the melting pot is that there is no significant power over price. This was something else Ofcom investigated. Ofcom has quite a lot of evidence in the decision to the effect that if suppliers sought to increase price, then buyers would switch and take action to stimulate new entry - for example, decision 5.50 at p.29 and a fairly detailed and lengthy discussion at paras. 7.54 through to 7.63.

The net effect of that is that Ofcom's decision, as it stands, we say is unremarkable. It analysed dominance and the market as of the date of the alleged infringement. We object to any attempt to reformulate the case at this late stage. The date of the alleged infringement was the date that the contract was entered into. It was 2004. Therefore Ofcom was required to analyse the market there and thereabouts. There is no law at Community or national level which says that Ofcom has to look at a three year or a two year period. It does whatever is necessary in the circumstances. In this case it asked a very, very large number of questions - there are about three or four pages just listing the number of requests for information it sent out to broadcasters and access service providers. It instructed an expert agency to conduct interviews for it, and it got very detailed, contemporaneous evidence as to the manner in which the market was operating. If any evidence had arisen which suggested the market was not in a relatively steady state or was going to be subject to unpredictable changes, it would have come out of that evidence. But it did not. So, we submit that Ofcom's approach was beyond criticism. The matters it addressed its mind to were beyond criticism. In that regard, it squarely addressed the relevance of market share - market share as of mid-2004. We submit that in the context of a notice of appeal, which is, with great respect, exceedingly thin, and which is not supported by factual evidence of an expert, or even trade expert nature, that it is, with respect, not open to the Tribunal to simply find a reason to unravel a detailed decision. It might have been different if we had had, as in many cases, very detailed expert evidence which challenged the underlying facts, and in a merits appeal you concluded that Ofcom had misdirected itself or made material errors in those

facts. But, that is not this case. Simply because we have a relatively medium-sized company making the appeal is not an excuse to permit it to adopt a method of challenge which is out of the ordinary.

That is what I wanted to say about the decision. I do not know if that is an appropriate moment for today. I was going to deal tomorrow with the question of five or eight years. It would give me, overnight, the chance to find out what the position is on the contract because I would very much like to provide you with, in particular, the terms of Clause 4 of the contract, or a contract in redacted form so that you can see it. I think that will just cast light on the Chapter I issue.

THE CHAIRMAN: How much longer do you think you would be tomorrow, Mr. Green?

MR. GREEN: I think I would probably be half an hour.

THE CHAIRMAN: I think we had better rise now and then come back tomorrow morning.

Thank you.

(Adjourned until 10.30 a.m. on Tuesday, 8th April, 2008)