ERICSSON/CREATIVE MERGER INQUIRY

Summary of hearing with Arqiva Limited held on Tuesday 19 November 2013

Background

1. Arqiva Limited (Arqiva) was involved extensively in the UK broadcasting market and worked with a number of broadcasters in both television and radio. Playout represented roughly [✂] per cent of its business, approximately £[✂] million of a total turnover of about £820 million.

2. Arqiva carried around 50 channels globally and supplied playout to most of these. Its playout business had developed over a number of years and was recently upgraded.

The market

3. Arqiva believed that the linear playout requirements of the BBC, ITV and Channel 4 accounted for about 40 per cent of the UK's outsourced playout market revenues. It identified four distinct consumer groups in the market: public sector broadcasters (PSBs); bespoke channels; multi-channel customers; and single-channel customers, which included 'channel-in-a-box'. Each group had distinct requirements and distinct suppliers and Arqiva believed each was a separate market, with PSBs at the most complex end of the spectrum.

4. The single-channel customers had the least complex requirements, consisting of simple channel compilation, simple graphics and a fixed schedule with no live output. Arqiva believed this part of the market was very price sensitive and many suppliers were active in it. A typical channel had a viewing audience of less than 100,000 people and this part of the market accounted for less than 15 per cent of the total outsourced playout revenues.

5. The PSBs were the most complicated based on scale, complexity, live programming and disaster recovery. The PSBs supported complicated regional programming requirements and the commercial PSBs also supported regional advertising. The main ITV channel was equivalent to around 30 regional channels, with viewing figures of around 11 million for its most popular programmes. BBC One was just as complicated, providing regional programmes for around 20 regions and the nations, and had similar viewing figures to ITV for its most popular programmes.

6. The PSBs (except Channel 5) were currently served by Ericsson and Red Bee Media (RBM), which were the only providers that possessed the relevant assets, broadcasting experience and key skills to serve these PSBs. [✂].

Tender process

7. The playout market was quite dynamic, with a continuous supply of single-channel and multi-channel tenders. It was unusual to be informed by the customer of the identity of the other bidders, but it was not difficult to get a feel for what other competitors offered.

8. The tender processes differed by sector. For a single-channel tender, there would typically not be a formal process. Customers would contact providers to establish a price for their requirements and would choose a provider based on that price and the

facilities that were offered. The more complex channels would typically issue a request for proposal (RFP) to five or six providers, followed by a shortlist of three and a further discussion and refinement of the contract requirements. At this stage of the process a site visit was requested by the customer, and for some tenders Arqiva had created a test channel to demonstrate its capabilities.

9. Arqiva tried to ensure that its multi-channel customers used its standard architecture and equipment to avoid incurring additional investment and expenditure.

10. Eventually two bidders or an outright winner would be selected and it was at this stage the final price would be discussed. There were significant differences in the tender times. The less complex, multi-channel tenders could take three to four months and the PSBs 12 to 18 months. Arqiva believed barriers to entry for PSBs were very high and tenders for the PSBs were usually a long and expensive process.

11. The RFP would typically focus on technical and operational capabilities and the provider would have to demonstrate how it would comply with the requirements. Providers would reference current customers and demonstrate what it did with regard to technical architecture and service delivery. In the bespoke environment, Arqiva would cite BT's ESPN sports channel as an example of its achievements. In the multi-channel environment, it cited channels such as Fox and CBS, though it was brand familiarity with each, rather than the complexity of these channels, that was its key selling point.

12. Arqiva understood that the BBC would start its formal procurement process in early 2014 and Arqiva would engage in the early stages of the process to identify components of the tender that it could compete for. [✂]. The latest BBC playout procurement was expected to last about 18 months and Arqiva estimated it could cost around £[✂] million to participate in the entire process. The successful bidder would have to demonstrate that it would deliver complex services and channels and manage the transfer of the skills and knowledge from the incumbent.

13. Arqiva believed that a bid for the BBC contract [✂].

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Incumbency advantage

15. Arqiva believed that a company such as Ericsson could challenge the incumbent for the BBC contract due to its knowledge and understanding of a multi-channel environment. The ability to provide new technology could also level the playing field, though Arqiva was disadvantaged with the PSB contracts due to its lack of knowledge and experience in this environment.

16. The actual process of providing playout did not differ to a massive degree between suppliers. Moving content from one playout provider to another might prove a disincentive to switch providers as customers might have to change their method of operating to accommodate a new provider.

17. Due to its knowledge of the channels and the relationships they had in place, Arqiva tried to ensure that it could TUPE staff when it won a contract. It had recently taken over the Turner playout contract and though TUPE did not apply in this instance it was currently engaged with Turner to ensure that it could acquire individuals from its playout team.

Recent tenders

18. At the time it won the playout contract for ESPN, Arqiva was proving playout services for British Eurosport (Eurosport). The ESPN contract was effectively in two parts, with one section focused on Premier League football and the other focused on ESPN's US channels, for which RBM was the playout provider.

19. ESPN had acquired the rights to broadcast Premier League football following the collapse of Setanta and wanted a provider that could get the football coverage on air as quickly as possible, for which Arqiva was in a strong position. With the other channels, Arqiva offered a very good price and was able to demonstrate that it could support the channels' integration with the content preparation.

20. Arqiva was unsuccessful with its bid for the BT Sport tender. In Arqiva's opinion, some of the contractual clauses around playout errors were extremely punitive and BT was also looking for the provider to be as keen on price as possible. Arqiva believed that given how much BT was staking on its reputation, it wanted the provider it thought was the best and lowest risk in the market.

21. Arqiva had recently won the playout contract for Turner and would provide playout services from 2014. Turner had previously insourced its playout, but had decided to outsource to save costs. It had offered a number of playout packages during the tender and one factor behind outsourcing was that it wanted playout to be based in the countries where the channels were broadcast.

Complexity

22. Live content for the BBC presented a number of different challenges compared with other broadcasters such as ESPN or Eurosport. The latter operated in a fixed-genre environment, which meant that the number of unexpected events were limited to games overrunning and impacting on another live event or, during US sporting events, having to take advertisement breaks at short notice.

23. BBC One operated in a mixed-genre environment and had fixed points such as news and popular live shows. In the event of an unexpected breaking news story, interventions to the schedule were required. The difficulty with the BBC was that whereas the sports channels such as ESPN and Eurosport had one individual that made the decisions, the BBC had presentation editors discussing editorial decisions with a number of Controllers. For example, on BBC One, in addition to the Channel Controller, there would be different Controllers each responsible for a specific genre of programmes. A situation could arise where a certain genre of programme was about to overrun and clash with another genre of programme and the playout provider would be caught in the middle of a conversation between the different Controllers.

24. Arqiva highlighted the complexity of coordinating the BBC's Nations and Regions. ITV was slightly less complex than the BBC as it had regional opts and did not have the complexity of the BBC's nations which opted away from the network to a greater extent. However, ITV had more regions, sub-regions and regional advertising and the number of regions added to the upfront complexity of the playout system design. This required a very good knowledge of the customer's workflow and the capability to design and operate complex systems.

25. Channel 5 was less complex than Channel 4. Arqiva believed that Channel 5's requirements were closest to the type of services that it provided in its bespoke environment. Channel 5 had much less regionality, and the type of regionality it had

could be delivered with what it called ‘slave channels’. These were effectively channels run off the back of a main channel in an analogous way to the ‘pubs and clubs’ variant of a sports channel. [✂]. Channel 4 and ITV had a more granular level of regional advertising which made them far more complicated than Channel 5’s which had fewer larger advertising regions.

26. In 2008, Arqiva had the opportunity to bid for the Channel 4 contract. [✂].

27. Providing playout for Channel 5 [✂].

Competitors and the merger

28. Arqiva viewed RBM, Ericsson and Encompass as its main competitors in the bespoke environment. Encompass was credible as it held the Channel 5 playout contract and had a large presence in the USA. It could use this to leverage its position in the UK and could offer credibility with reference to its US-based clients.

29. Arqiva believed that if Ericsson and RBM merged, all effective competition would be removed from the [✂] playout market. A merger would create a dominant player that had over 50 per cent of the revenue from outsourced linear playout and the merged entity would have such scale that other smaller providers would then struggle to compete with in other market segments. Competition would be distorted across the market and it would be harder for companies such as Arqiva to grow, particularly in the segments in which it operated.