



**SKY'S SUPPLEMENTAL SUBMISSION IN RESPONSE TO OFCOM'S PHASE II SUBMISSION  
IN THE CMA'S PHASE II REVIEW OF BT'S ANTICIPATED ACQUISITION OF EE**

**24 AUGUST 2015**

This is Sky's supplemental submission addressing points raised by Ofcom in its submission to the CMA published on 13 August 2015 in the Phase II inquiry into BT's anticipated acquisition of EE (the "Merger"). This response supplements and should be read in conjunction with Sky's previous submissions.

**1. Introduction**

- 1.1 Sky considers that a number of the submissions made by Ofcom are untenable. Ofcom argues that existing and future behavioural regulation in the telecoms sector is sufficient to address any potential SLCs raised by the Merger.
- 1.2 Sky is concerned that a reliance on behavioural regulation, as proposed by Ofcom, would be wholly insufficient to address the SLCs likely to arise from the Merger, both as a matter of law and in practice, given that:
  - 1.2.1 behavioural regulation is unable to address the SLCs in a comprehensive, effective, clear-cut or merger-specific manner, of which the CMA is required to satisfy itself before approving the Merger;
  - 1.2.2 existing regulation is: (i) insufficient in the areas affected by the Merger that are currently regulated; and (ii) absent in other areas affected by the Merger; and
  - 1.2.3 future regulation is unable to resolve the SLCs in a timely manner, with the high degree of certainty required.

**2. Inability of behavioural regulation to effectively address the merger SLCs in a manner that discharges the CMA's legal duties**

- 2.1 As outlined in Sky's previous submissions, Sky expects the Merger to enhance BT's ability and incentives to foreclose downstream competition from rival communications providers (CPs), thereby significantly lessening competition to the detriment of end-customers.
- 2.2 Ofcom's submissions do not appear to take account of the CMA's legal duties in addressing these Merger-related SLCs. As the CMA is aware, once it has identified SLCs and is considering remedial action, it is required to achieve as comprehensive and effective a solution to the SLCs and any adverse effects resulting from them as is reasonable and practicable.<sup>1</sup>

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<sup>1</sup> See Section 36(3) of the Enterprise Act 2002 and paragraphs 1.7 and 1.8 of Merger Remedies: Competition Commission Guidelines November 2008 (the "Merger Remedies Guidelines"): [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/284415/cc8.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/284415/cc8.pdf).

- 2.3 To discharge this duty, the CMA has stated that it will identify whether remedies are capable of:<sup>2</sup>
- 2.3.1 comprehensively addressing the SLCs and their adverse effects;
  - 2.3.2 addressing the concerns quickly and throughout their expected duration (i.e., not relying on remedies that will only have an effect in the long term, or where the timing of the effect is uncertain);
  - 2.3.3 effective implementation, monitoring and enforcement; and
  - 2.3.4 achieving their intended effect to a high degree of certainty.
- 2.4 As the CMA is aware, contrary to Ofcom’s submissions, structural remedies are typically preferable to address merger-specific SLCs, rather than measures seeking to regulate the ongoing behaviour of the merging parties.<sup>3</sup> Structural remedies are designed to re-establish the market structure absent the merger, and are therefore expected to be more effective at addressing adverse merger effects comprehensively at source.<sup>4</sup> They offer a clear-cut solution thus avoiding the deficiencies of behavioural regulation, which include requiring costly ongoing monitoring and enforcement, distorting firms’ investment incentives and encouraging regulatory gaming. In Sky’s view, Ofcom’s submission is overly sanguine about the ease with which SLCs can be addressed effectively via regulation.
- 2.5 Where a merger leads to a lasting alteration of the structure of the market such that the merged entity has both the ability and incentive to distort competition, as in the present case, behavioural remedies are largely considered inappropriate.<sup>5</sup> As discussed further below, a reliance on existing or future proposed behavioural regulation would not meet the CMA’s criteria for remedies to be merger specific, nor is it capable of comprehensively or effectively addressing BT’s enhanced ability and incentives post-merger to foreclose downstream competition.

**3. Existing regulation is: (i) insufficient in the areas affected by the Merger that are currently regulated; and (ii) absent in other areas affected by the Merger**

- 3.1 Existing regulation is unlikely to be capable of comprehensively or effectively addressing specific SLCs arising from the Merger.
- 3.2 First, existing regulation is not merger-specific. Existing regulation was implemented before the Merger was in contemplation, premised on historic assessments of the pre-merger competitive landscape. By its very nature therefore, the existing regulatory regime cannot have considered the specific SLCs arising from the Merger.
- 3.3 Secondly, where Merger-related SLCs arise in areas which are currently regulated - fixed broadband and mobile backhaul - existing regulation is insufficient to meet the effectiveness criteria set out in section 2 above:
- 3.3.1 Even pre-merger, despite existing regulation, BT’s existing ability and incentives to undermine downstream fixed standard broadband competitors has resulted in distortions of competition arising from: (i) Openreach’s investment decisions and

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<sup>2</sup> Paragraph 1.8 (a) - (d) of the Merger Remedies Guidelines.

<sup>3</sup> Paragraph 1.8(a) of the Merger Remedies Guidelines.

<sup>4</sup> Paragraph 1.8(a) of the Merger Remedies Guidelines.

<sup>5</sup> See for example *Gencor v Commission* (Case T-102/96) and *Commission v Tetra Laval BV* (Case C-12/03P).

resulting quality of service; (ii) product development for competing CPs; and (iii) cost allocation.<sup>6</sup>

(a) In standard fixed broadband, for example, Ofcom has acknowledged elsewhere that regulation cannot remove BT's strong incentives to favour its downstream divisions, and can only partly control BT's current ability to foreclose downstream rivals.<sup>7</sup>

(b) Further, existing regulation primarily governs CPs' relationships with Openreach. However, CPs also source a number of key wholesale services from BT Wholesale rather than sourcing individual inputs from Openreach, for example, the managed mobile backhaul product MEAS. These managed wholesale services are not regulated and there is limited alternative supply to BT Wholesale. Sky has already highlighted in its previous submissions the effects of this lacuna in regulation.<sup>8</sup>

3.3.2 Post-merger, as outlined in Sky's previous submissions, BT's enhanced ability and incentives to distort downstream competition in fixed broadband and mobile backhaul would put further strain on the existing regulatory regime, rendering it even less capable of constraining BT's behaviour. For example, as Ofcom recognises,<sup>9</sup> in superfast broadband, BT has the existing ability and incentive to foreclose competitors through its provision of GEA, subject to "light-touch" regulation. Post-merger, the already complex VULA margin test that applies to BT's provision of GEA will increase in complexity and both its effectiveness and Ofcom's ability to monitor compliance with it is likely to be undermined, affording BT increased scope to evade the test.<sup>10</sup> A reliance on this complex regulation to resolve Merger-related SLCs would run counter to the requirement for the CMA to be mindful of effective implementation, monitoring and enforcement.<sup>11</sup> To the extent such activity is "elaborate and intrusive"<sup>12</sup> the practicality and therefore effectiveness of the remedy is unreliable.

3.4 Finally, as the Merger would extend BT's distortive incentives into new commercial activities, such as mobile network services, fixed-mobile services and small cell networks, SLCs are likely to arise in areas that are not currently regulated. As such, existing regulation offers no comfort. In relation to small cells, for example, access to BT's cabinets and its MIIS service is currently unregulated. Post-merger, BT-EE would have both a substantial ability and a new incentive to foreclose access and stifle nascent competing small cell deployments. This is a situation neither contemplated nor controlled by current regulation. Further, a reliance on non-discrimination obligations in SMP regulation (as Ofcom suggests) to contain the merged entity's incentives will only bite in relation to

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<sup>6</sup> See Section 3(A) of Sky's response to the CMA's Statement of Issues.

<sup>7</sup> See further the multiple examples of BT's ability to discriminate notwithstanding regulation set out in Section 11 of Ofcom's Strategic Review of Digital Communications, Discussion document dated 16 July 2015. <http://stakeholders.ofcom.org.uk/consultations/dcr-discussion/>

<sup>8</sup> See for example, Annex 2 of the Sky Response to the CMA Statement of Issues.

<sup>9</sup> Paragraph 3.69 of Ofcom's Approach to the VULA Margin - Final Statement (<http://stakeholders.ofcom.org.uk/consultations/VULA-margin/statement/>).

<sup>10</sup> See paragraphs 3.14 to 3.17 of the Sky Response to the CMA's Statement of Issues.

<sup>11</sup> Paragraph 1.8(c) of the Merger Remedies Guidelines.

<sup>12</sup> Paragraph 1.8(c) of the Merger Remedies Guidelines.

Openreach activity in regulated markets and therefore its ability to address the Merger-related SLCs in other areas, such as supply of services by BT Wholesale, is limited.

#### **4. Future regulation does not offer a timely and certain solution**

- 4.1 The CMA's guidance identifies a preference for remedies that act quickly in addressing competitive concerns.<sup>13</sup> A reliance on future regulatory intervention would neither be a timely nor a certain solution for addressing the Merger-related SLCs.
- 4.2 The outcomes of Ofcom's periodic market reviews lie too far in the future to offer a timely solution to the merger SLCs, and there is no guarantee that, at the end of any such review, Ofcom will introduce regulation that is targeted specifically at an SLC arising from the Merger. The CMA could not discharge its legal duties on this basis. For example, as part of its ongoing Business Connectivity Market Review, Ofcom is currently consulting on potential regulation requiring BT to offer a 'dark fibre' product. However, even if Ofcom proceeds with such regulation – it is fiercely opposed by BT – this would only become effective from 2017 and the details of its practicability are unclear. As such, that remedy is at present insufficiently certain, timely, or suitably designed in order to address the potential concerns highlighted by the CMA.<sup>14</sup>
- 4.3 Further, Ofcom's design of spectrum auction awards occurs only periodically and is primarily focused on ensuring the efficient distribution of the spectrum subject to the auction. As such, contrary to Ofcom's suggestions, it does not offer a merger-specific or timely solution to the Merger-related SLCs arising in mobile network services and small cell networks.

#### **5. Conclusion**

- 5.1 For the reasons set out above and already addressed in Sky's previous submissions,<sup>15</sup> behavioural regulation, as advocated by Ofcom, would be insufficient to effectively and comprehensively address the merger-specific SLCs arising from the Merger and therefore to discharge the CMA's obligations when considering remedial action.
- 5.2 Prior to full local-loop unbundling in 2005 and the absence of scale infrastructure-based competition, BT enjoyed a dominant position in the provision of retail broadband. If the Merger-related SLCs are left unaddressed or addressed insufficiently and ineffectively *ex ante* through a misplaced reliance on behavioural regulation, the Merger risks: (i) unravelling the significant developments in competition over the last ten years; and (ii) allowing BT to re-establish a dominant position and extend it into mobile, small cell networks and increasingly fixed-mobile services. The CMA could not in these circumstances discharge its duties in remedying the SLCs created by the Merger. Telecoms regulation would be left straining, retrospectively and inadequately, to cope with the significant reduction in competition and consequential harm to consumers arising from the Merger.

**Sky 24 August 2015**

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<sup>13</sup> See paragraphs 1.7 and 1.8 of the Merger Remedies Guidelines.

<sup>14</sup> See paragraphs 59 and 60 of the CMA's Statement of Issues ([https://assets.digital.cabinet-office.gov.uk/media/55a8c150e5274a6fea00000d/BT-EE - issues\\_statement.pdf](https://assets.digital.cabinet-office.gov.uk/media/55a8c150e5274a6fea00000d/BT-EE - issues_statement.pdf)).

<sup>15</sup> See for example section 10 of Sky's initial submission in the Phase II review of the Merger.