5 Views of third parties

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Introduction

5.1. This chapter summarizes views of third parties. Almost half of the parties from whom we heard expressed concern about aspects of the merger, main concerns being about its effect on the market for pay-TV, in particular on providers of pay-TV content, but with some concern also about effect on telecommunications and other issues. In several cases, the concerns were based on a perception of the market strength of cable operators arising from the closed nature of the cable networks, and the ability of the operators to bundle pay-TV, telephony and other services. Others saw scope for the merger to enhance

competition between platform operators, although of these a number nonetheless felt aspects of the cable industry, in particular open access to it, should at some point be separately reviewed. We also asked a number of media commentators about their perception of the market.

Views of regulatory bodies

Independent Television Commission

5.2. The ITC told us that, with regard to competition issues, its role was to ensure fair and effective competition in the provision of TV and related services. In practice it saw this as protection of the viewers' interest. In the context of the move from analogue to digital transmission the ITC wished to see effective competition between the three main digital platforms, that is satellite, cable and terrestrial, and to encourage the development of other emerging technologies such as ADSL which could further increase viewer choice. It was, however, in its view essential to have competition for the provision of programme content and programme rights as well as competition among platforms, in order to provide as wide a choice as possible for viewers.

5.3. Furthermore, with increasing competition for programmes, the ITC believed that viewers must have the opportunity to move between platform suppliers at a minimum of cost and inconvenience. The ITC's view was that this goal could best be achieved through making access more 'open' by stimulating a market for open standard digital TV sets which did not contain embedded proprietary technology relating only to one platform or conditional access system.

5.4. The ITC said that while NTL and CWC were involved in both telecommunications and TV services, it was the latter area that was relevant to the ITC's duties and responsibilities. There were two aspects to consider: the retail market for pay-TV services, and the market for programme rights.

The retail market for pay-TV services

5.5. The ITC said that consumer demand for pay-TV services was presently met via three main distribution platforms: cable, satellite and digital terrestrial. The five largest pay-TV providers accounted for over 95 per cent of the market. The largest was BSkyB with over 50 per cent. The proposed merger would provide the merged entity with a share of this market, at the national level, of around 28 per cent in terms of subscribers. However, NTL and CWC did not currently compete with one another for pay-TV subscribers, because they operated in different geographic markets. Moreover, as a result of both policy (with the removal of exclusive licences, of restrictions on BT's ability to broadcast and the unbundling of BT's local loop) and technological developments such as ADSL, cable operators were expected in the near future to face significantly increased competition.

5.6. Cable operators had originally been granted exclusive licences in local geographical areas. However, they might now voluntarily give up this exclusivity (and many had a financial incentive to do so because it excluded them from significant tender payments to the Exchequer, and also from obligations to build further infrastructure) thereby allowing other operators to enter the same area. NTL had chosen this course in respect of its 14 exclusive Local Delivery Service licences with effect from the beginning of 2000, although it would continue to hold other, older exclusive licences that did not carry obligations to make tender payments for the time being. In accordance with Government policy, geographic exclusivity would be completely removed from 1 January 2001.

5.7. Despite this loss of exclusivity, it was highly unlikely that any cable operator would wish to incur the significant capital investment involved in building a parallel distribution network. In other words, even in the absence of the merger, NTL and CWC would be unlikely to build in areas where the other had already established a network. That said, the cable operators were likely to face the threat of the following new entrants.

5.8. First, under the Government's Broadband Britain initiative, public telecommunications operators (PTOs) would be allowed to offer pay-TV services over their main networks once the cable operators' exclusivity was removed. Developments in DSL technology would allow BT, in particular, to offer high

bandwidth services, such as VOD, over its public telephone network. This could be achieved much more quickly than the time it had taken the cable operators to build their infrastructure. For example, BT announced in July 1999 that it intended to upgrade some 400 exchanges serving 6 million households with DSL technology by March 2000.

5.9. Secondly, OFTEL had announced in December 1999 that BT was to make its local loop network available to competing operators who might wish to upgrade BT's infrastructure in order to provide high bandwidth services of their own over it. Moreover, the ITC understood that OFTEL would be launching a consultation on open access to cable networks. There were also prospects that microwave radio links could provide a further platform extension for pay-TV and other services currently available, for example, on cable.

5.10. The ITC accepted that cable operators accounted for as much as 80 per cent of viewing of pay-TV channels in multi-channel homes where cable was active, but believed that this overstated its market position. Cable accounted for a much lesser proportion of all multi-channel households, and remained highly dependent on the distribution of BSkyB programmes: its share of the total value chain in the provision of services would be much smaller.

5.11. The ITC told us that (subject to the announcement by the Secretary of State on 16 December concerning the divestment of France Telecom's holdings in Crown Castle) it was not concerned about NTL's range of interests in related activities including transmission systems and the DTT platform, given, respectively, the degree of regulation of transmission systems, and the limited extent of NTL's interests in DTT.

5.12. The ITC concluded, therefore, that a merger of NTL and CWC's cable business was unlikely to limit competition for pay-TV services in a way which was detrimental to the interests of viewers and subscribers.

The market for programme rights

5.13. The ITC said that the key drivers of pay-TV in the UK had been first-run sport and feature films, particularly football. The ITC believed BSkyB currently had market power in the supply of these premium services and it was keen to see the development of greater competition in the market for acquiring the related broadcasting rights. It believed the proposed merger would make this more likely.

5.14. On the supply side, the relevant rights owners were generally substantial organizations able to protect their own interests, most particularly perhaps in relation to those major Hollywood studios who owned key film rights. On the demand side, a buyer's ability to bid for exclusive rights was linked to its subscriber and thereby its revenue base, thus creating a virtuous circle whereby the acquisition of key rights could help drive subscriber take-up, and higher subscriber take-up helped fund more competitive bidding for rights. Currently, CWC had no presence in these markets and NTL had only a limited presence through its joint PPV film venture with Telewest (Front Row) and British Eurosport. The majority of films and sports programming offered to viewers by the cable companies was bought from BSkyB in its role as wholesaler.

5.15. The ITC believed that the enlarged cable operator would provide stronger competition to BSkyB and other pay-TV operators in bidding for exclusive programming rights offered by third parties for sport and films. The new company would be able to exert more buyer power, and this should increase competition in the wholesale markets for programme rights. The ITC also believed that sellers of rights, particularly in relation to football, would in future offer them in varied 'packages' in which more than one company could participate.

5.16. The ITC did not accept the concern that the merged company would be free to charge for transmission of must carry free-to-air public service broadcasts. Cable operators were obliged by statute to carry such programmes, and could not displace that obligation by imposing a price.

5.17. The ITC said that the question of possible open access to the cable networks was a matter for OFTEL, to whom the ITC, once it had considered its position, would be giving its views. However, until there was more competition in programme supply, it might be considered too early to move to open access; if open access were rapidly introduced, BSkyB was likely to move from a wholesaling to a

retailing function, enhancing its strong market position in the supply of premium programme services. The problems that arose with the crowding out of some channels would, the ITC believed, be resolved when digital transmission was introduced on cable, and the current limitation on the number of channels that could be carried was removed. Open access would still be available as a remedy should the cable operators develop a stronger position in the market in future than was currently expected. Should the OFTEL review, therefore, conclude that open access was not at present appropriate, it would be desirable for the matter to be reviewed again in two or three years' time.

Conclusions

5.18. The ITC therefore believed that the merger would not operate against the interests of viewers and subscribers in the retail pay-TV market. Moreover, the increased buying power of the new company in the markets for exclusive programme rights should actually increase competition. The ITC believed, therefore, that it was in the public interest for the proposed acquisition to proceed.

Office of Telecommunications

5.19. OFTEL said that its overall assessment was that the transfer of the assets of CWC's consumer business did not raise competition concerns. While NTL and CWC were present in the pay-TV and certain fixed telephony services markets, the concerns of OFTEL had related mainly to separate arrangements for interconnection post-merger.

Pay-TV

5.20. In OFTEL's view, retail pay-TV, including satellite, cable and DTT, was a relevant product market. As stated in a recent ITC/OFTEL consultative paper, different platforms appeared to be effective substitutes for most viewers. OFTEL also believed that there was no basis currently for considering analogue and digital to constitute discrete product markets. In OFTEL's view, the question of the geographical coverage of the market was debatable. However, having considered the arguments in favour of there being either a national or a number of local markets, OFTEL considered that a national market was the more appropriate definition. This was because of the effect of nationally uniform tariffs of ONdigital and BSkyB on the ability of cable companies to set prices. Consumers would still have the choice between three competing platforms, as now, regardless of the change in ownership. Furthermore, other platforms for delivering pay-TV might become available in coming years, including, for example, DSL technology.

5.21. On this basis, the parties had estimated their combined market share at 28.5 per cent by subscribers and 20.5 per cent by value. The corresponding shares for BSkyB were 52 and 65 per cent respectively. Telewest shares were estimated at 15.5 per cent by number of subscribers and 14 per cent by value. ONdigital, a new entrant, had an estimated 4 per cent share of subscribers. Market share alone, however, was not conclusive. Although the market was considered to be national, the fact that there was no present geographic overlap between the parties in pay-TV meant that there was no effective reduction in the number of competitors from which consumers could choose. Consumers would still have a choice between three competing platforms, as now, regardless of the change in ownership, and DSL technology could also, within five years, deliver the volume of data that a broadband system could currently deliver with a cable system. The market power of the cable companies was further limited by their dependence on the premium programming of BSkyB: OFTEL believed the effect of the merger could be to strengthen cable's position in pay-TV and the countervailing power of the merged group, with the possibility of it becoming a wholesale premium programmer itself.

5.22. While cable operators were, together with BSkyB, obliged to make available their digital conditional access services, cable operators were not currently obliged to grant access to their delivery network. However, OFTEL would be considering this issue in more detail in the near future through a consultation on open access. Even if, however, cable operators did not currently have market power, that would not necessarily apply for the future. Open access would be a legitimate regulatory tool if it led to more effective competition: if cable operators in future had such market power that such circumstances

arose, OFTEL would have to seek an amendment to their licences to impose any open access requirement.

Fixed retail telecommunication services

5.23. OFTEL agreed with the parties that even taking the most limited of various possible alternative market definitions, the increment accruing to the combined NTL and CWC telecommunication services to directly connected residential and small business customers would not alter the overall competitive position to any appreciable extent, because of the lack of geographic overlap between the companies and BT's continued very strong position.

5.24. However, the reasons for being relatively relaxed about the effects on competition in relation to directly connected residential and small business customers did not read across to the position in the wider business telecommunication markets. OFTEL had three main areas of potential concern, discussed below.

Cross-shareholding arrangements

5.25. Although the parties maintained that they were not proposing to merge their operations in these areas as part of the notified transaction, OFTEL had been told that C&W would have a stake of between 4.3 and 17.3 per cent in NTL on completion. A stake larger than 7.5 per cent would entitle C&W to appoint a director to the NTL board. A minority stake would not confer control, and it might be argued that the remaining shareholders would move to prevent C&W influencing board decisions against their own interests. However, control by other shareholders would not necessarily prevent exchange of information between C&W and NTL which could facilitate collusive behaviour to NTL and C&W's mutual advantage. This was not to say that such collusion was inevitable. But given that there might be an incentive for NTL and C&W to compete less vigorously against one another than if they were entirely separate, and that a cross-shareholding arrangement might facilitate such behaviour, it seemed legitimate to consider the possible effects on competition were that outcome to occur. At one limit, the effects of coordination of activities between NTL and C&W could be similar to those of a full merger.

5.26. OFTEL believed it was unclear why cross-shareholdings should be necessary in order for the parties to proceed with the merger, since the main benefits accruing to the parties were not obviously dependent on them. Even if a case could be made as to why the cross-shareholdings were needed, there would still be a need to consider the potential effects on competition arising as a result of any coordinated or collusive behaviour by the parties outside the merged entity. The limited market shares of the two companies in providing indirect access services for businesses did, however, reduce that concern, as did the reasonably competitive nature of the market.

Preferential termination rates

5.27. The parties had agreed interconnection agreements which they stated were a key part of the overall transaction. Under the relevant arrangements, the parties had agreed that for national traffic terminating on the other party's network, [*Details omitted. See note on page iv.*]. (This agreement was later amended; see paragraphs 3.86 to 3.118 and 6.119.) [

Details omitted. See note on page iv.

]

5.28. Accordingly, BT's call termination rates were currently subject to an RPI–8 per cent price cap under the Network Charge Control regime. This cap was set in the context of agreeing principles for guiding charges for call termination paid by BT to other licensed operators for terminating calls on their networks. The industry agreed that charges for BT terminating calls on other licensed operators' networks would be set on a reciprocal basis—ie they would be based on charges for terminating calls on BT's network.

5.29. OFTEL believed, therefore, that [

Details omitted. See note on page iv.

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[

Details omitted See note on page iv.

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Preferred supplier agreements

5.30. The parties had agreed that C&W would be NTL's preferred supplier for some services where NTL was unable to deliver the service itself and [*Details omitted. See note on page iv.*]. OFTEL recognized a legitimate rationale behind such an agreement in principle, but queried why the terms were set [

Details omitted. See note on page iv.

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5.31. OFTEL felt that it was not obviously in NTL's interest to tie itself into C&W if that meant passing up the possibility of keener prices elsewhere—at least not without gaining something in return. It might be that in the context of the merger C&W was able to extract conditions from NTL which would not otherwise seem attractive to NTL on a stand-alone basis. If the parties were found to have market power in any of the services covered (or indeed, if C&W were likely to develop market power within the life of the agreement) then the agreement could have the effect of foreclosing the market to other competitors.

The cumulative effect on business telecommunication markets

5.32. While the separate concerns could be considered individually, OFTEL said that it may also be appropriate to consider their cumulative effect in business telecommunication markets. Market definition in this area was not straightforward, given the diverse and changing nature of product and service offerings, patterns of demand, and pace of technological change. However, it was highly doubtful that conventional supply- and demand-side analysis would lead to the conclusion that there was a single national business telecommunication market. Therefore, market share calculations based on highly aggregated data needed to be treated with caution (as, indeed, did volume measures which might mask very different revenue shares).

5.33. Were the parties proposing a full merger of their operations in business markets, it would be appropriate to compare the effect of the merger with the situation where the parties remained independent. The effect would appear to be the loss of an effective, or potentially effective, competitor. It might be argued that NTL's present share of the business market was currently small. However, in the context of a transition from monopoly through duopoly towards effective self-sustaining competition, one would expect the present share of new entrants to be small relative to established incumbents.

5.34. Moreover, market share data were of limited value for the purposes of competition analysis unless they related to well-defined economic markets. It was open to question whether it was realistic to speak of a single business telecommunication market. In a changing market, OFTEL did not have any predetermined view on where product market boundaries lay. It was by no means clear that the range of products and services falling under such a heading represented effective substitutes, or that they were sufficiently linked by a chain of substitution for them to be considered as forming a single market. Without an assessment as to where product market boundaries might lie, and the extent of effective competition in individual markets/segments, there was insufficient basis to conclude that coordinated behaviour between NTL and C&W would not have adverse effects on competition.

5.35. Competition between network operators and BT tended to be confined to a handful of serious players, all of whom were to some extent interdependent already. Coordination between the parties could have an effect similar to that of reducing the number of effective or potentially effective competitors, so the potential for a material effect on competition could not be ruled out. On the other hand, OFTEL was not convinced that the cross-shareholdings and other agreements which gave rise to such concerns were an intrinsic part of the acquisition by NTL of CWC's local cable franchises.

5.36. OFTEL believed that any problems arising from the cross-shareholding should not prove insuperable, as structural remedies were clearly available if needed. Subsequently, OFTEL considered briefly the Heads of Agreement as amended on 9 February 2000 and notified to the Commission. OFTEL considered these arrangements to be distinct from the structural elements of the merger and, in view of the potential concerns, believed the possibility of further scrutiny by OFTEL and/or the OFT should not be excluded under the Competition Act 1998 or the Telecommunications Act 1984.

Views of broadcasters

British Broadcasting Corporation

5.37. The British Broadcasting Corporation (BBC) said that the UK cable TV market had evolved slowly since the mid-1980s, from being a highly fragmented market with a large number of very small and insufficiently resourced franchise monopolists, to being an increasingly consolidated market comprising well-resourced operators that held multiple, and usually contiguous, franchises across the UK. Increasingly, major international communication companies were acquiring ownership stakes in UK cable operators. Recent examples included the acquisition of 28 per cent of Telewest by Microsoft (also owner of 3 per cent of NTL) and the acquisition of a total of 24 per cent of NTL by France Telecom.

5.38. There were now only three major operators (treating CWC and NTL as distinct companies for now) that had franchise coverage across large parts of the UK, with a small number of operators who had a more local presence. Of almost 3 million subscribers to cable TV, CWC and NTL respectively accounted for some 29 and 33 per cent, Telewest (including Cable London) for a further 37 per cent, and two other operators for 2 per cent. There were four other franchisees, but they currently had no cable operations.

5.39. The BBC told us it was 'platform neutral' and so provided its own services on all platforms wherever practicable. It believed that the public interest was best served by strong competition and that a competitive market would exert pressure on prices and quality of service, thereby speeding up the penetration of digital services.

The relevant markets and competition

5.40. NTL/CWC competed in two markets:

(a) the provision of telephony and, increasingly, broadband interactive services; and

(b) the retail of multi-channel pay-TV.

The BBC said that, in telephony, the merged NTL/CWC entity would remain a small player relative to BT; but the merged entity's ability to benefit from greater economies of scale could be expected to enhance competition with BT. Nor would the merged entity be in a dominant position in the provision of broadband interactive services. BT had already begun to roll out DSL services which enabled broadband services to be delivered over the existing local telecommunications infrastructure, and had announced its intention to reach around a quarter of UK homes with DSL by March 2000. OFTEL had also opened up DSL over BT's network to wider competition from 2001.

5.41. The BBC said that in multi-channel pay-TV, competition in any given franchise area was not primarily with other cable companies but with other multi-channel platform providers; notably BSkyB on analogue and digital satellite and ONdigital on DTT. Different prices and services offered by different cable companies in each franchise area had provided a useful benchmark for consumers and promoted a small measure of innovation, but any benchmark effect was insignificant given that platform competition operated within a franchise area.

5.42. BSkyB was, by a considerable distance, the largest player among the platform competitors. It directly retailed pay-TV to 51 per cent of multi-channel homes (3.6 million). By contrast, ONdigital's most recent figures gave them a 5.5 per cent share with 0.4 million homes. The combined NTL/CWC entity would have a 26 per cent share with 1.8 million homes. These share figures, however, understated the strength of BSkyB's position:

(a) BSkyB was the major wholesaler of premium pay-TV channels to both the cable and terrestrial pay platforms.

(b) BSkyB currently held the rights to major sporting events, which were themselves key drivers of premium pay-TV.

(c) The digital satellite platform operated by BSkyB already contained over 100 TV channels, over 80 NVOD channels, over 60 audio channels and interactive services, including the TV-based joint venture e-commerce service, Open.

5.43. Terrestrial spectrum capacity constraints meant that ONdigital's platform could not provide more than a fraction of this offering. Only broadband digital cable was likely to be able to provide competition across this wide field.

5.44. The BBC therefore believed that, subject to one concern set out below, the proposed merger between NTL and CWC was likely to enhance competition and consumer benefits, by providing more effective competition to BSkyB.

The public interest and free-to-air channels

5.45. The BBC said that previous investigations by the OFT and the European Commission had concluded that pay-TV and free-to-air TV were separate but related markets. On the cable platform the interrelation between these two markets was closer than on other platforms. This was because cable was a closed platform, ie the cable operator controlled the encoding equipment, the delivery infrastructure, and the consumer's decoding equipment. Free-to-air channels did not have access, as of right, to the viewer on the cable platform as they did on the digital terrestrial or digital satellite platforms. This was particularly important to the BBC whose public service free-to-air channels were universally paid for, through the licence fee, and which should thus be universally available at no additional change to the licence payer.

5.46. As the cable industry consolidated there was a reduction in benchmark competition and there was a greater risk that one single operator could prevent access by a significant number of licence payers to the BBC's public services, or seek to charge licence payers (or the BBC itself) additional sums for access. Although digital cable networks had much greater capacity than that of analogue networks, the commercial imperative to maximize revenue per channel (for example, by increasing NVOD or PPV) would continue to put pressure on the space made available for public service channels.

5.47. Section 91 of the Broadcasting Act 1996 would, if activated, impose a 'must carry' requirement on digital cable for the BBC's public service channels and those of ITV, Channel 4 and Channel 5. Activation could be triggered by the ITC when it was satisfied that the current or proposed roll-out of digital in the service was sufficient to classify it as a digital local delivery service. However, it was far from clear that section 91 stipulated that the cable company was disbarred from charging its viewers additional sums for the privilege of receiving those channels (for example, by limiting them to the higher-cost premium tier of services).

5.48. As a public interest safeguard, the BBC therefore suggested undertakings from the cable operators to provide access to the full range of licence-fee-funded BBC public service channels. Such a recommendation would provide certainty for cable viewers that they would continue to be able to view all licence-fee-funded channels and that they would not face any charge, additional to the licence fee they had already paid, to view them. The BBC believed that this would be in the public interest and that it would not damage NTL or CWC. Both NTL and CWC had rolling, short-term agreements in place with the BBC, whereby the BBC delivered the signal for its public service TV channels to the cable companies at no charge to them. The cable companies then relayed these channels to all their viewers at no additional charge to the viewer or the BBC. Since the companies had voluntarily chosen to make these services available, the BBC believed the extra security for the public of guaranteeing that availability would not present difficulties for the companies.

British Sky Broadcasting Group plc

5.49. BSkyB argued that the main implications of the merger arose through the cable operators' control at retail level of a closed network which enabled them to deny access or make access subject to unreasonable terms both to their suppliers and to their competitors. Whereas BSkyB had never been dominant at the retail level, the cable operators had considerable power in local markets. The distortions which flowed from their role as gatekeepers to closed cable networks also impacted the power they could deploy in negotiating the purchases of programme rights, and in offering customers high-speed Internet access and interactive TV services. The merger would compound this market power and the structural and cost advantage which underlay the ability of the cable companies to distort competition at a critical stage in the development of the UK's information-based economy, and should not be allowed to proceed while cable operators continued to distort those markets and damage competitors in this way.

The scope of the proposed merged entity

5.50. BSkyB submitted that the acquisition by NTL of CWC ConsumerCo would greatly increase NTL's customer base. According to an NTL/CWC press release, CWC ConsumerCo included approximately 1.2 million residential customers, 29,000 business customers and cable networks in the cities of London, Manchester and Leeds, among others. On current figures, total customers of the merged entity would exceed 2.8 million residential customers and 60,000 business customers. NTL's franchises would extend to over 12 million homes in the UK and Ireland, and at present the combined group passed almost 8 million homes with high-speed, high-capacity two-way communication networks that were capable of delivering video entertainment, telephony, Internet and interactive services. The Chief Executive of NTL had stated that the three cable companies combined had a market capitalization two to two and a half times the market capitalization of BSkyB. The merged entity would undoubtedly have a substantial financial presence.

5.51. Each of the major shareholders in the merged entity was extremely significant in the broad global communication market. The size of these shareholders and the market capitalization of the cable companies confirmed the very firmly entrenched expectations of future success and profitability for the merged cable companies. The significance in particular of Microsoft's stake in NTL had been acknowledged by NTL (press release of 25 January 1999). Further consolidation might be likely because Microsoft had stakes in both Telewest and NTL.

5.52. NTL owned Premium TV Limited through which NTL acquired 6.3 per cent of the share capital of Newcastle United Football Club (subsequently increased to 9.9 per cent, and NTL had subsequently taken a similar interest in Aston Villa). NTL decided not to proceed with the acquisition of control of Newcastle United but had stated that it remained committed, through the activities of Premium TV, to widening choice and diversity of sports programming. NTL had confirmed that it was acquiring sports and film rights directly for itself. It also had a 50 per cent stake in Front Row, the PPV service which was offered over NTL's and Telewest's networks.

5.53. NTL had an interest in DTT. It had a 33.3 per cent stake in SDN and two directors. SDN had been awarded the licence for DTT multiplex A which had the best coverage after the multiplexes awarded to the BBC and ITV. SDN and ONdigital had formed a joint venture which was likely to launch PPV services early in 2000. NTL had also built and would operate the DTT transmission system for Multiplexes 2 and A.

5.54. In addition to its TV activities, NTL offered business and residential telecommunication services, national and international carrier telecommunication services, radio communications and satellite services. NTL had a substantial presence in respect of Internet services. As a result of the proposed merger, NTL would acquire CWC's 50.1 per cent stake in Two-Way TV which would strengthen its role in interactive services. Further examples of the extensive scope of NTL's communications activities were: access to digital radio through its stake in Digital one; uplinking for eight of the nine multiplexes on Astra 2A; analogue transmission contracts with the ITV companies and Channel 4; development for the ITC of an implementation plan for the transition to DTT from analogue; the contract to deliver Front Row to cable networks; and mobile phone transmission services for Orange and Vodafone. By virtue of this extensive range of activities, NTL would be uniquely able to bundle a range of communication services together.

The market power of the proposed merged entity

5.55. BSkyB noted that the OFT had, in the past, proceeded upon the assumption that a market existed for pay-TV services which was separate from the supply of free TV. BSkyB contested this assumed product market. In the past, BSkyB had consistently argued that the pricing of pay-TV services was effectively constrained by the availability of free-to-air services. The ITC and others had argued against the introduction of the proposed BBC digital licence fee on the same basis. The Restrictive Practices Court in its July 1999 judgment had stated that it found BSkyB's arguments that there was no discrete pay-TV market to be exceedingly cogent. Nevertheless, solely for the purpose of submitting representations on this merger, BSkyB's position was that, if the UK regulators in general continued to assume the existence of a separate pay-TV market when regulating BSkyB, the same assumption should carry across to the assessment of other parties, such as this merger between NTL and CWC ConsumerCo.

5.56. Having identified pay-TV as a relevant product, a key issue to consider was whether the cable operators enjoyed market power in respect of pay-TV and whether the proposed merger could leverage that market power or otherwise lead to distortions of competition. The next question to address was whether the pricing behaviour of cable operators was constrained by other suppliers. This was important because, the OFT having apparently excluded free-to-air TV, the only potential sources of constraint on the retail pricing activities of a cable operator were other suppliers of pay-TV services. BSkyB believed that cable operators faced competition from DTH and DTT, but that the effectiveness of this competition was clearly limited.

5.57. For some homes, there was no effective choice between TV distribution platforms. However, this was not relevant to an assessment of market power because issues of demand substitution depended on the willingness of the marginal customer to switch. The majority of homes did consider supply by the different platforms to be effective substitutes.

5.58. There was evidence to suggest that cable operators' prices were not effectively constrained by DTH and DTT. The reason for this was that cable operators enjoyed economies of scope denied to DTH and DTT which enabled them to deliver a range of TV and telephony services at a cost which was less than the combined cost of delivering the services individually. Because cable operators enjoyed exclusive franchises, they were the only suppliers that enjoyed this cost advantage. There was considerable anecdotal evidence to suggest that this cost advantage was material. Cable operators had been known to boast publicly of the high margins and cost advantages they enjoyed in respect of both TV and telephony services. On the assumption that the claims of the cable operators were true, it would appear that even though cable pricing was currently pitched at a level which was more attractive than that offered by BSkyB and BT, cable operators were still able to earn significant profits. BSkyB concluded that cable operators enjoyed market power in retail pay-TV and the delivery of bundled TV and telephony services.

Eradication of competition in cable areas

5.59. It was, BSkyB argued, of fundamental importance to have regard to the dynamics operating in the market for pay-TV services and not to restrict analysis to a static view of that market. Seen in that perspective, cable operators enjoyed market power against which retail competition from other TV platforms provided only a limited counterweight. [

Details omitted. See note on page iv.

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5.60. [

Details omitted. See note on page iv.

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[

Details omitted. See note on page iv.

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Relevance of cable profitability

5.61. BSkyB noted that, in the past, cable operators and regulators had referred to their 'limited profitability' with the implication that cable operators did not, therefore, possess market power. This was an inappropriate description as current profits or losses reflected a mixture of ongoing network investment combined with customers in respect of which cable operators enjoyed significant margins. The market value of the cable operators indicated that there was considerable potential for them to earn very significant profits in the future when the investment phase of their business was behind them. For the week ended 20 May 1999, the market capitalizations were £9.96 billion for CWC, £6.21 billion for Telewest and $6.93 billion for NTL. The current and past losses needed to be seen as an investment which would lead to significant profits in the future. Thus a claim that a sole cable operator enjoyed market power was not inconsistent with that cable operator recording current losses.

5.62. OFTEL and the ITC had, in the past, also stated that 'there is no evidence of cable operators earning excessive levels of profit—in fact the opposite is the case'. This was an entirely inappropriate line of reasoning because, as the OFT had indicated, issues of excess profits were more complex than a straightforward examination of current annual profit enjoyed by a firm (especially during a period of investment) and must take account of expectations of future profit streams.

5.63. In 1996, the OFT had acknowledged that BSkyB had made very significant past losses in reaching its market position and that these had not yet been recovered. But the OFT also noted that BSkyB had moved into annual profit and that its market value indicated an expectation of further profits. The OFT combined this information in a complex analysis to assess whether BSkyB was earning 'excess profits' or enjoyed market power and thus was able to maintain price above the competition level. BSkyB had expressed a number of concerns about the OFT analysis. As this analysis was the principal basis for the OFT's conclusion that BSkyB enjoyed market power, it seemed only proper that the same test should be applied to the cable operators.

5.64. A rough analysis of Telewest undertaken by BSkyB using publicly available data (and taking into account its past losses and current market value) suggested an internal rate of return in excess of 30 per cent. This was considerably greater than the OFT had found in 1996 when it had concluded that BSkyB enjoyed market power.

Conclusion on market power

5.65. Overall, therefore, the evidence first of cable's unique ability to benefit from its economies of scope and [*Details omitted. See note on page iv.*] led to the conclusion that cable operators possessed market power. Although there was no direct competition between the two operators, and any indirect competition between them had provided only a very weak constraint on their activities, the merger between NTL and CWC ConsumerCo would compound this market power and the existing ability of cable operators to distort competition in a number of ways in respect of pay-TV services.

The anti-competitive nature of cable consolidation

5.66. The general argument that the cable industry had used to justify consolidation was that it would create a more effective competitor for both BT and BSkyB and was therefore pro-competitive. Upon examination, there was very little substance to this claim. BSkyB submitted, however, that NTL needed no boost at this time to compete with either BSkyB or BT; both its performance and a number of its recent statements demonstrated this.

5.67. [*Details omitted. See note on page iv.*]

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Details omitted. See note on page iv.

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5.68. The parties might claim that the merger would improve their ability to compete with BSkyB in bidding for programming rights. But here again cable operators were perfectly able to compete for rights at the present time. Their modest presence as providers of programming was attributable to their choosing to concentrate their efforts elsewhere and did not indicate any barriers to competition against them. On the contrary, the fact that cable operators enjoyed closed networks gave them a positive advantage in bidding for programming rights. Because cable operators could exclude other channel providers from their networks and because the DTH network was open, cable operators were the only bidders able to bid on the assurance of access to all pay-TV households. (NTL also had guaranteed access to DTT homes through its shareholding in SDN.) [

Details omitted. See note on page iv.

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5.69. NTL had claimed that the merger would improve the bargaining position of the cable industry when dealing with BSkyB for BSkyB's premium channels. Even if this were true, it was not clear that there would be any public benefit. The most likely effect of an increase in bargaining power would be a simple transfer of revenue from BSkyB to the cable industry. While this might be good news for cable shareholders, there was no guarantee that consumers would benefit at all.

5.70. But there would be a much greater concern if the NTL bargaining power were to increase in this area. If the bargaining position of the cable industry improved against BSkyB as a result of the merger, then it would also improve against all other channel providers seeking carriage on cable networks. What 'improved bargaining position' meant in effect was that cable operators had a more credible basis for threatening, in negotiations, to refuse to carry a channel at all and it would be even less credible for broadcasters to refuse to accept low wholesale prices if they would lose distribution to 25 per cent of multi-channel homes: hence BSkyB believed the market power of cable operators would increase as a result of the merger. Improved bargaining power for cable operators would see greater pressure on small channel providers and lower rates of carriage across the industry, with a likely reduction in the number of channels able to survive, more channels excluded from cable carriage and a lower incentive to invest in new channels. All of this was contrary to the interests of consumers in general and not only to BSkyB. BSkyB was fundamentally a supporter of multi-channel broadcasting, whether by it or by third parties. If there was a reduction in the available diversity of channels, the whole pay-TV industry, including BSkyB, would suffer.

5.71. In respect of telephony, the parties were likely to claim that the merger would create a stronger competitor to BT. For this to be true the merger would have to deliver some form of cost savings or synergy which would lower the marginal cost of the merged entity. A lower marginal cost would allow the merged entity to price lower and place greater competitive pressure on BT. But there were three key flaws in this argument:

(a) There seemed to be no avenue for marginal costs to be lowered by the merger. Savings on fixed costs would have no effect on competition as they had no impact on the profit-maximizing price for a firm. Only changes in marginal costs could lead to greater price competition.

(b) Even if marginal costs were to be lowered by the merger, there was no evidence that this would translate into lower prices. The cable operators generally claimed margins of more than 70 per cent on their telephony services and this suggested very little relationship between marginal costs and prices. So there was no guarantee that a reduction in marginal costs would translate into lower prices.

(c) It was very common for firms ranked two and three or three and four in an industry to claim, when seeking to merge, that this would allow them to become a stronger force in the market and compete more effectively with the number one firm. Those claims were normally given short shrift by merger control authorities for the very good reason that standard economic theory predicted exactly the opposite of this claim. The standard economic theory that underpinned merger control was that industries that became more concentrated tended to become less competitive as collusion (either overt or tacit) became easier. A well-supported rationale would need to be presented for the conclusion that more concentration in the provision of residential telephony services (and exchange lines) would provide an incentive to compete more vigorously rather than seek to collude.

5.72. In conclusion, there appeared to be no economies which resulted from the merger in respect of which it could legitimately be argued that the merger would result in more effective competition.

5.73. The concerns expressed over the potential for consolidation of cable operators and their multiple systems to undermine the position of programme providers were echoed in US regulation. In the USA the Federal Communications Commission (FCC) had sought to restrict the degree of horizontal concentration in the cable industry by limiting the number of homes passed nationwide that any one multiple system operator could reach through cable systems in which that operator had an attributable interest (although for legal reasons it had been unable to enforce its policy). The FCC imposed a subscriber limit of 30 per cent (with the caveat that the share could reach 35 per cent of homes passed nationwide, provided that the additional systems were minority controlled). In a number of cases, local government used the opportunity of mergers to require the provision of open access (and other states were introducing or considering open access legislation).

The nature of cable's closed network

5.74. Cable operators had substantial monopsony power. In respect of the DTH platform, channel providers had the option of going direct to viewers or alternatively to have their channels retailed by BSkyB. BSkyB was required to offer conditional access services and access control services to third parties on fair, reasonable and non-discriminatory terms. These regulatory arrangements prevented BSkyB from being able to abuse any position in terms of operating a gateway to DTH, but were, as BSkyB put it, in 'stark contrast' to the situation on cable networks, where the cable operators were not presently obliged to offer third parties access services. Accordingly channel providers who wanted their services distributed over cable networks did not have the option of retailing their services directly to cable customers. They were dependent upon reaching wholesale commercial agreements with cable operators for the distribution of their channels. In practice, this meant that the cable operators were monopoly retailers of pay-TV (and telephony) services over their networks. The fact that the cable networks were closed and that broadcasters could get distribution to cable homes only by supplying their services wholesale to the cable operator of itself gave each cable operator substantial market power and reinforced the market power which cable operators already enjoyed as a result of their unique cost and structural advantages.

5.75. When a broadcaster (as a content provider) offered its channel to a cable operator, it had to negotiate a carriage fee with the operator. In these negotiations the cable operator would typically be in a much stronger bargaining position than the broadcaster. This was because, from the perspective of the broadcaster, it would normally not be credible to refuse to provide the channel if the cable operator was unwilling to agree to a certain wholesale price. The broadcaster's costs were mostly fixed and it had an incentive, once the fixed costs had been sunk, to have its product distributed as widely as possible, even at very low wholesale prices. From the cable operator's perspective it was much more credible to bargain hard and commit only to low wholesale prices. This was because the percentage of its total revenue that a cable operator risked losing if a particular service was not distributed over its platform was normally very low.

5.76. Consolidation in the cable industry would further strengthen this aspect of the bargaining power of cable operators, to the detriment of content providers. Currently the latter, if they failed to reach a carriage agreement with NTL or CWC individually, risked losing distribution to 12 or 13 per cent of total UK multi-channel homes if they did not accept the terms offered by either of these cable operators. If this merger were completed, broadcasters that were unwilling to accept the wholesale prices offered by NTL would lose distribution to 25 per cent of all multi-channel homes. Following the merger, therefore, it

would be even less credible for broadcasters to refuse to accept low wholesale prices, particularly because broadcasters whose services were only available to 75 per cent of multi-channel homes might not be able to compete with rival services that had 100 per cent distribution though being able to use cable and the open satellite systems. This would put even more downward pressure on the prices that broadcasters could expect to receive from cable operators, which might have serious long-term consequences. In BSkyB's view it could jeopardize at the outset the successful launch of digital technology. If the cable operators squeezed the margins earned by broadcasters they would undermine the incentive to invest in new products and innovative services. If this occurred the potential for proliferation of channels and other services, made possible by the introduction of digital technology, would be stifled.

5.77. BSkyB recognized that it might be thought that a reduction in the wholesale price of pay-TV channels would be a good thing in itself, but it argued that any gains from lower wholesale prices could only be relevant as long as competition between pay-TV retailers was such as to ensure that the gains were, and would continue to be, passed on to consumers. If there were an elimination of competition then the benefits would rest with the shareholders of cable companies and would not be enjoyed by consumers. The fact that NTL already had in excess of [✂] per cent of multi-channel homes in its franchise areas suggested that it was extremely unlikely that any further reductions in the wholesale price of channels, or other digital services, would be passed on to subscribers. (For example, there was no evidence to suggest that the inclusion of BBC News 24 (a channel which is provided free at wholesale level) instead of Sky News (which relies on a wholesale fee) had resulted in a reduction in the price charged to customers for cable pay-TV services.)

5.78. The market power of cable operators could be deployed in a similar way in the provision by cable operators of services, such as the new digital interactive TV services. The issues centred on the power of the cable operators to impede access by third party broadcasters of interactive services who would be competing with a cable operator's own provider of interactive services. OFTEL had been concerned to ensure that such third party broadcasters were not unfairly hindered from entering the market. Exactly the same issue would arise for Internet access, since only the cable operators' Internet provider of choice could be accessed via the cable and it would therefore be open to the cable operator to offer higher-speed access (as part of a 'bundled service' offering) to those subscribers opting for its own ISP, while requiring call charges to be paid by customers accessing other ISPs who would rely on the telephony network and not on the cable system. The closed cable network, combined with bundling practices, would therefore lead to distortions of competition. Cable consolidation would lead to an even greater distortion of competition, because the extent of disadvantage faced by ISPs that have to compete against cable-owned services would be increased.

5.79. BSkyB provided some specific examples of actual abuse by cable operators and the potential for abuse of their market power. One example was the treatment of Sky News. In June 1997, before the launch of BBC News 24, there were 2 million broadband cable subscribers in total, of which 91 per cent were authorized by their local cable operator to receive Sky News. The wholesale rate at that time for Sky News was approximately [✂]p per subscriber. BSkyB's annual income in respect of cable carriage of Sky News amounted approximately to £[✂] million. The launch of BBC News 24 in November 1997, which continued to be provided free of charge to cable operators by the BBC, resulted in a large proportion of the cable industry serving notice on BSkyB of its intention to drop Sky News on 60 days' notice. [

Details omitted. See note on page iv.

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5.80. A second example of the ability of cable operators to abuse their market power due to the closed nature of their networks was provided by Zee TV. Zee TV had been ejected from the cable platform of distribution as the result of an agreement with Sony concerning PPV rights. The ITC had criticized this outcome. Similar treatment could not, however, have arisen on the DTH platform where Zee TV was able to retail itself on its own account and had availed itself of that access right. Nevertheless the fact that Zee TV was now being denied access to a substantial number of cable homes, whereas its principal competitor, Sony's ethnic channel SET, had exclusive access to these homes, would be likely to have a material impact on the finances and future viability of this channel.

5.81. A third example of distortion of competition arose in respect of PPV services. At the time of writing the BSkyB submission, only NTL and Telewest distributed the PPV services of Front Row, which they jointly owned following the acquisition of General Cable by Telewest. These cable operators

currently refused to make competing PPV services, such as Sky Box Office, available to their viewers. In contrast, CWC currently offered the services of Sky Box Office to its viewers. [*Details omitted. See note on page iv.*] [*Details omitted. See note on page iv.*] If Front Row chose to launch its services on satellite, it would have access to 100 per cent of multi-channel homes and [*Details omitted. See note on page iv.*].

5.82. [*Details omitted. See note on page iv.*]

5.83. The cable operators' ability to deny access to third party services could be expected to result in distortions to competition in the acquisition of programming rights. Bidding for rights was influenced by the expected number of viewers who would pay to view the relevant programmes. The operators of closed networks were therefore advantaged in any competitive bid for rights. Competitive distortions would become more acute if more and more closed networks fell under the control of a single operator. Moreover, whereas BSkyB supplied its content to all platforms, the cable companies adopted a policy of reserving channels exclusively for cable exploitation.

5.84. In the view of BSkyB, cable operators (and particularly NTL) had demonstrated little interest in marketing and retailing TV services to customers, and in particular premium programmes. The cable industry had a preoccupation with telephony and had regarded multi-channel TV as a secondary, not a core, business. In the case of premium channels, this lack of interest in pay-TV was demonstrated by the consistently poor 'pay-to-basic ratio' (ie the ratio of premium channels subscribed to in proportion to the total number of cable TV subscribers) performance of cable operators in comparison with BSkyB's performance in respect of DTH subscribers. The pay-to-basic ratio was in essence a measure of how effectively a distributor was marketing premium channels to those subscribers who had elected to take TV services from that distributor. As at 1 April 1999, the average pay-to-basic ratio for the cable industry was 129 per cent. This compared with a ratio of [✂] per cent for BSkyB's subscribers.

5.85. The fact that the cable industry had focused on telephony to the detriment of pay-TV could also be shown by a consideration of the number of premium pay-TV units in cable active and non-cabled areas. In areas that were cabled, the number of premium units (including DTH and cable subscribers) sold per home passed was [✂]; in areas not cabled, the level of penetration of premium pay-TV channels was higher at [✂]. If cable operators were truly interested in retailing Sky's pay-TV channels, it should be expected that the presence of two competing platforms in cable areas would lead to a significantly greater degree of channel penetration. While cable had undoubtedly added some homes, the benefit from this had been exceeded by the extent to which cable had taken customers from DTH and then overseen a deterioration of those customers.

5.86. Cable operations therefore had a negative effect on the penetration of premium channel TV. BSkyB had performed marketing projects in the past with cable operators which had achieved impressive results and showed that additional marketing efforts by the cable companies would increase sales of premium channels. Among the three major cable operators, NTL had been worst in encouraging take-up of premium channels and CWC had been the best. BSkyB was concerned that the proposed merger would see a further hardening of attitudes against distribution of TV, particularly premium TV, [*Details*

omitted. See note on page iv.]. Again, the solution was for the cable networks to be opened up, which would allow BSkyB to market its own services and sell many more premium channels to the same base of homes.

Further reduction in retail competition

5.87. In BSkyB's view, the appropriate analysis of each cable operator's market position must be in respect of the geographic areas in which it operated. However, all the cable operators had taken the view (in response to the ITC/OFTEL joint consultation on the effects of the bundling of TV and telephony on pay-TV) that the relevant geographic market for pay-TV services was national. They also stated that rival platforms operated national pricing strategies. If that were true, it followed that cable operators in different franchise areas would act as an indirect constraint on one another's prices (for example, if one cable operator reduced its prices, BSkyB may have to follow, putting pressure on the prices of the other cable operators), and therefore that the merger, by reducing the number of cable companies by one, was potentially anti-competitive.

5.88. The merger would remove potential competition between NTL and CWC. As exclusive franchises were being phased out, the possibility existed for NTL and CWC to compete in telephony and other services. In certain parts of the country, it might be economic for a cable operator to overbuild its network into adjacent franchises.

5.89. NTL had been particularly successful in exploiting the practice of bundling TV and telephony services. No doubt the bundling of services permitted cable operators to exploit their economies of scope but the efficiency gains in terms of lower costs were only acceptable if they were passed on to consumers. The merger with CWC would compound the problem of the imbalance between the gains to the cable operators and the benefits to consumers.

5.90. OFTEL had concluded that BT should be required to permit access to its local loop by July 2001. However, this did not mean that cable consolidation did not give rise to competition concerns. The kind of benefit which could be realized by cable operators through cable consolidation would not be replicated by operators which relied on the alternative ADSL technology. ADSL would be a regionally-based service and was likely to be rolled out only in urban areas with a high population density. [*Details omitted. See note on page iv.*] Even if these points about ADSL were discounted, the cable operators would have a two-year head start.

BSkyB's proposed stake in ONdigital

5.91. BSkyB outlined the history of its having been required to abandon its stake in ONdigital in 1997. It considered that consistency of treatment should be applied in relation to NTL. The rationale for the opposition to BSkyB's 33.3 per cent stake in ONdigital (which was that no one company should have a significant stake in two distribution platforms) applied equally to NTL's 33.3 per cent stake in SDN. The proposed merger would result in NTL controlling over 60 per cent of cable homes and 33.3 per cent of SDN. Given the open nature of the satellite platform and the closed nature of cable, it was illogical that BSkyB was not permitted to have an interest in DTT, while NTL was allowed such an interest. In BSkyB's view, NTL should be required as a condition of the merger proceeding to divest its stake in SDN.

BSkyB comments on the ITC submission

5.92. BSkyB also provided us with some comments on the ITC's published submission to the Commission. BSkyB said that the ITC seemed to have considered this merger only in the narrow context of broadcasting services, although its responsibilities may extend somewhat wider than it suggested. The ITC therefore only identified two relevant issues: the retail market for pay-TV services; and the market for programme rights. It had not considered factors such as the issue of access to cable networks;

discrimination by cable operators against third party services; cable's general disinterest in promoting third party TV services; cable's preferential treatment of TV services in which it had an equity stake; an exacerbation of the adverse effect of bundling TV and telephony services on competition in the retailing of pay-TV services; gateway control of high-speed Internet access; gateway control of interactive services (e-commerce); and the holding of stakes in the two closed TV platforms, DTT and cable.

5.93. Secondly, the ITC had failed to apply the provisions of its own code on defining geographical markets (as the ITC expressly acknowledged): namely that the key aim should be to identify an area just big enough to embrace only those services which represent a competitive constraint on the behaviour of a hypothetical monopolist. On the basis that NTL and CWC operated in different geographical markets, their shares of pay-TV subscribers must be calculated individually for their respective geographic markets. At present, NTL had a share of [✂] per cent of pay-TV homes in the geographic area in which it was active and CWC had a share of [✂] per cent. [*Details omitted. See note on page iv.*] The ITC previously acknowledged that a firm with a persistently high market share relative to its competitors, and one which was increasing over time, may be considered to have market power. The ITC had acknowledged such dominance in respect of the cable operators, for example, in evidence to the Commission's report on BSkyB's proposed acquisition of Manchester United.

5.94. Thirdly, whilst acknowledging that, even absent the merger, NTL and CWC would be unlikely to over-build into each other's franchises, the ITC still asserted that other entrants would be willing to over-build or make the necessary capital investment. However, the most obvious potential entrants were the cable operators: it was not credible for the ITC to claim that the cable operators would not over-build but that other new entrants would. The ITC also overstated the possibility of new entry by telecommunications operators. The ITC claimed that BT's roll-out of DSL technology would create competition in the retailing of pay-TV services, yet it did not claim that BT's network would be used to provide these services. [

Details omitted. See note on page iv.

] Finally in connection with potential competition, the ITC referred to OFTEL's consultation on open access to cable networks. The mere fact that OFTEL had indicated that it would look at the question of open access did not, in and of itself, imply that retail competition would increase.

5.95. Fourthly, the ITC offered no evidence in support of its assertion that the key drivers of pay-TV in the UK were films and sport. This assertion was plainly wrong: the biggest driver of pay-TV services was cable's unique ability to bundle the services with telephony. The relatively low level of penetration of premium channels in cable homes clearly indicated that films and sport did not drive the take-up of pay-TV. While the ITC asserted that it was keen to see the development of greater competition in the market for acquiring broadcasting rights, it did not demonstrate any lack of competition currently for those rights. That there was already fierce competition for rights was demonstrated by the significantly escalating costs of rights over the last few years. The reason why the cable operators had not, to date, had a substantial presence in programming was because they had previously focused on building their networks and selling high-margin telephony services. As the build phase had ended, the cable operators had demonstrated a greater inclination to involve themselves in programming. There was absolutely no evidence that the cable operators considered themselves to be too small to bid for rights and that the merger would enable NTL to overcome this hurdle. Furthermore, the ITC seemed to imply that only other pay-TV operators competed with BSkyB for exclusive programming rights: free-to-air channels had also successfully done so.

5.96. BSkyB considered that the ITC's claim that a buyer's ability to bid for exclusive rights was linked to its subscriber base was partly correct. The ITC should, however, have regard to the total number of households which could be accessed by a particular buyer of rights. The ITC had overlooked the fact that cable operators could access DTH households directly without needing to be included as part of BSkyB's retail offering.

5.97. The ITC also thought that the merger would be beneficial because the merged entity would have greater bargaining power when negotiating with channel providers for wholesale supply of channels. Whilst the ITC may consider that it would be desirable if NTL had greater bargaining power when negotiating with BSkyB for provision of its channels, the ITC has apparently ignored the fact that the 'new NTL' would also have increased buyer power when negotiating with other channel providers, and in particular small channel providers.

Conclusion on the effects of the merger

5.98. BSkyB therefore concluded that:

(a) The proposed merger raised several competition concerns and might be expected to operate against the public interest. Cable operators enjoyed substantial market power in the retailing of TV services. The proposed merger would compound this market power and the existing ability of cable operators to distort competition in respect of TV services.

(b) No economies resulted from the proposed merger which could substantiate the claim that the merged entity would be a more effective competitor either to BT or to BSkyB. Cable was already more than an effective competitor in the retailing of TV services [*Details omitted. See note on page iv.*]. BSkyB's concerns about the influence that a consolidated cable industry might be able to exert over broadcasters and the scope for consolidation to undermine the position of content providers had been endorsed by the US FCC.

(c) Cable currently ran a closed network. Accordingly, it had substantial monopsony power. This closed nature of the cable networks enabled cable operators to squeeze broadcasters' margins and permitted them to discriminate against third party broadcasters. Evidence of this had arisen in respect of Sky News, Zee TV, Sky Box Office, Open, and others. The closed nature of the cable networks would lead to distortions in competition for broadcasting rights and high-speed Internet access over the cable networks. These distortions of competition would be exacerbated by the proposed merger.

(d) If, as the cable operators suggested, they operated in a national market, they should be regarded as currently competing, albeit indirectly, with each other and the proposed merger would result in a further reduction in retail competition (although BSkyB did not believe this was the case). It would, however, also remove the potential for competition between NTL and CWC and further enable the cable industry to abuse the unfair advantages which resulted from its unique ability to bundle TV with telephony and other services (including high-speed Internet access over the cable broadband network). Currently, ADSL was a poor alternative to cable in respect of delivering broadband services.

(e) In BSkyB's view, the regulators should proscribe the consolidation of the cable platform within a company which owned a stake in the DTT platform in the same way that they proscribed BSkyB's proposed stake in the DTT platform in 1997.

Proposed remedies

5.99. BSkyB therefore submitted that the proposed merger would result in substantial distortions of competition and should not be allowed to proceed. However, if it were allowed to proceed, the following conditions should be attached in order to remedy the adverse effects of the increase in market power that would result from the merger:

(a) NTL must divest its interest in SDN;

(b) NTL must provide open access to its networks in order to enable third parties to retail their services directly to consumers over cable networks;

(c) NTL must offer conditional access and access control services on fair, reasonable and non-discriminatory terms in accordance with the prevailing OFTEL regulations;

(d) NTL must offer access to its EPG on fair, reasonable and non-discriminatory terms in accordance with OFTEL and ITC regulations;

(e) NTL must provide sufficient information to third parties about the technology of its platform to enable those third parties fully to exploit that technology and such information must be made available to third parties at the same time as it was made available to NTL's own retail services; and

(f) the bundling of services by NTL must be addressed in accordance with the submission previously put by BSkyB to OFTEL and the ITC. This submission stated that the ITC and OFTEL should prohibit pure bundling of TV and telephony services by cable operators; impose a positive obligation on cable operators to publicize the availability of their separate services as actively as they publicized any bundled services which may be permitted; and require cable operators to prove that the difference between any bundled service and the sum of the stand-alone prices for pay-TV and telephony did not exceed the lower of the magnitude of the economy of scope of providing the two services together, and the value of the shared costs which were recovered via the charges for the separate services.

5.100. Various parties had argued in favour of the merger on the grounds that competition would be improved. BSkyB submitted that NTL did not itself believe that it needed any boost to compete with either Sky or BT; both its performance and a number of its recent statements demonstrated this.

BSkyB's further submission on the open nature of satellite

5.101. At a later stage in the inquiry, BSkyB made further representations about the openness of the satellite platform. Every channel provider which wished to gain access to the satellite platform had to rent transponder capacity and obtain transmission services, irrespective of whether its channel was retailed by BSkyB or whether it retailed itself independently. The only additional distribution charges which would be incurred directly by a broadcaster if it retailed its services independently on the satellite platform would be the charge for conditional access services, if the channel was to be encrypted, and the charge for EPG services, if the channel wished to have a listing in Sky's EPG. The charges for both of these services were regulated by OFTEL and had to be fair, reasonable and non-discriminatory. Accordingly, these charges could not present a barrier to small channels coming on the platform. The fact that there was no such barrier to entry had been demonstrated, since the launch of digital satellite services on 1 October 1998, by the entry of 31 broadcasters of 52 TV channels, 20 radio channels and 1 portfolio of interactive services on the platform independently of BSkyB. Each of the 73 channels and services which was currently available independently of BSkyB on the satellite platform had obtained a listing on Sky's EPG.

5.102. Independent channels on the satellite platform did not have access to BSkyB's customer base. BSkyB's customer base was one of its key assets and of the utmost commercial confidentiality. Other broadcasters could gain exposure by being available on Sky's EPG and by undertaking their own marketing; u>Direct had done this, for example, and the identity of its customer base was not known to BSkyB. The independent broadcasters on the satellite platform included four of the five most watched channels in the UK (namely BBC1, BBC2, Channel 4 and Channel 5, the ITV companies refusing to make ITV available on digital satellite).

5.103. Potential entrants were not able to retail services over the cable platforms or by using DTT capacity. Cable operators were not required to provide channel providers with access to their networks; and they had an incentive to vertically integrate and to foreclose channels that directly competed with channels which they owned. In the case of DTT, all of the existing commercial multiplex capacity had been allocated to SDN and ONdigital, and therefore other pay-TV broadcasters would not be able to enter on this platform.

5.104. BSkyB went on to submit that by virtue of the closed nature of the cable networks, free-to-air channels, even those on the BBC, were not available independently of a pay-TV subscription on cable networks. In contrast, viewers on the satellite platform could obtain free set-top boxes which had been subsidized by BiB and Sky without the need to subscribe to any pay-TV service. This opportunity was not open to viewers on the DTT platform where set-top boxes, which had been subsidized by ONdigital, were

available only to subscribers to ONdigital. Open's services were available on the digital satellite platform independently of any pay-TV package; households could receive a free subsidized set-top box capable of receiving Open's services without having to take out a pay-TV subscription. The DTH free set-top box offer merely required viewers to sign up to a 12-month contract with MC Co, the subsidiary of BiB which provided its set-top box subsidy, and undertake to keep the set-top box connected to a telephone line for 12 months. The box belonged to the viewer.

5.105. BSkyB noted that Open was seeking carriage on other platforms, and that it was only foreclosure by other platform operators which caused Open to be exclusive to the digital satellite platform.[1]

Carlton Communications Plc

5.106. Carlton told us that it had no objection to the NTL/CWC merger in as much as it involved a merger of two complementary cable platforms, serving customers in separate areas, and in which neither company had secured a dominant position in acquisition of rights.

Channel Four TV Corporation

5.107. Channel Four said that in principle it did not have any major concerns over the merger. However, it was concerned that the NTL platform should provide open access to content providers at reasonable cost. This should extend to the carriage of new TV channels, the ability of a TV channel to carry out interactive commerce on the NTL platform, and access to data and information regarding a channel's viewers or customers.

Flextech Television Limited

5.108. Flextech pointed out that the views expressed here were solely those of Flextech and not Telewest. It told us that it was the largest supplier into the UK market of thematic TV channels, the small niche channels which represented the basic channels provided by most of the platforms. They included a joint venture with the BBC. It had agreed in principle a merger with Telewest, which it saw of value both in the creation of new interactive services, and by combining its interests as a content provider within those of a platform operator, strengthening its position in the market.

5.109. Flextech said that recent consolidation of the UK cable industry had resulted in a very significant change in the market place. Flextech welcomed this consolidation because it had created a number of well-funded competitors to the benefit of the market and consumers. However, consolidation had resulted in a significant shift in power towards the distributor at the expense of the content-providing industry. Increasingly Flextech found itself subject to unreasonable carriage terms which impacted on the commercial interests of its channels and on consumers in terms of the quality and range of services to which they had access. Flextech's negotiating power had been further weakened by the ITC's ruling that there should be no MCRs.

5.110. The proposed merger would create the second largest communications group in the UK after BT. However, unlike BT, which was required to provide open access on fair, reasonable and non-discriminatory terms, NTL would be free to enjoy unfair market power in terms of controlling access to its subscribers for content providers like Flextech. Since, as a result of the merger, NTL would be in a position to withdraw access to two-thirds of the cable market, contract providers such as Flextech would have no alternative but to accept the terms offered.

5.111. Flextech told us during the course of the inquiry that it had agreed carriage terms with NTL on 9 December 1999.

5.112. Flextech said that it was a major stakeholder in the pay-TV sector with over a decade of experience building a business as a provider of programmes to all TV platforms. Through the building of a portfolio of channels and a joint venture with the BBC, it had invested over £100 million in digital TV

[1] At a late stage in the inquiry, BSkyB made comments on the Consumers' Association submission. It also stated that according to press reports ITN would launch a news channel on satellite and was reported as saying that it had no need to negotiate with Sky.

content. Given its dealings with NTL and its concern about the possible abuse of power exercisable by a dominant gatekeeper of a cable system, it had real reservations about any further consolidation of the industry unless there were strict regulatory conditions attached.

5.113. Flextech said that NTL wanted to dominate wherever broadband communications extended. NTL had interests that spanned broadband cable networks, DTT (SDN), terrestrial transmitters and satellite distribution. In addition, NTL had invested heavily in content, the most notable being British Eurosport and Front Row. Undoubtedly a merger with CWC would make NTL a dominant player in the provision of pay-TV services. The merged company would control access to 1.9 million UK homes connected to pay-TV, representing 62 per cent of the cable market (27 per cent of the total pay-TV universe).

5.114. Flextech regarded the merger as an inevitable development, and acknowledged it would improve the position of the merged company in negotiating for broadcasting rights, but did not believe that consumers would necessarily benefit as a result. The merger would, however, give NTL significant market power and effectively create a duopoly in the provision of pay-TV services (enlarged NTL and BSkyB). In order to ensure that NTL did not abuse its dominant position, and to rebalance the negotiating position of content providers relative to the cable operators, content providers should have the alternative of being able to rent capacity, possibly in alliance with other content providers, and access cable subscribers directly. NTL should therefore be required to open its network to allow third party access to competing service providers.

5.115. Flextech said that strict conditions must therefore be attached to counter the enhancement of NTL's bargaining strength that would result from the merger, and preserve the developing competitive market, and address the following specific concerns:

(a) NTL's focus on obtaining high margin revenues from telephony, the Internet, transactional and interactive services, in preference to promoting TV beyond the access pack, had reduced take-up for Flextech's channels. NTL should be required to promote services on an equal footing. If this was not forthcoming, third party access should be granted to help inject competition in the retailing of TV services via cable networks.

(b) Bundling different types of services had unnecessarily increased the cost of entry for the consumer, again reducing consumer take-up of cable TV and damaging the commercial interests of Flextech's channels. NTL should be required to offer TV services independently of all bundled offerings.

(c) Content providers were investing millions of pounds to create interactive content across all platforms that would empower consumers to choose, challenge and control the services they watched and used. The value to the user was located wholly in the content embedded in the signal. NTL should not limit access by third parties to the enhanced functionality available from its digital platform or the technical information relevant to understanding that enhanced functionality.

(d) While network operators should expect to be compensated for the one-off cost of investment in enhancing services on their platform, regulation should ensure that NTL did not abuse its dominant position by seeking to charge excessive access and back-end fees (namely fees charged by platform operators to transport a request and/or information back from the customer to the interactive service provider or broadcaster) for enhanced and interactive services, as it was currently trying to do. Back-end fees should not apply to enhanced services (passive 'non-commercial' services, ie digital teletext) and only fair, reasonable and non-discriminatory charges should apply to commercial transactions.

(e) Safeguards should be put in place to ensure that NTL did not exploit its position to demand substantial shares in revenues generated by a channel's own interactive and/or enhanced services and advertising.

(f) Conditional access and access control rules did not apply to NTL because it operated a closed system. Given that NTL would control 27 per cent of the pay-TV universe, strict rules should apply for access to interactive applications transmitted as part of TV programmes. All prices charged for access to a network system must be fair, reasonable and non-discriminatory. Also, NTL was a vertically integrated business and this situation could lead quickly to anti-competitive

activity as NTL favoured its own services (Front Row, British Eurosport and new interactive services) over third parties.

(g) Conditional access rules also ensured access to content and access by service providers to end-users via the EPG. Given NTL's EPG would supply the navigation for some 1.9 million viewers around the plethora of services available in digital it should be classified as a 'regulated supplier' under OFTEL's conditional access rules.

(h) NTL had stated that it would invest directly in content if it did not get it at the best economic terms. NTL should not use its dominant position to squeeze independent content providers to get the economic terms that best suited its own vertically integrated business.

(i) The consumer would lose out if NTL was allowed to acquire exclusive premium content. For the benefit of all consumers all such content owned by NTL must be capable of being made available to viewers across all platforms.

5.116. Flextech added that, ideally, it wanted to see a transparent digital universe where content providers competed against each other and networks competed with each other on price, value quality and flexibility. If consolidation meant fewer competing platforms then what was urgently needed was a framework that delivered commonality, openness and choice. Without such a framework, it would be better for the merger not to go ahead.

Granada Sky Broadcasting Ltd

5.117. Granada Sky Broadcasting Ltd (GSB) told us that it provided three TV channels to the cable industry and had done so for the past three years. These were: Granada Plus, Granada Men & Motors and Granada Breeze. Following the consolidation of the cable industry into three major companies (Telewest, NTL and CWC), and the abolition of MCRs, it observed that:

(a) Since the abolition of MCRs, GSB had seen no increase in the number of subscribers to its channels, and it now achieved lower penetration levels due to the increased complexity of programme packages available to the customer.

(b) Carriage fees (ie pence per subscriber) had been reduced significantly by the cable operators in recent negotiations, without regard to the consequences of *(a)* above.

(c) In GSB's experience, negotiations always included some element of the threat of non-carriage of one or more of its channels. As each of the operators now comprised such a significant proportion of the cable market, it was left with little choice but to comply with their proposed terms. [*Details omitted. See note on page iv.*]

(d) All operators were keen to remove channels from their analogue platform ostensibly to increase their digital capacity, and this point was clearly made in negotiations. This coincided with the expansion of their own pay services in analogue.

(e) All digital TV carriage agreements now required the channel provider to make commitments regarding interactive and e-commerce developments. Operators had demanded up to 45 per cent of revenues generated from such commercial exploitation as well as significant access payments.

MTV Networks Europe

5.118. MTV Networks Europe (MTVNE) is a division of Viacom Inc, a major international entertainment group: its submission was supported by MTV Networks. It owns and operates a variety of pay-TV programmes which are distributed to customers via cable TV networks such as those of NTL and CWC, DTH satellite services such as BSkyB, and ONdigital's DTT platform. MTVNE's TV programmes are distributed by both NTL and CWC.

5.119. MTVNE said it understood that competition authorities in the EC would generally consider the activities of cable operators in two separate pay-TV markets: *(a)* the market for the purchase of pay-TV programme services by cable TV operators; and *(b)* the market for the supply to consumers of pay-TV programme services by cable TV operators. MTVNE said that its own principal concern was the first of these markets, as it was one of the channel providers whose TV programme services were purchased by cable TV operators. However, MTVNE did not consider that the increased power of NTL/CWC which would result from the merger would lead to any countervailing benefits to consumers in the second market.

5.120. MTVNE said that it had to obtain transmission on both cable and satellite in order to generate sufficient distribution and advertising revenues to cover its fixed costs. The cable operator was at a considerable advantage in relation to channel providers, as it both controlled access to viewers and had regulatory protection in the form of the ITC's rules on MCRs. Access to viewers was the ultimate determinant of the revenue of channel providers—payments by the cable operator were usually calculated by reference to the number of cable operator subscribers who chose the channel, and advertising income depended on viewer figures. With an open system, on the other hand, there was always an alternative in negotiation: Viacom could take its Paramount, Nickelodeon, MTV and VH-1 channels and rent the transmission capacity from a cable system, pay them a fixed fee for it and have a direct relationship with the consumer using its own marketing operation. This option was not available with cable operators.

5.121. [

Details omitted. See note on page iv.

] On the other hand, it acknowledged that the open system as operated by BSkyB had made no difference to the level of abuse of power regarding negotiation of deals since content providers remained dependent on the subscription fees provided by BSkyB. BSkyB, as well as the cable operators, had behaved aggressively towards independent programme providers.

5.122. The ITC had issued a direction on 26 June 1998 (the MCR Direction) to prohibit agreements between channel providers and distributors such as cable operators which guaranteed that the channel would be carried to a specified percentage of subscribers to the pay-TV service (MCRs). The effect of the MCR Direction was to disable channel providers such as MTVNE from seeking to stipulate the packages in which their channels were sold. The cable operators therefore determined the channel packages available to consumers. The ITC had stated that the 'underlying objective' of the MCR Direction was 'to increase viewers' freedom of choice in relation to basic channels and to minimize actual or potential anti-competitive effects of buy-through'. The ITC considered that the MCR Direction left considerable flexibility in how channel providers and cable operators determined pricing for channels. In practice, MTVNE's experience was that the cable operators relied on the regulatory advantage they had been given by the MCR Direction in order to impose pricing and packaging terms heavily weighted in their favour, with a significant adverse effect on the profitability of companies such as MTVNE.

5.123. One cable operator, for example, categorically ruled out any minimum revenue guarantees despite the ITC's support for minimum revenue guarantees to protect the channel providers against the loss of MCRs. MTVNE could not risk jeopardizing its valuable relationship with the operator; it had therefore not sought to prevent carriage of all six of MTVNE's channels on its cable service—even though it had not yet been able to invoice for them because there was no agreement on fees. A recent article in the trade press had reported on some of the difficulties encountered by channel providers in general in dealings with NTL.

5.124. In MTVNE's view, the abuse of market power did not produce benefits to consumers, but was positively harmful to consumers' interests. There was no evidence that the highly favourable financial terms extracted were passed on to consumers, the charge to subscribers being up to five times greater than the payments offered to MTVNE. Cable operators also routinely ignored the ITC's statement that 'the composition of packages must reflect, so far as was practicable, viewer demand. To this end, channel providers should be able to influence the positioning of their channels'. MTVNE's experience had been that cable operators did not provide any information to channel providers on how they determined packaging, whether based on viewer research or otherwise. This exclusion of channel providers from the decision-making process ignored the valuable help they could offer, using their highly developed data sources and research tools. For example, the current digital offerings failed to increase customer choice since, by bundling channels by genre (for example, music), a customer desiring a varied selection of programme types had to buy at least two-thirds of the packages on offer.

5.125. MTVNE was also concerned about the plans of the cable operators for the digital environment. The cable operators were seeking both carriage fees and a share of advertising revenues on web sites included in the 'walled gardens' to be offered by some of the cable companies, although companies such as MTVNE had incurred the cost of repurposing their web sites. MTVNE was also concerned about the issue of the EPG with cable operators, as it believed this was a new gatekeeping control. If there was an EPG being put together by a distributor, the distributor could rank channels as they saw fit. If NTL and CWC created a single EPG, the merged company could use as a negotiating tool the need for channel providers to be listed on it and to be in as prominent position as possible. MTVNE as an independent programme provider did not have the budget to pay for such positioning. If the merger were to proceed, MTV believed it should be able to provide an independent EPG so that there was an option for it not to be completely controlled by one single commercial entity. MTVNE was also concerned about the overlaying of interactive services of other service providers on part of the screen while MTV was being watched, adversely affecting advertising revenues. Similarly, MTVNE believed that the 'Now and Next' information should be programming information only which appeared on the screen for a short time as and when the consumer asked for it. CWC had told MTVNE it wanted to be able to put advertising and sponsorship banners in the 'Now and Next' material which would be overlaid on to its channel screen, and MTVNE had no power to stop it. The merger would make the situation worse as the combined entity would represent even more of MTVNE's revenue. It would control a large number of homes and, as it grew, a large percentage of homes. That in itself might lead to a redistribution of advertising sales away from channels to the cable operators, the net effect of which would endanger the existence of MTVNE's channels.

5.126. MTVNE said that it would be less concerned at the current and future market power of NTL and CWC if abuses of that market power could be readily challenged and subject to meaningful remedies. However, its experience to date had been that the ITC had been unable or unwilling to take an effective role in monitoring and acting against anti-competitive practices. MTVNE was also concerned that, even with its enhanced powers under the Competition Act 1998, the OFT would be unwilling to devote its scarce resources to intervening in commercial arrangements within an industry which was subject to regulation by both the ITC and (for certain purposes) OFTEL. Past experience suggested that the OFT may be reluctant to intervene on issues which were within the jurisdiction of the ITC as well as the OFT, even though the ITC lacked experience in competition regulation.

5.127. MTVNE believed that the merged group's increased market power would inevitably lead to more abuses, unchecked by regulatory intervention. It believed NTL wanted to apply to the former CWC systems either the MTVNE/NTL contract or the MTVNE/CWC contract for programming, depending on which was most favourable to the merged NTL/CWC group. In effect, NTL/CWC would cherry-pick the best deals in order to apply them across both cable systems of the merged group. The market power of the merged group was such that channel providers such as MTVNE had little choice but to accept such terms as were imposed by NTL in order for NTL/CWC to realize benefits from the merger. This could bring into question the continuation of some channels in the UK.

5.128. MTVNE believed that, to meet its concerns, the issue of minimum payment guarantees should be revisited, and open access to the cable systems should be considered, to give MTVNE the facility, possibly with other content providers, to market its channels direct to consumers. Open EPG provision should also be required so editorial control of the EPG was not solely with the cable operators.

ONdigital plc

5.129. ONdigital told us that it believed the merger of the two cable operators had been inevitable for some time, and was necessary and desirable to create competition with BSkyB. It believed, however, that there should be a review of the market power of the combined group in telephony and related markets and of whether open access to the cable networks should be required. It was also concerned about the bundling by cable operators of telephony and pay-TV, which, it felt, involved cross-subsidy of pay-TV from telephony rentals and, given the market power of the combined entity, would amount to unfair competition.

Open Interactive Limited

5.130. Open told us that it recently launched as the UK's first national interactive digital TV company, operating an interactive platform and providing a broadcast channel under its own licence from the

ITC. Open had secured carriage on the digital satellite platform with the effect that its services were presently available to approximately 1.8 million homes.

5.131. The digital satellite platform was open in the sense that competing service providers may procure access to subscriber terminals in accordance with the applicable conditional access and access control regime. Other companies had announced their intention to operate competitive services to Open. Open sought to reach as many homes as possible, despite the risk of competition on the open platform, to ensure success. Open did not have the ability to go elsewhere unless the 'gatekeepers' allowed it, and at present the cable companies were legally allowed to act as gatekeepers.

5.132. Open was seeking actively to bring its services into the largest possible number of UK homes by means of different distribution mechanisms. Cable consumers would only be provided with a choice of interactive services if the services offered by Open, and those of other market entrants, were available to viewers in cable homes. Otherwise, short of switching to an alternative digital platform, cable subscribers would have no choice but to use the digital interactive TV services offered by the cable operator, even where they might have a clear preference for an alternative provider.

5.133. Open had concerns that the proposed merger between NTL and CWC's consumer cable and TV operations was likely to have adverse consequences for the development of competition and choice in this area. It believed the proposed merger raised significant issues regarding the development of a competitive market for interactive digital services in the UK, and that the merger could create a company whose interactive services business could attain a potentially dominant market position across digital platforms. Open was one of a number of companies in the market place offering new kinds of services. Unless Open was able to have access to open platforms for its interactive services, the prospect of its being able to compete would be hindered. Two-thirds of the UK cable industry would be controlled by one company with significant resources at its disposal if the merger went ahead, and NTL had demonstrated an unwillingness to permit competition across its networks. With the merged company able to foreclose its network to other interactive service providers such as Open, there would be a serious impact on those companies' chances to build successful and competitive businesses.

5.134. Open was party to continuing discussions with representatives from each of the cable companies. NTL had made much of the development of its interactive TV services, and Open feared it had no intention to give consumers the opportunity to choose interactive services provided by competing operators. If the merged company were to foreclose its cable network to Open, Open's opportunity to obtain access to a percentage of the digital TV homes in the UK would be significantly diminished.

5.135. If Open could not procure carriage on the merged company's networks, competition would be threatened by a reduction in Open's ability to market its interactive service to potential content providers. In those circumstances, when competing to attract content providers, the merged company would be at a substantial competitive advantage since it would be able to provide third parties with the opportunity to reach consumers in a much larger number of digital TV homes, including cable homes and satellite homes. The extent to which Open's penetration was limited in this manner as compared to the merged company's would also have implications for Open's ability to recover its fixed costs.

5.136. In any event, the consolidation of the cable industry from three operators to two (and the probability of further consolidation) meant that the newly created merged company would, by reason of its increased subscriber base and therefore greater attractiveness as a platform, be able to exercise greater market power in relation to the determination of prices for access control and related services to incoming interactive TV companies whom it permitted to access its network.

5.137. Open said that it expected to face competition in the provision of interactive services from each of the existing cable companies as well as QVC and others. However, following the proposed merger, Open would face the unenviable proposition that the merged company, backed by the greater breadth of resource and investment capital that the merged company would be able to bring to bear, would be able to market its interactive TV services to subscribers in digital satellite homes. On the other hand, even if Open were able to market its interactive TV services to subscribers in digital cable homes, it might well be obliged to accept terms that were onerous and put it at a cost disadvantage relative to the merged company's own interactive service provider. This would substantially undermine Open's ability to compete effectively against interactive TV services provided by the merged company. Such a reduction in competition would be detrimental to consumers and act against the public interest.

5.138. Open therefore believed that the merged company would be able to use its ability to foreclose access, or to provide access only on condition of paying excessive amounts for access control services, to a large percentage of digital TV homes in order to position its interactive service as the most attractive multi-platform service to the detriment of other interactive service providers. This would substantially prejudice Open and any other interactive services company and, Open believed, would lead to a reduction in competition to the detriment of consumers.

5.139. In the light of the above concerns, consolidation of the cable industry, if permitted at all, should be accompanied by undertakings, or the imposition of measures, to ensure that those companies wishing to offer competing services may gain access to the cable networks and that access should be provided to them on fair, reasonable and non-discriminatory terms.

QVC The Shopping Channel

5.140. QVC said that if the merger were allowed to proceed without safeguards it would be against the public interest. However, with proper safeguards that assured fair access to gateways, the merger could improve competition among the providers of multi-channel TV.

5.141. Cable currently provided TV carriage to 3 million multi-channel homes, and it was growing by 500,000 to 600,000 new homes each year. The merged company would currently control 65 per cent of connected cable homes (25 per cent of multi-channel homes). Cable would play a crucial role in access to the information highway, at a time when there was widespread recognition of the social and economic benefits from such access; it also enjoyed unique advantages of scope and scale. A company such as NTL, if left unregulated, would have the ability to hold up the introduction of the information society.

5.142. QVC said that there was a high degree of lock-in once a subscriber signed up to a multi-channel distributor. Very few subscribers took more than one multi-channel provider, and once a consumer was locked-in, competition became irrelevant. Competition and choice was the best way to serve the public interest. A merged NTL/CWC would be a monopoly supplier and this would deny choice to consumers. The merged company could either deny carriage or charge rates unrelated to the normal competitive environment and this would increase costs, which in turn would lead to higher prices for consumers. If QVC or any other channel could not negotiate terms which were market driven, they would then have no alternative means of reaching their audiences.

5.143. QVC said that electronic retailing was bringing increased competition to the UK market place, and new technology distribution methods were on the horizon. However, the potential boon would not reach the public if there was a gatekeeper to the system able to demand terms and conditions that would be in excess of those chargeable in a free market environment. The gatekeeper would be able to favour his own downstream entities, which were part of a vertically integrated business. This would restrict competition and therefore be detrimental to the public interest.

5.144. Safeguards for cable distribution should be set in the context of its main competitor, satellite DTH distribution. Over the last six years DTH distribution had moved from a gatekeeper-controlled environment to open platform. QVC said that safeguards should protect against the merged company becoming a gatekeeper. One way of achieving this would be to require it to make carriage open with tariffs that were fair, reasonable and non-discriminatory. Companies conducting business with the new company should be able to gain information which allowed them to establish whether the terms and conditions were fair. QVC said that NTL had announced its entry into the business of an e-commerce portal via TV; safeguards should also be put in place so that the merged company did not favour its own downstream business, nor should it be allowed to stop or inhibit competition with its own downstream businesses.

Tara Television Limited

5.145. Tara Television Limited (Tara) believed that the merger would not have any significant adverse effects on competition nor would it be against the public interest. While the effect of the merger

would be to reduce the number of major cable operators from three to two, Tara believed that significant competition would still exist in the delivery of multi-channel TV given the strength and size of BSkyB and ONdigital. Economies of scale would result which might be passed on to subscribers.

5.146. Smaller TV channels that served the interests of an ethnic group, such as Tara TV, could limit the number of intricate carriage negotiations and, when successful, be assessed by a wider population. In addition, the successful merger of the two companies should, in Tara TV's opinion, give rise to benefits in the area of telephony services: subscribers of NTL's telephony services should be able to make savings when making calls to subscribers in CWC's franchise areas. Sufficient competition would continue to exist in the area of telephony services given the number of telephone and mobile telephone companies operating in this sector of the industry.

Telewest Communications plc

5.147. Telewest told us that it believed the proposed merger was unlikely to operate against the public interest. NTL and CWC both operated in the pay-TV and telephony markets, as did Telewest. Telewest doubted that the merger would lead to any significant reduction in competition in either of those markets. Telewest believed that the consolidation of the cable market that had taken place over the last two years had transformed the prospects of the cable industry given the need for scale to invest in expensive technologies. The pay-TV market was, however, still unbalanced and, although Telewest believed it would itself be viable (despite its merger talks with CWC having proved unsuccessful), it believed that the pay-TV market would remain unbalanced with BSkyB still dominant irrespective of whether the NTL and CWC merger did proceed.

Pay-TV

5.148. In relation to the UK market for the retail distribution of pay-TV services, NTL, CWC and Telewest operated in geographically distinct franchise areas and did not therefore compete with each other. However, each cable operator competed, in a national pay-TV market, with the dominant pay-TV operator in the UK, BSkyB, and the recently established DTT operator, ONdigital. There were no local pay-TV markets.

5.149. All three cable companies had invested significant amounts of capital in building their networks within those franchise areas. As a result of this large investment made in their franchise areas, there was no realistic prospect in the short and medium term of the cable companies building out their networks into rivals' franchise areas, even after those franchise areas had become non-exclusive in 2001.

5.150. There was therefore no actual competition between the two parties to the merger in the pay-TV market and negligible prospects of potential competition. Consequently, the merger would not significantly lessen competition within that market.

5.151. Asked about the issue of open access to the cable network, Telewest said that it did not see itself as a 'closed network', since it was dependent on offering its customers the products and services they wanted—irrespective of whether they were produced in-house by Telewest or by third parties. Nor, on the other hand, could satellite be regarded as an 'open' platform, given that it was aware of only one broadcaster which used the conditional access regulation to market direct to customers: almost all formed part of the BSkyB bundle of services. BSkyB was the broadcaster that would have most to gain from using cable as an open system, and dealing directly with cable customers, since it was the only third party with the necessary subscriber and management billing system, call centre and billing and other facilities. Given the scale of investment in the cable system (£[✂] in the case of Telewest plus continued investment particularly in digital technology), it was necessary to be able to develop products and services to provide a return on that investment, which was still a few years away.

Telephony

5.152. The UK telephony market was still dominated by BT, both in the residential and business segments. Telewest was one of many relatively small telephony operators, as were NTL and CWC (CWC's business telephony business would be divested to C&W prior to completion of the NTL/CWC transaction). The conditions of competition were such that the geographic scope of the relevant market(s) was national rather than regional or local. The combination of NTL and CWC would therefore have no adverse competitive effects.

United Broadcasting & Entertainment Limited

5.153. United Broadcasting & Entertainment Limited (United) said that it had no objections to the merger. It believed that the merger would enhance effective competition and had the potential to deliver benefits to the consumer.

5.154. Both businesses were already providers of 100 per cent of cable TV in their respective franchise areas and did not compete with one another in any area. The merger did not change this position and at the level of supply, competition and choice would not therefore be adversely affected. On the contrary, it regarded the merger as likely to generate benefits to consumers, content providers and rights owners, and to improve competition in the TV market generally.

5.155. First, the merger would create, for the first time in the cable industry, a realistic alternative to BSkyB as a purchaser of premium programming rights (for example, the rights to major sporting events). This would benefit rights owners; but it would also be beneficial to TV consumers by increasing the likelihood of premium content being made available via all pay-TV platforms competitively.

5.156. Secondly, it would benefit other content providers, who needed credible alternative distribution platforms in competition with each other in order to increase their chances of securing sufficient distribution to underpin their content/channels.

5.157. Thirdly, although the purchase price of premium rights may rise as a result of competition between BSkyB and the merged group (and others), United believed it was unlikely that prices charged to the consumer would rise accordingly. In practice, platform operators would need to sell such rights across all platforms in order to offset the cost of purchase and often, in addition, to satisfy the demands of rights holders. This would ensure increased availability of the most attractive pay-TV content to viewers. In this situation, it would expect to keep retail prices in check.

5.158. United said that it was widely anticipated that new categories of rights for premium content would become available in the future. The most obvious example was PPV. Increased balance in the competitive strength of pay-TV operators would improve the prospects of new form of rights being held by different platforms. This would also help to ensure competitive pressure on retail prices. Without well-matched competitors there was a risk that all new rights would end up being held by the dominant platform which was unlikely to be in the best interests of the consumer.

5.159. The combination of NTL and CWC cable operations would provide scope for economies of scale in such areas as hardware purchasing, telecommunication networks, the development of digital cable networks, the development of interactive and Internet-based services and in central overhead costs. Given the high level of competition between alternative pay-TV platforms to secure increased subscriber levels, there was a reasonable prospect that some of these benefits would be passed on to the consumer in order to increase cable's competitiveness against BSkyB.

5.160. The acquisition would therefore result in a pay-TV operator which was more able to compete with BSkyB and hence increase the level of competition in the pay-TV market.

5.161. However, United believed that consideration should be given to the implications for 'open access' in both cable and satellite, particularly where the distributor was also a content provider, in order to ensure that all suppliers have access on fair, reasonable and non-discriminatory terms. In addition, NTL should be bound to continue to offer consumers a variety of channel packages. The potential that cable operators had to bundle TV services, telephony services and other interactive services should also be

considered. United believed it important to ensure that cable operators did not secure undue competitive advantage through this means and that pricing remained clear and transparent at all times.

Another TV channel

5.162. Another TV channel said that the purpose of cable must be to have the ability to provide a wide range of diverse programming from a range of sources, which met the needs not only of the majority but also the many minority interest and ethnic groups, and in addition to be a source of educational and beneficial programming for the whole nation.

5.163. It said that minority and ethnic programming had been constantly rejected and undermined by NTL, ranging from arts programming to local news services such as Channel One and Live TV, despite the fact that these were contracts it inherited and required carriage by NTL. The channel said that it was being dropped because of NTL's pursuit of popular programming, stating that it had no capacity among its planned increased new service of 150 digital channels.

5.164. The channel said that if NTL wished to provide useful services and programmes for schools, then a language channel must be high on the list to assist the 3 million schoolchildren currently learning a language.

5.165. The channel said that if the merger between NTL and CWC were to proceed, and the new company became a dominant force in the UK cable industry, then there should be some public service remit attached as a condition whereby it was required to supply educational, international, European and ethnic minority interest programming as well as the more popular football and soaps.

Views of telecommunications operators

British Telecommunications plc

5.166. BT said that extensive competition existed in the telecommunication market in the UK, and this included competition at the stage of the final connection between a network operator's system and the individual customer (the 'local loop'). The NTL/CWC merger was unnecessary to create an effective competitor to BT in telecommunications. The entities involved the proposed merger were well-established and vigorous players, with strong technical, marketing, organizational and economic capability.

5.167. The proposed merger would, however, result in the elimination of competition between two existing and well-established players, in particular in the areas where each entity held contiguous or near-contiguous franchises and each would have competed vigorously with the other. There were services that could only be supplied by a cable TV network. Regulatory barriers prevented BT from offering broadcast services over its telephone network, and the economics of BT deploying a cable TV network or upgrading its own network to provide all services capable of being provided over a cable TV network meant that barriers to entry for BT were high. The most likely potential competitor to a cable TV operator was another cable TV operator in an adjacent franchise area, extending its network to the streets next to its area. That would not now happen between NTL and CWC. The Government had sought to encourage multiple build by changing its policy on exclusive franchise areas for cable TV and this transaction could be viewed as undermining that policy. The elimination of competition between the two entities as a result of the transition was detrimental to the structure of competition in the UK market and to consumers, for example in terms of reduced choice.

5.168. It was important to consider how to secure effective choice and availability of broadband services for the foreseeable future in the UK. BT's ADSL products generally offered customers a dedicated 1.5–2Mbit/s downstream (into the home) and a couple of hundred kbit/s upstream (out from the home). This capacity could then be used for the transfer of bulk data, e-mail, Internet access, e-commerce, telemetry or multimedia. The multimedia offering consisted of only one 'video quality' channel. Distance and physical characteristics of copper affected transmission rates and the services that could be offered. To offer VDSL with 25Mb services would require a five- to ten-year period of investment in electronics in, for example, fibre networks beyond the exchange and street cabinets.

5.169. The UK cable TV companies had built in tandem both a telephony network and a fibre/coaxial cable network. The fibre/coaxial network could support all of the offerings set out above. In addition, the cable network could also support some 20 to 30 TV analogue channels or 150 to 200 digital TV channels and still have capacity for cable modem access enabling a whole range of Internet and data services to be supported. The cable companies currently thus offered a bundled full range of services, a unique position in the market which was not capable of being replicated by existing or foreseeable competitors. However, these services were offered on a local basis, largely as a consequence of the Government's historic exclusive franchising policy.

5.170. At present, BT was restricted from broadcasting TV channels until 2001. However, even when this restriction was lifted, BT's ADSL offering could not offer a substitute for consumers requiring multi-channel broadcast TV together with interactive offerings, or even some interactive capability offered over cable modems. BT's cable networks were not cable TV networks and were not capable of offering multi-channel TV services, or two-way high-speed services. BT, therefore, would only be in a position to compete in this market if it were given access to a cable TV network on reasonable terms. This solution had been adopted to the issue of bottleneck monopoly control in other contexts. Satellite could provide the TV content, but this was only one way into the home, and was offered on a national or European basis. Also, BT could not see how it could be tailored for local and regional offerings in the way cable TV could.

5.171. NTL and CWC therefore operated systems which were technologically advanced and flexible and gave them advantages which non-cable operators, such as BT, did not enjoy in relation to the provision of high bandwidth services (broadband services) to customers. The demand for such services was present and growing at a rapid rate, for both business and for residential customers, having been stimulated recently by ever-increasing and popular uptake of personal computers and the Internet in the UK for leisure-, education- and work-related purposes.

5.172. The proposed merger would therefore lead to reduced competition between the two entities in the provision of broadband services in the UK and allow the merged company an effective monopoly control over the majority of the fibre and high-speed consumer connection in the UK. There would consequently be a detrimental impact on providers of broadband services (service providers). Companies such as BT were unable to compete 'head on' with the merged entity, with a detriment to the structure of competition in the UK and to consumers.

5.173. NTL and CWC presently practised 'bundling' of their TV and telephony offerings, and this was unconstrained by the industry regulators. Non-cable competitors such as BT, were constrained in their ability to respond directly to this practice, for both technological and regulatory reasons. TV content-providers suffered a detriment as a result of the practice and consumers suffered reduced choice. The proposed merger would increase the detrimental effects of NTL's and CWC's bundling practices.

5.174. The transaction also strengthened the existing market power of NTL as a cable operator in its ability to offer a package of products. It raised an issue of third party foreclosure in that a vertical relationship was being created between C&W and NTL. C&W's wholesale international and data products, together with its US Internet activities (acquired from MCI), would have a unique position in local markets in the UK. No competitor could sell the same or any equivalent package of voice, data, Internet and cable TV services to the customer.

5.175. In the event that C&W were to be regarded as having material influence over NTL following the transaction, there could also be a risk that the level of competition in the market for business telephony may be reduced. BT said that it would also be concerned about any element of discrimination in interconnection agreements which had been subject to little regulatory oversight when involving operators other than BT.

5.176. BT concluded that the proposed merger was likely to lead to effects on the structure and nature of competition in both the telecommunication and TV markets in the UK which were against the public interest.

5.177. On this basis, measures that perpetuated asymmetry of treatment of a merged entity from the treatment of BT, such as asymmetrical obligations on access to networks, should not be sustained since they distorted the structure of competition in the UK market for telecommunications and TV. BT believed that the merged company should therefore be subject to the same requirement as BT to allow open access to its network to a broad range of service providers.

Cégétel

5.178. Cégétel, a telecommunications operator in France, told us that, based on experience of competition in European communications markets, conditions must be attached to the proposed merger if it were to be approved. Failure to regulate a vertically integrated operator of the size of NTL/CWC, which was able to draw on the monopoly profits of its largest shareholder, France Telecom, would result in the creation of an unduly powerful player in the converged communications market. This would not be in the public interest.

5.179. Currently, voice telephony made up the greatest part of the average retail customer's communications need and spend. Most of the UK regulatory framework concentrated on BT, given BT's historical position in the UK voice telephony market, particularly its share of control of local access for voice services. NTL and CWC were at present largely unregulated, since their respective shares of the voice telephony market were much smaller than BT's.

5.180. However, voice telephony would shortly assume second place to other communications services in the average customer's basket of communication needs. UK customers were fortunate that aggressive competition in voice services and forward-looking, enlightened regulation had created an environment in which innovation may flourish.

5.181. The new communications environment would be a converged market, in which customers would be able to choose from hundreds of broadcast entertainment channels, numerous information resources, streamed audio and video on demand and two-way communications pathways. Services would be new but the regulatory issues would be the same as for voice. Control of access to the customer was everything and, once an operator had achieved the first mover advantage, particularly with access to revenues from a market in which there had been a monopoly, competition became extremely difficult to introduce. Ex-post regulation in such a situation would be 'closing the stable door after the horse had bolted'. Prevention was called for rather than cure.

5.182. Cégétel's concern was to press upon the UK competition authorities the need to appreciate fully the strategic impact of France Telecom's investment in NTL, through which the balance of competition could be permanently distorted in the UK's converged communications market. Cégétel was aware that France Telecom's investment had to date been treated as a separate competition issue to the NTL/CWC merger, but regarded this as erroneous. France Telecom's investment was in the acquisition of a major shareholding in the UK converged communications market. The NTL/CWC merger was a vehicle for that acquisition. France Telecom was a monopolist both in practice and in its corporate culture and expected to gain a foothold in the UK through leveraging its market power in the French local access market.

5.183. France Telecom continued to control access to the French local loop. This enabled it to ring-fence significant revenues from traditional markets and effective control of the provision of new technologies. In March 1999, the French Competition Council reported that despite enactment of laws in France which legally put an end to France Telecom's monopoly rights, and despite the entry of 54 new licensed operators into the French market, the difficulty of gaining access to the local loop meant that France Telecom continued to have a quasi-monopoly over communications services in the local loop. The council went on to express a view that the impossibility of gaining local access from any operator but France Telecom was likely partly to explain why competition in long-distance markets was weak, giving France Telecom a market share of 94.9 per cent of the fixed long-distance market in December 1998, a year after full liberalization, compared with BT's market share of less than 50 per cent in some long-distance markets. The French Competition Council had also commented on the slowness with which competition in electronic communications and information resources had developed, in particular because of the costly obstacle of having to upgrade outdated cable networks to provide communications services (nearly 70 per cent of which belonged to France Telecom) and the cost of access to public and private property to lay new infrastructure. The net result, according to the French Competition Council, was that France Telecom was the only operator capable of offering the full range of communications services within French national boundaries.

5.184. The French Competition Council had also forcefully criticized France Telecom's failure to offer non-discriminatory tariffs for Internet access, saying that this had prevented competition in the Internet access market. Cases had been brought before the Competition Council by 9 Telecom and

AOL-Cégétel relating to France Telecom's abuse of dominance on the local loop market which allowed France Telecom to favour its large bandwidth ISP's services, France Telecom being today the only operator able to market an ADSL service.

5.185. In spite of the findings of the French competition authorities, the local loop continued to be the monopoly of France Telecom. Through its acquisition of a stake in the merged NTL/CWC, France Telecom would have local access to more than 2.8 million UK customers, particularly for Internet access. No UK operator currently had any prospect of accessing on economic terms a market of this size in France, let alone capturing control of the local access gateway. No decision to require access to the French local loop was currently envisaged although recently there had been some political support for some form of unbundling but no details or date for a legal requirement had yet been set.

5.186. Cégétel believed the creation of a merged NTL/CWC, facilitated and funded by France Telecom, would operate against the public interest, as long as the merged group had unlimited and unconditional access to France Telecom's monopoly funding.

5.187. High up-front costs and a long payback created significant barriers to entry in the communications market, particularly where networks were being built or upgraded. Network competition had got further in the UK than anywhere else in the world because the former monopolist had been effectively regulated and new entrants were in comparable positions. Cable operators all had to build out their networks and were given a period of grace, by the ban on broadcast services by BT, in which to do so. They did not compete against one another, but rather were in comparable competitive positions against a heavily regulated BT and indirect access operators who did not share their economies of scope.

5.188. The cable industry was now changing into an altogether different creature. Consolidation had reduced the number of operators from hundreds to only three. Cable operators would soon be competing against each other beyond the footprint of their own franchises through BT's ADSL roll-out and carrier pre-selection. And most importantly, as charges for voice services were reduced towards costs, all operators would be concentrating on interactive and information age services. The social and economic importance of ensuring access for all to these services was frequently underlined by the UK Government. Cable operators with modern broadband networks were uniquely placed to provide access to these services. Unlike BT's ADSL service, roll-out of which was just beginning, broadband cable networks already passed more than 50 per cent of households. The competitive balance between cable operators and BT was maintained as long as their balance sheets carried the same costs of network development. But a cash injection for one of these from a new, external source was likely to upset the fragile balance in the emerging market for Internet and high bandwidth services, and this was particularly so where the cash injection was funded by monopoly rents from outside the UK. NTL would share the advantages of France Telecom's monopoly. The benefits of such inward investment from abroad might be short-lived, by leveraging France Telecom's dominant domestic position into the lucrative and not yet competitive UK market in order to steal a first mover advantage.

5.189. BT was making a significant commitment to ADSL roll-out. OFTEL had required local loop unbundling as competition to BT and many operators were committing resources to this strategy. The economic viability of these investments could disappear if the new NTL was able to develop its networks through monopoly rents whilst offering retail prices which did not reflect costs. The impact on the consumer was likely to be negative in the long term. NTL would buy Telewest, which would be unable to compete without NTL's access to monopoly funds. This would leave only BT and NTL, which was likely to result in a duopoly in the provision of high bandwidth services of the sort which existed between Mercury and BT in the 1980s. Effective competition did not develop in the voice telephony market then and would not develop in the Internet and broadband services market in the future. New entrants would not want to compete against two giants, one dominant in the UK and the other dominant in an adjacent national market, where both could achieve economies of scope and scale in developing technology and purchasing power.

5.190. Cégétel accepted that France Telecom's market power in France could not be regulated in the UK. One condition open to the Commission would be accounting separation between NTL business funded by France Telecom and NTL's other business. In Cégétel's view, this would not be a solution. Not only would it be difficult to develop in practice and impossible to police, it would probably also be counter- productive since the benefits of a flood of inward investment might be lost. In Cégétel's view, a better solution to the problem was to protect the UK customer from the impact of France Telecom's dominance in France so that its contribution to the UK market did not distort competition.

5.191. Cégétel therefore argued that the merger as currently proposed would not be in the public interest without certain controls on France Telecom's ability to leverage its monopoly into the UK. An undertaking from France Telecom to unbundle its local loops—therefore giving access to the bare copper—would resolve the problem, by opening up the French local market to competition, which would exert the full force of competition on France Telecom, ensuring that its investments in the UK were economic and long term rather than predatory and designed for market capture. There would be other benefits to the UK economy in that the French telecommunication market would become as open to UK operators as the UK market was to operators from abroad. This was the intention of the EC Open Network Provision Directives and inward investment generated from new markets could only benefit the UK consumer.

Crown Castle UK Limited

5.192. Crown Castle said that it had an interest at one remove in the merger between NTL and CWC. Crown Castle explained that it acquired the transmission infrastructure of the BBC (in excess of 700 transmission sites) during 1997. It currently owned approximately 2,000 transmission sites in the UK, which were used to provide broadcast and other telecommunications site services to its broadcast and telecommunications customers: its broadcast customers at present included the BBC, ONdigital, NTL and a number of commercial radio broadcasters as well as all the wireless service providers in the UK. It did not compete with broadcasters or other customers, but offered them an independent service provision of site and network infrastructure facilities.

5.193. Crown Castle said that it was not its intention that the proposed merger should be prevented or delayed in any way. It was fully appreciative of the business reasons why such a merger helped the development of the UK cable sector as a stronger competitor to the existing satellite and terrestrial platform delivery systems.

5.194. However, Crown Castle had certain concerns about the potential impact upon the cooperation between itself and NTL that was necessary for the deployment and expansion of digital broadcasting and other services. The ownership of the terrestrial broadcast site networks used to provide analogue and DTT services in the UK was currently divided up and down the country in roughly equal numbers between itself and NTL. It was necessary therefore for there to be cooperation and a sharing of tower sites between itself and NTL for the networks to function as a seamless and cohesive whole for the benefit of customers and the community. Such cooperation and sharing had recently been required for the development and expansion of the first phase of digital broadcasting services.

5.195. The terrestrial analogue and digital broadcast sites which Crown Castle and NTL owned represented one form of TV delivery mechanism in the UK. Satellite was the other main competing platform, with the potential for cable to become a further and additional competing platform. Third generation telephony (3G) technology which would converge voice, video and data might become yet another platform with the relevant licence auctions due to take place in early 2000. Utilization of current UK tower sites (along with the development of additional new tower sites) would be instrumental in the success of 3G roll-out, and again required cooperation for rapid and comprehensive deployment.

MCI WorldCom Limited

5.196. MCI said that it did not wish to make any representations in favour of, or in opposition to, the merger. However, it did perceive potential for future anti-competitive behaviour given the increase in market power for NTL in the residential market that would result, and the potential for emergence of duopoly power between BT and NTL. This development emphasized the importance of full unbundling of the local loop, and it may also be appropriate to investigate whether NTL should be required to offer carrier pre-selection and/or indirect access to competing operators. Any exclusivity arrangements between NTL and CWC relating to carriage particularly of international traffic may also be detrimental to effective competition in the wholesale market.

United Pan-Europe Communications NV

5.197. United Pan-Europe Communications NV (UPC), a Dutch company with headquarters in Amsterdam, told us that it was one of the most innovative broadband communications companies in Europe and owned and operated one of the largest pan-European groups of broadband communication networks. It provided cable TV, telephony, high-speed Internet access and programming services in 12 countries across Europe and in Israel. As of 31 October 1999, UPC's systems passed approximately 9 million homes with more than 5.9 million basic cable subscribers. In addition, UPC systems had 166,000 residential telephony lines and 20,200 business telephony lines, as well as 89,400 residential Internet subscribers and 3,600 business Internet subscribers.

5.198. Although not a cable operator in the UK, UPC was an investor, with a variety of programming interests, and with one of its corporate offices in London. With a view to its focus on the broadband market in the widest possible sense, UPC may in the future be interested in expanding its presence in the UK through wireless local loop or other infrastructures. Furthermore, it was interested in regulatory and competition policy developments across the EC. In that light, it was interested in the Commission's consideration of the proposed acquisition by NTL of CWC's cable businesses, and had a variety of comments on this issue in the light of its substantial experience of the cable sector elsewhere in Europe.

Future of cable

5.199. As a general comment, UPC believed that the cable industry across Europe was at something of a crossroads. Increasingly cable provided a strong and effective competitor to incumbent telephony operators and, itself, competed or would compete with a variety of access technologies. The growing importance of a strong cable sector was something that had been implicitly and explicitly recognized by the European Commission. For example, in accepting an offer from Telia and Telenor to divest their cable networks the European Commission recognized the value of real competition from cable. Equally, the outcome of the European Commission's cable review highlighted the important competitive pressure that cable could bring to bear in the telephony arena.

5.200. In UPC's view the consolidation of the UK cable sector, by creating strong and vibrant companies, had gone a long way towards establishing cable as a viable competitor to BT, BSkyB and the powerful mobile communications sector. In the future cable would be competing with a variety of other technologies and companies in a variety of markets. In UPC's view, the merged entity would be a more effective actor in all these markets. In any event, NTL and CWC's cable businesses did not, today, compete. UPC therefore saw that this merger would bring the benefits of increased competition to UK consumers.

Access issues

5.201. UPC understood that one of the issues that the Commission might be asked to consider was whether NTL should be required, as a condition of approval of its acquisition of CWC's residential cable business, to grant a right to access directly the available frequency spectrum on the cable network (also referred to as forced access).

5.202. This issue was being hotly debated in many EC countries and was something of great interest and concern to UPC and to all companies which had invested in building broadband communication networks. Any conclusion reached on this issue in the context of the merger reference would not only impact on third parties within the UK, but would also establish a precedent for the treatment of the same issue in other countries.

5.203. Moreover, there was no equivalent for forced access by, say, someone seeking to provide conditional access services in relation to the networks of, for instance, BSkyB or ONdigital. Nor, following the merger, would such a requirement be in place on the system of Telewest. The European Commission, in its recently published 1999 communications review, discussed access issues in some detail and recognized that forced access had considerable implications for investment in infrastructure and that the regulatory framework should not distort incentives for investment and innovation in services and in infrastructure. It was therefore necessary to take into account the serious impact that forced access may have on investment in infrastructure and to consider whether it would be appropriate for the UK to

impose forced access on a relatively new market player in the UK, such as NTL, whilst these matters were still under review at the European level.

5.204. In UPC's view, the best way to protect incentives to invest was to consider any possible measure with respect to access within a clear and robust legal framework. This framework must derive from established competition law principles, imposing onerous obligations only on those who were truly dominant, and ensuring a fair level of competition between the new multimedia infrastructures on satellite, digital terrestrial, cable, ADSL and wireless local loop. Furthermore, this framework should, in general, provide for ex post remedies to deal with specific abuses of dominance, and avoid imposing ex ante conditions on those who had some degree of market power in a market today where there was no certainty that they would continue to have market power in the market of tomorrow.

5.205. It was clear that if NTL was allowed to go ahead with the CWC acquisition it would be, by some margin, the largest cable operator in the UK. But, of itself, this should in no way justify the imposition of forced access. It was necessary to consider whether NTL, as a result of the acquisition of CWC, would be dominant in any relevant market and, if so, whether such dominance would give rise to anti-competitive effects which demanded the imposition of forced access as an ex ante condition.

5.206. In examining the relevant market, the electronic communications market as a whole and its likely development over the next few years should be considered, rather than the more limited pay-TV market of today. The next few years promised the development of real infrastructure competition in local access networks for the delivery of a range of digital services. Some of these services were already available (digital satellite and DTT), others were in the offing (digital cable and ADSL provided by BT and others), others (wireless local loop and 3G mobile) would emerge over time. Those who were making the risky investments in those systems should be able to exploit those investments by selling services over those networks, subject only to the constraints of general competition law. With no one network likely to be in a position of dominance, forced access for service providers would be neither justifiable nor necessary. The multitude of infrastructures developing should ensure the viability of commercial negotiations between all parties in the market.

5.207. If a dominant player emerged at some time in the future, then any abuse of that dominance should be dealt with at that time. It should not be dealt with pre-emptively at this stage. The imposition of forced access of any kind on NTL at this stage would risk stifling the very investment in alternative local access networks that would in the short to medium term start to produce real competition and consumer benefits.

5.208. The European Commission, within the context of the 1999 communications review, was doing much work to set out a policy at EC level for the resolution of access issues. Within the UK, OFTEL had recently addressed in its statement, 'Delivering Competition for the Information Age', the issue of access to BT's network. Within that document, OFTEL stated that it would be examining the issue of access to cable networks in the New Year. Similarly, regulators in other European countries were examining the issue. This was a far-reaching debate, which impacted on many market participants in the UK and elsewhere. The proper authorities to consider the matter were these regulatory authorities and the European Commission.

Conclusions

5.209. UPC was therefore of the view that the proposed transaction would be of benefit both to consumers and to competition within the UK. Were access requirements to be imposed as a condition of clearance for this merger, such a decision would have a deleterious effect on the competitiveness of communications in the UK. This matter could and would be addressed by OFTEL in accordance with the policy guidelines of EC communications and competition policy. Action in this area would not be appropriate in the context of this proposed transaction.

Vodafone Limited (on behalf of UK Operators Group)

5.210. Vodafone Limited (Vodafone) wrote to us on behalf of the UK Operators Group to comment on suggestions which had emerged in the press regarding any mandating as a result of this inquiry of some form of 'open access' to the infrastructure of the combined NTL and CWC residential cable interests in the UK.

5.211. Vodafone told us that the Operators Group was an informal grouping of non-BT-licensed operators active in the UK telecommunication market to provide a forum for joint representation of participants' views to regulatory authorities. Its membership was committed to the development of telecommunication services competition, including infrastructure-based competition, within the UK.

5.212. While the UK Operators Group contained both NTL and CWC, it also represented the interests of a wide variety of operators providing competing infrastructure in the UK communication market. A shared concern was that regulatory rules must ensure appropriate incentives to support the development of competing infrastructures. In its view 'open access' to competitively developed and privately financed infrastructure should be required by the regulatory authorities only where there was unambiguous evidence of serious, non-transitory competitive problems which could not be rectified, except through intervention.

5.213. 'Open access' was an important and complex policy area where OFTEL and the European Commission had already begun to develop a regulatory framework. For example, in the UK this was emerging in areas such as the Access Control Class Licence. A Competition Commission ruling pre-emptively imposing 'open access', even if only applying to NTL/CWC, would set an unwelcome precedent and have profound adverse implications on infrastructure development within the UK competitive environment.

5.214. Operators believed that, given the continued existence of a sectoral regulator and the work now being done by the European Commission, the development of additional policy in the area of access should fall to those bodies. As policy on 'open access' was explored by sectoral regulators, this should give rise to a coherent overall framework which could be applied consistently across the communications and broadcasting sectors, rather than emerging from the examination by the Competition Commission of a specific merger.

5.215. In the case of the planned NTL/CWC merger, the Operators Group would anticipate that regulators would monitor the activities of this entity in the market and, should significant competitive problems develop and persist, consider intervention only after such problems have been identified.

5.216. The Operators Group therefore urged the Competition Commission to forbear from creating any additional access obligation on a combined NTL/CWC beyond that which sectoral policy determined was appropriate.

Views of consumers and trade associations

Consumers' Association

5.217. The Consumers' Association (CA) said that the proposed merger between NTL and CWC covered a number of markets, most notably fixed line telephony, pay-TV and interactive services (both Internet and platform-specific). The former two markets were categorized by dominant players that were not concerned in this merger. In the case of residential fixed line telephony the merged company would have to face the dominance of BT and in pay-TV the less monolithic position of BSkyB. This position was recognized by both OFTEL and the ITC.

5.218. In terms of consumers affected by this merger, as of April 1999 NTL had cabling that passed 3,361,998 homes and CWC 3,981,578, a total of 7,343,576 homes passed. NTL penetration ran around an average of 30 per cent (rising to 40 per cent in their strongest markets), with CWC reaching around 21 per cent of homes passed. The combined companies would possess a total of around 1.8 million subscribers compared with 3.5 million for BSkyB.

5.219. The key question was whether the merged entity would possess sufficient market power in the relevant market in order for its actions to have any lasting detrimental impacts upon competition and the terms upon which services are provided to consumers. For the reasons set out below, CA did not believe that the merged entity would possess such market power.

Fixed line telecommunications

5.220. CA believed that the market for residential telephony services was effectively a national one. In the areas of cable activity the consumer had the choice of at least two platforms. For the consumer facing a choice between cable and BT (or a smaller indirect access provider) the range of choice was the same irrespective of the provider. It was only limited by the particular cable operator that had the franchise for the area in which they lived. As the cable franchises were not overlapping in telecommunications provision, the likely effect of this merger was extremely limited. If anything, the merger of the companies may allow for greater efficiency gains through the merging of such things as billing and maintenance staffs and software. Such efficiency gains may allow the firms to offer consumers better services or lower prices. In any case the competitive threat from the massive market power of BT was such that any merged entity would not be in a position to abuse its customers.

5.221. There was no competition problem in the proposed merger regarding residential fixed line telephony. BT still had a statistical monopoly over residential and business telephony on a local, national and international basis. The size of the NTL/CWC merged entity would reach a maximum of around 10 per cent for residential customers. If business customers were included, the market share of the merged company would be a few percentage points lower in each market segment. The dominance of BT in the retail fixed market was so great that this merger could only be a good thing for competition in telephony.

Pay-TV services

5.222. The market for pay-TV services was also framed by the options available to the consumer dependent upon the area in which they lived. A consumer in an area with a cable franchise in operation would be able to choose between at least the cable service and BSkyB and, in most areas, ONdigital (but need not choose any of the services at the moment, given the universal access to analogue terrestrial programming). Pay-TV was thus an elective choice made by the consumer on the basis of the choices available in their area.

5.223. The market for pay-TV was currently led, by some margin, by BSkyB with 50 per cent of subscriber numbers and 65 per cent of revenue. The combined market share of NTL/CWC would rise to 27.1 per cent, in terms of subscribers, and 21.9 per cent in terms of revenue (although the latter excluded data for ONdigital).

5.224. The market was particularly concentrated because of the dominance of the largest player, BSkyB, in the key markets for sports and, to a slightly lesser extent, film rights. The key issue in pay-TV, as in telephony competition, was whether the merger would lead to a loss in the number of companies competing in the market. The answer was not the obvious one that one would find in most merger cases. This was because the market for pay-TV, as chosen by consumers, was largely driven by competition between platforms, rather than between the companies supplying those platforms. In essence it mattered little whether there were three or four cable companies as they operated non-overlapping territories and competed directly with digital satellite and digital terrestrial services. The competition between pay-TV platforms had also to be framed against the background of a market which was still growing, and was not yet mature. If the market had been mature, then in CA's view there would be an issue arising out of the increased concentration brought about by the merger.

5.225. The only possible competition and consumer welfare issue CA could see emerging in this case was the issue of access to networks. BSkyB made great play about its inability to gain access to cable networks on a totally open basis. However, CA thought that the issue of open access contained a number of important strands to it. First, there was the competition issue, which may be reduced to an analysis of whether cable was an essential facility. Secondly, there was the important element of public policy and the extent to which access by consumers to competing broadcasting platforms was part of the concept of universal service and access for consumers.

5.226. While CA recognized that there might be important issues in the longer term, particularly when the market began to mature, it did not think that this referral was either the right place, nor came at the right time, for this debate to take place. This market was a growing one and one that was subject to quite marked technological developments such as the new generation of mobile telephony devices that may shape the market in ways that current players may have little control over. It was also unlikely that the market for digital interactive services would be able to develop in the hands of Open or cable-based interactive services, in isolation from broader Internet-based interactivity.

5.227. CA did not think that, in a rapidly growing market and one that was nowhere near maturity, the essential facilities doctrine had a major role to play. In the longer term such a situation may arise. However, this merger did not raise issues of such major significance as to warrant such a large step to be taken.

5.228. The key issues for the future of digital pay-TV related much more directly to the market for sports and film rights. The UK aspect of the sports rights market was essentially categorized by the dominance of BSkyB which held almost all of the commercially important sports rights and then on-sold them to competing platforms and broadcasters. The sports rights market within the UK could be categorized as a duopoly. While the greatest owner of sports rights was BSkyB, there remained a public service sports broadcasting presence which had gained rights on a European basis through the operation of the EBU cartel. The proposed merger was unlikely to make this situation any worse and indeed was likely to make it better. The bidding power of BSkyB and the companies that made up ONdigital was sufficient to ensure that a very limited degree of competition existed for sports rights in the UK and for beyond the border sports events with a pay-TV element. The introduction of strengthened cable operators was merely likely to add a new competitor to the mix. It was thus likely to help break the current stranglehold that BSkyB had on the pay-TV and PPV sports market. For the consumer and competition this could only be a good thing. The current limited coverage of the cable network was also likely to ensure, at the moment, that any sports rights bid for by the merged NTL/CWC were unlikely to be bid for on an exclusive basis.

5.229. The market for film rights was less rigid than the one for sports rights and the merger of NTL/CWC was unlikely to have a negative effect on the market. A strengthened NTL/CWC may be in a better position to compete with BSkyB and ONdigital for existing film rights and may be in a position to sign deals with film studios that it currently could not. This was partly due to the fact that film rights were not sold entirely on the basis of the amount of money bid for those rights, since the seller was also interested in ensuring a wide exposure for the film in question. The proposed merger may thus enable NTL/CWC to offer more audience in film rights bids and thus be able to compete more effectively with the digital terrestrial and satellite broadcasters.

Interactive services

5.230. Interactivity figured greatly in all discussions of the future of broadcasting. However, it was currently in its infancy, be it Internet-based or platform-specific interactivity. The idea that the merged NTL/CWC could create a significant problem for Internet access or charging at this stage of its development was, in CA's view, wide of the mark. Again, the Internet market was a very small one and one that was growing and evolving rapidly. The major impact that a merged NTL/CWC operation may have on Internet access was to enhance it through offering faster modem access for subscribers. The issue of interactivity related to both the idea of cable companies acting as exclusive ISPs (ie directing consumers to specified sites) and to their role as the providers of access to superior technology. Again the latter raised the issue of whether cable was an essential facility, in a technical sense, for future provision of broadband services and whether the Internet itself could be classed as an essential facility for the future provision of services, be they governmental or private. In either case it was still premature to look at this issue in the context of a Commission review of a specific merger when the implications of open access and Internet access would affect the entire broadcasting and network infrastructure industries. The existing regulators were better placed to carry out such a review.

5.231. The only possible problem with this development would occur if those consumers were directed to certain sites ahead of others, or were led into a closed sub-section of the Internet. Even then, provided that they were aware that what they were getting was a closed, rather than open, system, as occurs with the Open proposition, and had the option to connect to the Internet via the more traditional means of PC and modem, CA did not think that this was an issue worth worrying about.

5.232. The issue of interactivity via dedicated platform-specific sites was slightly less clear, but still not currently a significant problem. However, CA recognized that it may emerge as a larger issue in the future. The limited, platform-specific operations were clearly not as popular, nor as enticing, as Internet services. The real problem that the digital satellite operators were likely to have with cable-based interactive services was the fact that they were likely to be considerably faster and more capable of dealing in larger volumes of data. This had nothing to do with unfair competition, dominance, or restrictions to competition, it was a simple technology issue: the digital satellite interactive service simply could not deal as quickly with large volumes of data as a broadband cable-based system. Should cable be able to

reach a majority of houses and establish a dominant market position, the issue of cable as an essential facility may arise. Again, this was neither the time nor the place to be considering such a situation.

Conclusion

5.233. CA did not therefore think that the proposed merger would in any way undermine competition or consumer welfare. Indeed, provided competition from alternative platforms remained strong, it thought that the merged company might become a more effective competitor in the markets for sports and film rights. It also thought that the merger may create some consumer benefits in the form of service improvements or price reductions, provided that the merged firm passed on some of the benefits that it might accrue from efficiency savings or enhanced buying power.

5.234. CA was concerned that the only possible competition issue, that of open access, be dealt with by the right regulators at the right time. The pay-TV and telephone markets were marked by dominance of incumbents and by significant technological change. The telephone market was still dominated by BT. Here the merged company might be able to compete more effectively for custom. Even if it did not, the new generation of mobile telephony licences may inject a new wave of competition for BT. In either case the proposed merger provided no competition problems. In pay-TV the situation was slightly different. The pay-TV market was a long way away from being a mature market. As such, current market positions were only part of the picture. The dominance of BSkyB in subscriber numbers and revenue was a good reason to view the proposed merger with leniency and was a good reason not to worry unduly about the issue of open access. Household penetration levels for cable were currently so low (20 to 30 per cent on average past around 6 million homes for the firms under review) that it would be premature to contemplate the cable operators as an essential facility. There was little in the technology that would stop a later reassessment of this position, should the cable industry reach a market position of any real significance. Even were this position to occur, there was already a regulatory environment in which such provisions could be negotiated or imposed as a result of consultation. The Commission was not the best place for this debate to occur, particularly considering the fact that a consultation on the issue of platform access is scheduled to occur early in the new year.

5.235. CA therefore thought that the merger should be passed without any conditions attached.

Professional Footballers' Association

5.236. The Professional Footballers' Association (PFA) said that it represented almost 4,000 professional footballers in England and Wales who were members of the Association and who would be directly affected by the merger. The increasing domination of football by TV companies, and in particular concerns regarding PPV, were matters regularly discussed by the Association's management committee and delegates at all the football clubs.

5.237. The PFA was concerned at the damage which could be done to the national game if those controlling TV coverage also controlled one or more of the major football clubs. At the time of the BSkyB bid for Manchester United, the PFA said it had predicted that TV companies would look to impose an increasing stranglehold upon professional football, including increased PPV, and it felt that this was anti-competitive and contrary to the interests of spectators as well as creating undesirable risks for players. The power of TV could easily destroy the less attractive clubs whose games might no longer be televised and who might be excluded from a share of the income which they currently received through collective bargaining.

5.238. In the PFA's view, it seemed likely that there would be further penetration into football club ownership by TV companies, and in doing so they would seek to secure a controlling position for TV rights which would benefit nobody but the TV companies themselves. The power of TV companies to build up the profile of particular football matches and then increase the cost of PPV was a real concern. The amalgamation of a TV and utilities company such as NTL (which had already shown its hand by making a bid for Newcastle United in early 1999) with a dominant cable company in England which had a significant interest in PPV was not in the public interest. It was designed to create the opportunity to

charge higher prices to the detriment of the viewing public. The PFA submitted that the merger of interests between NTL and C&W should be prohibited.

Telecommunication Managers Association

5.239. The Telecommunication Managers Association said that whereas there was adequate infrastructure competition in the urban areas, BT had a monopoly grip of the means of delivery outside them. However, where competition did exist outside urban areas, it was from either CWC or NTL, and not both: they tended to be complementary in the areas where it mattered. The impact of the merger on competition in the cities would therefore be insignificant, and outside the cities the merger would even be welcome as a new counterweight to BT, with national reach. The effective service provision capabilities of each player, when combined, should also be able to offer strong competition to the e-commerce offerings from BT and (now) Vodafone/Airtouch/Vivendi.

5.240. Hence, the merger would give added infrastructure competition outside urban areas, plus a powerful player on the service provision stage. The merger should be allowed to proceed with minimum delay.

Views of individuals

Councillor Martin Curry

5.241. Councillor Martin Curry objected to the proposed merger of NTL and CWC ConsumerCo without the imposition of conditions designed to promote competition. CWC had a monopoly in the supply of broadband entertainment, information and education in many of the locations that it operated in, and specifically in Bromley, and the merger with NTL would reinforce this position, whereas refusal of permission for the merger as proposed would allow competition to flourish to the benefit of the consumer.

5.242. Cable TV penetration was now 25 per cent according to recent figures published by the ITC, so therefore a local monopoly existed under English law; given that this had risen from 22.5 per cent in July 1998, cable TV penetration may now be over 25 per cent. It was government policy to allow competition in the provision of broadband services, and both NTL and Telewest had sought and recently obtained the permission of the ITC to change their franchises to non-exclusive ones. This allowed them to compete directly with each other now, rather than have to wait until 1 January 2001 when full competition would be imposed by the Government. Whilst the cable companies had claimed that they needed to merge in order to compete with BSkyB and the very limited number of channels provided on DTT, NTL and Telewest had very successfully worked together in the provision of Front Row, their joint PPV movie service. They were also able, through their joint programming venture CPP1, which had recently bought Live TV's carriage rights, to supply additional joint programming if they so wished without the necessity to merge. There was therefore no need for cable companies to come together as one UK cable company in order to compete with BSkyB.

5.243. Councillor Curry did not object absolutely to the merger being allowed, but if it was allowed, believed that a number of conditions should apply.

Separation of the programming and broadcasting functions of the merged company

5.244. CWC acted as both broadcaster and programmer, since it chose the channels that it wished to carry and which channels to drop. This was not the case for BSkyB, the satellite broadcaster with which CWC claimed to be in competition for customers. In order to promote competition in the supply of satellite services, BSkyB was required to provide its own encryption service to any satellite channel that wished to use it at a fair, non-discriminatory, published rate. Additionally, channels that did not wish to

be encrypted could be broadcast to satellite viewers free-to-air, from both satellite positions used by BSkyB without the agreement of BSkyB. EC rules required satellite receivers designed to receive Sky programming also to receive all free-to-air channels. A similar requirement on a combined CWC/NTL company would be in the interests of customers and programmers alike.

Cessation of the compulsory bundling of telephony with TV services

5.245. CWC had systematically migrated (in Councillor Curry's case against his specific requests) its customers from TV-only packages to combined packages that bundled TV with a free telephone service. As these combined services were more expensive, typically £6 to £7 more per month than the previous TV-only service, customers wishing to subscribe to multi-channel TV only were cross-subsidizing telephone-only and bundled customers. Cross-subsidization of a competitive service, telephony, by customers of a monopoly service, cable TV, was a classic example of abuse of monopoly power and should not be allowed to continue. The ITC/OFTEL report of their inquiry into the practice of bundling had been delayed until next year, but it was interesting to note that Telewest had now unbundled its cable TV service from its telephone service, with the combined service being charged for at a higher price than that for TV only. This was in the interests of its customers, who could choose which services they subscribed to, without having to pay for services that they did not want.

An increased public service requirement to require the carriage of at least four European language channels

5.246. CWC and NTL had consistently reduced the number of European language channels carried on their networks, despite the emphasis laid on these channels in many of the original licence applications. Councillor Curry did not believe it was in the interests of consumers as a whole that cable companies continued to remove European language channels that supported the national curriculum and adult students seeking to improve their language skills in order to assist British industry to compete more effectively in Europe. Specifically, one French, German, Spanish and Welsh language channel should be carried to support the GCSEs, A levels and adult education courses taught in this country; he suggested TV5 Europe, 3:Sat, TVE I, and S4C, all public service channels, which he believed could be provided free of charge to the cable companies. With 200 to 1,000 channels available for carriage of programming, it was unbelievable and unfortunate that cable companies were not providing these four channels to their customers. A cable company [✄] had indeed at a meeting (at director/councillor level) with representatives of a council [✄] agreed that certain European language channels would be available from the start of its digital service. Those assurances to retain language channels had not been kept, and it was because of this failure to keep to this agreement with the local educational authority that the combined company should be required as a public service obligation to provide at least these four European language channels.[1]

Access by other programmers to the local loop of the combined company

5.247. Such a requirement would apply to franchises where telephone penetration rate was greater than 25 per cent, from the date at which BT was required to provide access to its local loop. NTL currently managed to achieve rates of penetration of 40 per cent in the areas in which it operated, and had therefore obtained significant market share. It was only equitable that when BT was required to make its own local loop available to competitors the same condition should apply to other PTOs that had significant market share. If this policy was adopted, it should also serve to support the separation of programming and broadcasting functions of the combined cable company.

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[1][✄] said that it had insufficient time to investigate the veracity of this statement. The digital service in the area [✄] was only now being trialled and the ability to offer foreign language channels depended on negotiating successfully for the rights, customer demand and available bandwidth. [✄] already offered Asian and Chinese channels and intended to offer more foreign language channels in the future.

Local customer involvement in the choice of channels provided in each individual franchise area

5.248. The nature of the cable TV market in the UK was one of local franchises that could provide local programming tailored to their particular audience. The cable companies had consolidated into a number of groups, and had sought to provide a single national digital offering. This may be in the interests of the cable companies, but was not necessarily in the interests of their customers. A requirement to provide for local customer involvement in the choice of (at least some) channels carried in each franchise area would enable the customers in each area to exercise real control over the choice of channels made available.

5.249. Councillor Curry had also been very concerned to see a representative from NTL informing the House of Commons CMS Committee that NTL did not carry the UK's premier 24-hour news channel, Sky News, which apparently had four to five times as many viewers as BBC News 24. Councillor Curry observed that Sky News was the fourth most popular TV channel in the UK on Millennium eve beating all but three of the terrestrial channels, even though it was not carried by NTL in the UK. As a potential NTL subscriber, if the merger went ahead he wished for an assurance from NTL that Sky News would be carried in his franchise area. Its non-carriage on NTL demonstrated the abuse of monopoly and lack of consideration for customers that was currently only too common among cable companies.

Other individuals

5.250. We had comments from two other individuals:

(a) One, who had spent over 30 years at a senior level in the telecommunications industry, said that the reference of the proposed merger would set back the needful consolidation of the cable industry and wreck the plans for some £4 billion investment in the UK international Internet network. The ultimate losers would be customers who had long been at the mercy of BT's obsolescent end-user network, not to mention the BSkyB satellite channels. The workforce had lived with uncertainty and stress for two or three years as reorganizations and mergers resulted from rapid changes in technology and international markets. C&W had at last reached some stability in mission and management and a fragmented cable industry was getting its act together.

(b) The other was primarily concerned with the lack of choice which any local monopoly of broadband services created. First, the access to the Internet offered by CWC would be limited to its own favoured sites. These would be accessed via a TV screen and not a PC (there would be no facility for downloading). But the whole point of the Internet lay in the ability to access any site and not just those offered by an ISP. Access to academic and government sites would benefit from a 10Mb broadband cable modem, but such non-commercial educational material was unlikely to be available via NTL/CWC. Secondly, the bundling of TV services (cable, satellite or terrestrial broadcast) made a mockery of consumer sovereignty. The remedy in both cases was to give all service providers access to the local loop.

Media commentators

5.251. We also held, together with the group inquiry into the BSkyB/Vivendi merger, a hearing with a number of media commentators and analysts.[1] Among the points made were:

(a) As regards the definition of the market, it was appropriate to consider a market wider than the market for pay-TV, and to include interactive services. There was also an interaction between pay-TV and free-to-air TV, in that they were competing for audiences, advertising and programme rights, although free-to-air TV had not had the resources to compete head-to-head for live sports rights often. Pay-TV, however, had a separate sort of revenue, namely subscribers, which had had the further benefit of putting viewers in the position of customers, buying services

[1]Mr R Snoddy, *The Times* (who declared an interest); Mrs M Brown, *The Guardian;* Mr P T Larsen, *Financial Times;* Mrs E Duncan, *The Economist;* Mr N Higham, BBC; Mr P Richards, WestLB Panmure Limited.

because they wanted to view them. It was also suggested that pay-TV should be seen in the context of intellectual property rights in all their forms, the importance of which had led to an increasing degree of vertical integration in the industry, and a process of large integrated companies frequently cooperating with each other with or without the exchange of equity.

(b) It was also useful to distinguish between distribution platforms and the provision of content, BSkyB having the overwhelming advantage of being the only significant UK pay-TV operator which had a large amount of valuable content. This arose because BSkyB had taken the risk at considerable cost of acquiring football rights at an early stage, which gave it the demand which had made the platform widely taken. Cable had in the past been very fragmented so no single cable company had seen it worthwhile taking such a risk. BSkyB's position also resulted from its success in developing customer management systems, and the competence of its management, and the fact that the holders of sports rights liked BSkyB's presentation of programmes, in particular sport. The position of BSkyB was not, however, necessarily threatening, since it was an efficiently run company which had added a vital strand to the modern media scene, and, while powerful, this influence was neither overwhelming nor negative.

(c) The market was in a considerable state of flux. Demand from interactive services was by no means proven, but there was a market expectation that revenue per subscriber would double or treble. It would have to be left to the market to decide whether the nature of interactivity being introduced by new cable operators, involving of necessity a 'walled garden' approach giving access only to selected sites, would prove useful.

(d) The UK now had probably the most sophisticated cable system in the world, because of the time of its installation. An issue in the USA was whether the cable industry could foist upon consumers its own high-speed ISP, or whether it had to allow equal access to other ISPs.

(e) On the question of open access to cable networks, OFTEL was already investigating this question. It was a matter of judging when cable moved from being an impoverished industry still investing in the future to one that was mature and in which competition would be increased by open access. The moment might come when there was only one national cable company in the industry. Open access had been forced on BSkyB at a time when it was deemed to have a dominant position in the UK market, but it could not be said that cable was yet in a comparable position. The emergence of other technologies, including ADSL and mobile phones able to provide some services currently available on cable, could itself limit the strength of cable's position.

(f) It was thought that the merger did not make any difference to consumers, except in so far as it countered a fragmentation of the cable industry which made the industry inefficient. None of those present had significant concerns about the merger.