OFFICE OF FAIR TRADING

Completed acquisition by Creative Broadcast Services Limited of BBC Broadcast Limited

The OFT's decision on reference under section 22 (1) given on 2 November 2005. Full text of decision published 11 November 2005.

Please note square brackets indicate information excised or replaced by a range at the request of the merging parties or third parties for reasons of commercial confidentiality

PARTIES

1. **Creative Broadcast Services Limited (CBSL)** is a newly incorporated UK company which is 65.3 per cent owned by Australian listed investment fund, Macquarie Capital Alliance Group (MCAG), and 34.7 per cent owned by diversified international specialist financial and investment banking services provider, Macquarie Bank Limited (MBL), both members of the Macquarie Bank Group.

2. **BBC Broadcast Limited (BBCB)** was a commercial subsidiary of the BBC, offering a complete range of services required to launch, promote, playout and provide access to broadcast content on different media platforms. BBCB has two wholly-owned subsidiaries: Broadcasting Dataservices, which provides media scheduling information; and, BBC Broadcast USA, Inc. In the year ending 31 March 2005, BBCB's worldwide turnover was [ ] and its UK turnover was [ ].

TRANSACTION

3. CBSL acquired sole control of BBCB on 31 July 2005 and the consideration was £166 million. The administrative deadline expires on 2 November 2005.

4. The OFT considers that MBL has material influence over BBCB (via CBSL). As a minimum, a shareholding conferring on the holder 25 per cent or more of the voting rights in a UK company generally enables the holder to block special resolutions; consequently, consistent with OFT Guidelines, the OFT considers that CBSL's acquisition may give MBL the ability materially to influence the policy of BBCB. The OFT's analysis does not rely on a statement by CBSL that this is a temporary underwriting stake to be sold down to third party investors in the short term.

5. The OFT also considers that MBL may have the ability to materially influence the policy of another playout provider, Arqiva (formerly ntl Broadcast) having regard to all the circumstances of the case and, in particular, a combination of shareholdings, a management services agreement, and [board appointments]. Arqiva is wholly owned by Macquarie UK Broadcast Holdings Limited (MUBHL). MUBHL is 54 per cent owned by Australian listed investment fund, Macquarie Communications Infrastructure Group (MCIG), 4.3 per cent owned by MBL, 10.9 per cent owned by other funds managed by MBL subsidiaries, and 30.8 per cent owned by other investors. In addition to MBL's direct shareholding in Arqiva, a wholly owned MBL subsidiary has an 8.5 per cent interest in MCIG. MCIG has delegated to this subsidiary the responsibility for managing MCIG's interests in the companies it invests in under a management services agreement. Finally, there are a number of [board appointments], the key ones being MBL has jointly appointed one director to the board of Arqiva and an executive director of Macquarie Bank is the deputy chairman of Arqiva.

6. The parties have entered into a 10 year services supply agreement (the Framework Agreement) with the BBC, whereby the BBC exclusively outsources to CBSL the provision of services previously supplied to it by BBCB. The OFT has been asked to form a view as to whether the Framework Agreement would be considered ancillary to the merger. The OFT generally follows the European Commission's Notice on ancillary restraints, which provides that only those restrictions that are 'directly related and necessary' to the legimitate objective sought of implementing the concentration are justified. In particular, restrictions to competition should be of limited duration. The Commission Notice indicates that the duration of supply restrictions are acceptable for up to five years. The life of the Framework Agreement agreed by the parties is outside this time limit. A 10 year duration agreement is further demonstrated to be unnecessary as [ ]. Therefore, the OFT does not consider that such an arrangement is directly related and necessary in order to implement the merger.

JURISDICTION

7. As a result of this transaction CBSL and BBCB have ceased to be distinct. The UK turnover of BBCB exceeds £70 million, so the turnover test in section 23(1)(b) of the Act is satisfied. The OFT therefore believes that it is or may be the case that a relevant merger situation has been created.

RELEVANT MARKET

8. This transaction gives rise to a horizontal overlap for the provision of linear playout services for TV insofar as MBL is considered by the OFT to have material influence over both BBCB and Arqiva (as discussed above).

Product market

9. Playout is the process by which programme content is transformed from a number of individual tapes or digitised formats to a continuous stream of content ready for TV transmission. It can range from the provision of technical facilities to fully managed services (including operational staff), and include associated services such as channel management which is the administrative task of providing detailed schedule planning to ensure that a playlist runs exactly to time within the main broadcasting schedule.

10. Traditionally many channel owners provide their own playout services, although there appears to have been a recent trend for outsourcing if it proves cost effective by comparison with self-provision. The parties submit that as customers regard self-provision as a substitute for outsourcing, and can readily switch from one to the other, the relevant product frame of reference should include both outsourced and in-house playout services.

11. As the immediacy and extent to which outsourcing channel owners could self-provide playout services and the extent to which channel providers currently providing their own playout services could supply third parties are both unclear, it may be appropriate to limit the relevant frame of reference for the purpose of this assessment to the provision of playout services to third parties, while considering the former alternatives as constraints in the assessment below. In any event, given no competition concerns arise at even this narrower level, it has not been necessary to conclude on product market definition.

Geographic market

12. The parties and third parties have indicated that playout services providers do not necessarily have to be situated in close proximity to the customer and can be provided on a transnational basis (although one third party indicated that it would not consider using non-UK providers for logistical reasons). Therefore, the narrowest relevant geographic frame of reference is considered to be UK-wide. However, as no competition concerns arise at even the UK level, it has not been necessary to reach a firm conclusion on geographic market definition.

HORIZONTAL ISSUES

Market shares

13. According to the parties, the total combined share of supply of BBCB and Arqiva for outsourced and in-house playout provision is [approximately 20-25 per cent by

volume or value] and the increment is relatively low [less than 10 per cent] in both cases.[1] The parties estimate that the combined share by volume would increase if in-house (including affiliate) supply was excluded to approximately [30-40 per cent (increment no more than 10 per cent], and approximately [50-60 per cent (increment no more than 10 per cent] for share by value. It should be noted that the previously in-house supply to the BBC by BBCB is now treated as outsourced playout provision, with around three quarters of BBCB's revenues being derived from the provision of services to the BBC under the Framework Agreement in the last year. Therefore, the parties argue that BBCB's share of supply to 'pure' third party channels is very small.

Bidding data

14. The parties submit that the supply of playout services is a bidding market with business being mainly acquired through contracts put out to tender and, accordingly, share of supply data is not necessarily a key indicator of market power. Of likely greater importance is the number of credible bidders available, as it would be open for customers to seek bids from other playout providers if the parties' prices were to rise following the merger.

15. Bidding data for the last three years provided by BBCB and other third parties suggests that Arqiva and BBCB have bid for the same contracts on a limited number of occasions (around one third of BBCB's total number of bids and a much smaller fraction of Arqiva's total during this period). A number of significant playout providers remain (e.g. Ascent Media, BT Broadcast, and Technicolor), including at least one other playout service provider which has bid against BBCB with similar frequency as Arqiva. Taken in conjunction with third party opinion that BBCB typically bids for more complex, high quality contracts than Arqiva, the OFT believes that they do not appear to operate as each other's closest competitors.

Barriers to entry and expansion

16. On the basis of the evidence provided, it appears that barriers to entry are not insurmountable. Although equipment is expensive, investment can be recouped over the medium to long term. Moreover, third parties broadly supported the view that sponsored new entry by channel owners has occurred and a number of credible entrants appear to exist (e.g. post-production companies).

17. Contracts with buyers, which the parties have indicated tend to be awarded for relatively long durations (ranging from three to five years for less complex

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[1] BBCB estimates of share of supply for playout services by total number of channels played out in the UK and by revenues for 2004.

channels up to seven to ten years for larger, more complex channels), may be identified as a potential exclusionary device, at least in the short to medium term. As it is unclear whether a playout provider without a three to ten year contract would be able to obtain much work on an ad hoc basis, a firm wishing to enter may have to wait until large contracts with incumbents are about to be re-tendered. Contracts may not be cancellable with relatively short notice and significant switching costs may exist, particularly taking into account the need to maintain continuity of transmission during changeover.[2] However, new providers are generally willing and able to absorb these costs, which may be amortised over the term of the new contract.

Buyer power

18. Buyers of complex channel playout services are typically large, sophisticated channel owners, including terrestrial broadcasters, which may possess a degree of buyer power. They make purchasing decisions on the basis of a tendering process. In-house provision appears to be an option for some customers, and/or wholly captive broadcasters (e.g. ITV, Channel 4) could supply third parties in the event of a price rise or sponsor new entry. Taken in conjunction with existing competition, these factors together would appear to represent a competitive constraint on the merged entity.

VERTICAL ISSUES

19. No vertical issues arise from this transaction apart from those raised by third parties addressed below.

THIRD PARTY VIEWS

20. Some third parties expressed the concern that the merger brings together BBCB, a large sophisticated complex playout service provider (with a reputation for high quality service derived from its experience of servicing the BBC), and the terrestrial TV broadcast transmission services capabilities of Arqiva (as one of only two UK terrestrial transmission providers). In particular, post-merger Arqiva might be able to bundle BBCB's playout services with its terrestrial transmission services at a price substantially undercutting its competitors. There is no evidence to suggest, however, that any change in this respect as a result of the transaction would be significant as Arqiva already provides playout and could currently bundle its services. Furthermore, given the limited capacity of terrestrial TV, most playout contracts relate to satellite and cable and there would be limited foreclosure.

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[2] [ ]

21. A customer raised the concern that the merger reduces the number of credible playout providers who combine with channel management services to one post-merger. The OFT does not have reason to believe, on the basis of the evidence provided, that the merger has a significant impact on competition in this respect taking into account: BBCB has not previously provided channel management services to unaffiliated customers and does not, therefore, act as an existing constraint on outsourced provision; the vast majority of channel owners appear to carry out channel management services in-house; and, there do not appear to be substantial barriers to entry in providing channel management services for channel owners not currently self-supplying (according to the parties, likely start-up costs can be limited to readily available off-the-shelf software and staff training).

ASSESSMENT

22. The OFT considers that the parties overlap in the supply of playout services as a result of the material influence (34 per cent shareholding) over CBSL by MBL, which may also have an existing ability to materially influence playout provider, Arqiva, by virtue of a combination of factors outlined above including a combination of shareholdings, a management services agreement, and common directorships.

23. A combined share of [approximately 20-25 per cent] for outsourced and in-house playout service provision is created, with an increment of [no more than 10 per cent]. This share increases to approximately [30-40 per cent (increment no more than10 per cent)] by volume when third party provision is considered alone, however, the bulk of this can be attributed to the previously exclusive in-house supply of playout by the BBCB to the BBC and, therefore, share of supply data may be misleading. The parties opine that this is a bidding market and there appear to have been only a limited number of occasions when Arqiva and BBCB have bid for the same contracts in the last 3 years. Based on the evidence provided, the parties do not appear to be each other's closest competitor for playout provision and there are a number of other significant playout providers providing sufficient actual rivalry to constrain post-acquisition behaviour. The threat of customers switching to self-supply would appear to act as a viable competitive constraint in the event of a price rise, as would potential outsourcing by wholly captive broadcasters and/or the sponsoring of new entry.

24. Taken in conjunction with a general lack of third party concerns, the OFT believes that the loss of any competitive constraint as a result of this transaction will not be significant. Consequently, the OFT does not believe that it is or may be the case that the merger has resulted or may be expected to result in a substantial lessening of competition within a market or markets in the United Kingdom.

DECISION

25. This merger will therefore not be referred to the Competition Commission under section 22(1) of the Act.