

LMR Network Services Market Investigation

Overview of unpublished Working Papers

13 May 2022

This is one of a series of consultative working papers which will be published during the course of the investigation. This paper should be read alongside the issues statement and the other working papers which accompany it. These papers do not form the inquiry group's provisional findings. The group is carrying forward its information-gathering and analysis work and will proceed to prepare its provisional findings, which are currently scheduled for publication in June, taking into consideration responses to the consultation on the issues statement and the working papers. Parties wishing to comment on this paper should send their comments to MRN@cma.gov.uk by 27 May 2022.

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The Competition and Markets Authority has excluded from this published version of the working paper information which the inquiry group considers should be excluded having regard to the three considerations set out in section 244 of the Enterprise Act 2002 (specified information: considerations relevant to disclosure). The omissions are indicated by [✂]. [Some numbers have been replaced by a range. These are shown in square brackets.] [Non-sensitive wording is also indicated in square brackets.]

Introduction

1. This document aims to provide interested parties with an overview of pieces of analysis that we are carrying out in the course of this market investigation but are not publishing on our website at this point in time, due to the potential commercial sensitivity of these pieces of analysis. It is published to assist interested parties to understand the totality of the work being carried out as part of the investigation and to invite their comments and any further evidence for consideration by the Group conducting the investigation prior to the publication of its provisional decision report (currently scheduled for June). The [market investigation timetable](#) can be found on the CMA's dedicated case page. We should emphasize that the Group has not reached any (preliminary or otherwise) conclusions at this stage and that our analysis may change, as our work continues and as we consider additional evidence submitted in response to the working papers.
2. The evidence we have gathered to date and our emerging thinking are set out in a series of Working Papers, some of which are being disclosed to Motorola or Motorola and the Home Office only, rather than being published on our website for the reasons set out above. This document aims to provide an overview of these working papers, which relate to: Airwave contracts; Benchmarking provisions; Negotiations between Motorola and the Home Office; and Transfer charges relevant to Airwave Solutions Limited (Airwave Solutions). The sections that follow introduce these four working papers in turn.
3. In addition, we are publishing non-confidential versions of working papers relating to: Motorola's dual role; Cost of capital; Profitability; the Scope for competition; and Remedies. All published documents relating to this investigation can be found on the [MRN market investigation web page](#).

Airwave Contracts

4. This section sets out the scope of the 'Airwave contracts' working paper.
5. The purpose of this paper is to set out the CMA's understanding of the contractual relationships between Motorola, the Home Office and users of the Airwave Network (Motorola's customers).
6. We are examining in particular:
 - (a) the contractual position in:

- (i) 2000, when the PFI Agreement was entered into by the Police Information Technology Organisation (“PITO”), the original contracting public authority, and the original service provider, British Telecommunications plc (“BT”);
 - (ii) 2016, when a number of contract extensions which provided for a uniform end date for all Airwave contracts and the shutdown of the Airwave Network were agreed. The Deed of Recovery was also agreed in 2016;
 - (iii) 2018, when a second set of contract extensions were agreed extending the end date for the Airwave Contracts to December 2022;
 - (iv) 2021 and now; and
- (b) the extent to which key contract terms were settled in 2016 and/or to which they were subject to further negotiation and agreement.
7. Our current focus is on understanding:
- (a) the important aspects of the key contracts entered into between the Home Office, other relevant authorities, and Airwave Solutions;
 - (b) how these contracts relate to one another; and
 - (c) the terms of the contracts which are most likely to be relevant to the competition assessment.
8. We note that, while an understanding of the contractual position is of value, the focus of this market investigation is broader and requires us to look at the market structure, firms’ behaviours and practices and the relationships in the market. The contractual terms are helpful in this regard but are not determinative.

Benchmarking

9. This section sets out the scope of the ‘Benchmarking’ working paper.
10. In its response to the Issues Statement, Motorola stated:

“The Issues Statement is silent on whether the Group intends to take account of the benchmarking provisions agreed between the parties, yet this may have a significant bearing on profitability [X] when the [X] to invoke these provisions. In addition to carefully drafted provisions on pricing, the contract with the Home Office contains an independent third-party referral process (the “Benchmarking Process”) to ensure that prices are fair, which has already

been used by the parties. Indeed, the Home Office [X]. The Home Office was satisfied by both the price discounts and overall contractual arrangements, including additional capital investments executed in those agreements. The Benchmarking Process was used on two occasions to verify the fairness of pricing, and on both occasions the third party found no excessive pricing for the Airwave service.¹

The Group is therefore respectfully invited to give requisite weight to the method chosen by the well-advised parties to address questions of value for money within the contract. The benchmarking provisions are fully capable of addressing value for money. Otherwise, contractual certainty is destroyed, and that cannot be an appropriate or proportionate intervention.”

11. The purpose of this working paper is to consider Motorola’s above submissions, including that *“the benchmarking provisions are fully capable of addressing value for money”*. Our current focus is on setting out the relevant facts pertaining to the above statements by Motorola, that we have been able to establish based on our review of the internal documents obtained from Motorola and the Home Office in response to our information requests. A review of these internal documents will help inform our assessment of whether benchmarking provisions, in the specific context of a PFI Agreement, are likely to be effective in constraining prices either through the benchmarking process itself or as a negotiation tool – or whether there are limitations of the benchmarking provisions which significantly weakens their effectiveness.

2016 Negotiations

12. This section sets out the scope of the ‘Negotiations’ working paper.
13. Motorola has made a number of representations in relation to the negotiations between it and the Home Office. For example, in its response to the Issues Statement, Motorola stated: *‘Any market investigation where there is a sole supplier and a sole customer should examine separately whether bargaining power is skewed in favour of one side to an extent that would give this side unilateral market power. If there are no grounds to consider such an uneven distribution of negotiation power, this points strongly towards the conclusion that the market is working well.’²*
14. In relation to the negotiations that took place in 2016, Motorola stated that: *‘The 2015/2016 negotiations yielded a very substantial improvement over the*

¹ Motorola Solutions (publishing.service.gov.uk), paragraph 94.

² Motorola Solutions (publishing.service.gov.uk), paragraph 38.

arrangements in place with the Airwave's prior owner and the Home Office leveraged its veto to achieve extraordinary flexibility to continue Airwave effectively as an open-ended insurance policy against ESN prolongation, as well as an interworking solution from Motorola that would achieve transition of users from Airwave to ESN (something that Airwave's then owners were not in a position to accomplish).'³

15. Our starting point is that high market concentration, in this case monopoly provision, in principle, can be expected to give a supplier a significant level of market power (by comparison to less concentrated markets). However, in cases where customers are sizeable institutions that represent a large proportion of a supplier's demand, the argument is sometimes made that they have countervailing buyer power that may be capable of counteracting the effect of the market power of the supplier, thus potentially securing outcomes that are comparable to those achieved in a well-functioning market. It is in this context that the analysis of bilateral negotiations may be required in considering whether the LMR market is functioning well.
16. As the CMA's Market Investigation Guidelines⁴ state:

“Countervailing buyer power may also be taken into account in the [CMA's] competitive assessment. In some markets prices are in effect determined by the relative bargaining power of sellers and buyers. The exercise of buyer power can sometimes be a feature harming competition. However, in other circumstances 'countervailing buyer power' can have the positive effect of preventing the exercise of a supplier's market power in the bargaining process. The presence of large buyers relative to the size of the suppliers does not necessarily guarantee that the buyers can exert countervailing buyer power. The relative importance to each buyer and supplier of its business with the other party factor, and the strength of the buyers' 'outside options', ie their alternative strategies in relation to the relevant product, is often the crucial determinant of countervailing buyer power.”
17. Therefore, in considering the bilateral negotiations that took place in 2016 in particular, our analysis is currently focused on determining the outside options

³ [Motorola Solutions \(publishing.service.gov.uk\)](https://publishing.service.gov.uk), paragraph 38.

⁴ [CC3 \(Revised\), Guidelines for market investigations: Their role, procedures, assessment and remedies \(publishing.service.gov.uk\)](https://publishing.service.gov.uk), paragraph 176

of each party to the negotiation and the cost to each party of walking away from the negotiation.

18. Undertaking a qualitative assessment of whether the outcomes of a negotiation for a customer are 'good' or 'bad'—and therefore whether the supplier that customer is negotiating with has market power—is an inherently difficult exercise and is better assessed through other means (such as profitability analysis). The purpose of the Negotiations working paper is therefore not to assess whether outcomes are 'good' or 'bad', but rather to carry out a qualitative assessment of the strength of the outside options available to the Home Office and Motorola at the time of the negotiations.
19. The Negotiations working paper therefore seeks to address Motorola's submissions by focusing on three key questions:
 - (a) the commercial context within which the provisions relating to extensions and their pricing were negotiated in 2016 and interpreted at that time and subsequently;
 - (b) the economic realities of the negotiating parties' respective bargaining positions and in particular the 'outside options' open to them; and
 - (c) the outcome of the negotiation process, to the extent that it is an indicator of the exercise of market power by the Motorola or buyer power by the Home Office.
20. The paper also notes that negotiations have taken place between the parties since 2016, in 2018 and 2021, that relate to the extension and pricing of the Airwave network.

Transfer charges

21. This section sets out the scope of the 'Transfer charges' working paper.
22. The purpose of this paper is to establish, for the current and recent past, the cost and revenue base for those business activities within Airwave Solutions that are relevant to this market investigation. We currently consider that these are the connectivity services that are delivered over the Airwave Network under the Airwave Contracts.
23. Airwave Solutions is not a standalone firm transacting exclusively with third parties, rather it is part of the Motorola corporate group and it transacts extensively with other businesses within that group. Airwave Solutions

therefore utilises both resources external to the Motorola corporate group and resources that have been provided internally.⁵

24. For externally provided resources, we note that Motorola, in common with the previous owners of Airwave Solutions, would have had the incentive to select suppliers in a way that minimises its overall cost base. Therefore, the costs reported for purchases are likely to reflect reasonably efficient choices at the time by Motorola.
25. For internally provided resources, however, it is not clear whether resources costed in line with the transfer charging practices of a corporate group would, necessarily, reflect economic costs. We are, therefore, undertaking a detailed review of Airwave Solutions transactions with the rest of the Motorola Group.
26. The starting point for this exercise is the statutory financial statements for Airwave Solutions, which amongst other things, accounts for all the services provided under the Airwave Contracts. We are considering which type of services provided by Airwave Solutions should be considered as relevant for our assessment of profitability and the revenues and associated costs for these services as reported by Motorola. The output of this exercise will be a set of revenues and operating costs for the identified services and an approach to measuring capex.

⁵ For this purpose costs that Airwave Solutions incurs by contracting with third parties (which would include its staff costs) are counted as external costs.