

## Ex ante and ex post regulation: Is regulation to be taken into account in deciding whether to regulate?

### Hutchison 3G UK Limited v The Office of Communications [2009] EWCA Civ 683

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Following a complex procedural history, the issue of mobile call termination charges was considered by the Court of Appeal. Hutchison 3G UK Limited ('H3G') appealed against a decision by the Office of Communications ('OFCOM'), upheld by the Competition Appeal Tribunal ('the Tribunal'), that it had significant market power in the market for mobile call termination on its network and should be subject to price controls. The Court of Appeal rejected H3G's appeal. It held in particular that the Tribunal was right to find that, in determining whether the conditions for imposing *ex ante* regulation were met, the qualified nature of existing *ex ante* regulation, and OFCOM's power to impose *ex post* regulation, should be disregarded.

#### Mobile call termination and its regulation

In the UK, five mobile telephone network operators ('MNOs') have a monopoly over their own mobile telephone networks. Each of them provides a service, to each other and to fixed network operators including British Telecommunications ('BT'), of connecting telephone calls to their networks. This service is called mobile call termination ('MCT'), and each operator charges for it.

OFCOM, as the UK regulator of the telecommunications market, has responsibility for determining whether the market in *inter alia* MCT is 'effectively competitive'. If it is not, OFCOM is to identify which undertakings in that market have significant market power ('SMP'), (defined as undertakings having the '*power to behave to an*

*appreciable extent independently of competitors, customers and ultimately consumers*), and to impose (or amend) regulation of that undertaking, which may include price controls. Such regulation is termed *ex ante* regulation, it being imposed prospectively to regulate future conduct on the market.

OFCOM also has a general power, under Section 185 Communications Act 2003, to resolve disputes between *inter alia* two telecommunications providers ('OFCOM's Dispute Resolution Powers'). In resolving a dispute, it has power to '*give a direction fixing the terms or conditions of transactions between the parties to the dispute*' (Section 190 Communications Act 2003). Such regulation is termed *ex post* regulation, it being imposed retrospectively to address conduct on the market which has already occurred.

## The appeal

The issue in this case was whether OFCOM was correct in determining that H3G had SMP in the market for MCT on its network. Although H3G is a monopoly seller of MCT on its network, it would not necessarily have SMP in that market, as it is possible that the buyer of its service (in this case, BT being overwhelmingly the largest buyer) might have sufficient power to counterbalance any power that H3G might otherwise be able to exercise (called 'countervailing buyer power', or 'CBP').

The Tribunal had held<sup>1</sup> that OFCOM had been correct to find, in its decision, that H3G had SMP and that price controls should be imposed. Although BT was a knowledgeable and price sensitive purchaser, it did not have sufficient CBP to negate the SMP that H3G enjoyed as a result of its 100% market share.

H3G appealed (with permission from the Tribunal) against the Tribunal's decision on three grounds:

- (1) The Tribunal was wrong to conclude that BT's obligation to permit interconnection with its network was not such as to negate H3G having SMP, because BT's obligation was only to purchase interconnection at a reasonable price. H3G could not require BT to pay a price for MCT that was appreciably above the competitive level, and it could not therefore behave independently of BT. This was sufficient to negate H3G having SMP;
- (2) The Tribunal was wrong to disregard OFCOM's Dispute Resolution Powers in determining whether H3G had SMP, because if BT were to dispute the price that H3G tried to charge for MCT, OFCOM would resolve the dispute by setting a price that reflected the competitive level. This also prevented H3G acting independently of BT in setting prices, and was sufficient to negate H3G having SMP;
- (3) The Tribunal was wrong to conclude that OFCOM could impose price controls, because even if H3G did have SMP there was no risk of it setting an excessively high price for MCT.

## The 'Modified Greenfield Approach'

The Court upheld the Tribunal's conclusions that BT's obligation to permit interconnection with its network only on reasonable terms was not such as to negate H3G having SMP, and that OFCOM's Dispute Resolution Powers should be disregarded in assessing H3G's SMP. OFCOM, supported by T-Mobile (UK) Limited who intervened in the case, argued that if these factors were such as to prevent H3G acting independently of its customers, then that would mean H3G could never be found to have SMP. The *ex ante* obligation imposed on BT would always be qualified (it being a requirement of Article 5(3) Access Directive<sup>2</sup> that the obligation be '*proportionate*') and OFCOM's *ex post* regulatory powers would always be available. Moreover, it was unlikely that any other MNO could ever be found

<sup>1</sup> *Hutchison 3G UK Ltd v OFCOM* [2008] CAT 11

<sup>2</sup> Directive 2002/19/EC

to have SMP on its mobile telephone network. The conditions for imposing *ex ante* regulation on those with SMP could never be met, and OFCOM would lose its ability *inter alia* to impose price controls in this market. The Court accepted this argument.

In doing so it followed Commission Decision DE/2005/0144 regarding call termination on fixed telephone networks in Germany. There, the Commission had rejected an argument from the German regulator that Deutsche Telekom had sufficient CBP to negate any SMP of the other network operators. It held that the 100% market share of operators '*raises a strong presumption of SMP, save in exceptional circumstances which need to be clearly and unambiguously demonstrated by the NRA [National Regulatory Authority]*' (at paragraph (17)). Deutsche Telekom's obligation to interconnect had to be taken into account, because the other network operators' SMP resulted from their 100% market shares, not from Deutsche Telekom's obligation to purchase interconnection from them – as such, there was no circularity if the interconnection obligation were taken into account.

The Commission's decision was a precedent establishing the application of the 'modified Greenfield approach'. The Court defined this as '*an analytical approach which is intended to avoid circularity...by requiring regulation to be ignored which would otherwise distort inappropriately the answer to the enquiry whether a network operator has SMP.*' (Etherton L.J. at paragraph 92). It interpreted the Commission's decision as requiring that if consideration of a particular regulatory obligation would mean SMP is negated, such that no undertaking in the market could ever be found to have SMP because of the existence of that regulatory obligation, then that obligation is to be disregarded. It would, the Court held, be '*self-defeating*' (Lloyd L.J. at paragraph 61) to do otherwise. It would also be contrary to the objectives of the European Common Regulatory Framework<sup>3</sup> for the telecommunications sector, as it would prevent the *ex ante* regulation of those with SMP that is clearly intended by that Framework (Etherton L.J. paragraph 99).

The Court therefore accepted that although the availability of these powers, and the threat of *ex post* regulation, may be a constraint on H3G's freedom of action, because any attempt to charge unreasonably high prices could be referred to OFCOM, nonetheless they were not relevant to assessing SMP.

On that basis, the Court upheld the Tribunal's finding that H3G had SMP. H3G's 100% market share gave rise to a strong presumption of SMP, and there was nothing in this case to displace that presumption. The Tribunal had found there were commercial constraints on BT requiring it to interconnect with H3G, which existed irrespective of the regulatory framework and which undermined any potential finding of CBP on the facts (Lloyd L.J. paragraph 71; Etherton L.J. at paragraphs 102 and 104). The Court upheld those findings as '*The Tribunal is a specialist and highly qualified body, this court would be very slow to interfere with its findings of fact*' (Etherton L.J. paragraph 107).

The Court rejected H3G's argument that it lacked SMP because the obligation for BT to purchase interconnection from it was qualified, requiring BT only to do so on reasonable terms. It noted that the same argument had been advanced to the Commission by the German Regulator, and although the Commission had not given reasons for rejecting that argument, clearly it had been rejected. It also rejected H3G's argument that the Dispute Resolution Powers were, like the obligation to interconnect, obligations existing independently of a finding of SMP. Although the argument was '*fairly made, so far as the express reasoning of the Commission is concerned*', nonetheless the Court preferred to decide the case on the basis of the actual decision, which was clearly analogous on the facts as found by the Commission and the Tribunal respectively, '*regardless of what might be deduced from one or another phrase or sentence in the expression of the Commission's reasoning*' (Lloyd L.J. paragraph 67).

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<sup>3</sup> Relevant parts of which, for the present case, were Directive 2002/21/EC, the Framework Directive; Directive 2002/19/EC, the Access Directive; and Directive 2002/20/EC, the Authorisations Directive

## OFCOM's ability to set a price appreciably above the competitive level

A separate issue arose as to whether, if the Dispute Resolution Powers were to be brought into account, the Tribunal erred in accepting OFCOM's argument that, when resolving a dispute over charges for connectivity, it had the power to impose charges that were appreciably above the market level. Although it was not necessary to determine this issue, the Court did express some disquiet about the Tribunal's conclusions. Lloyd L.J. indicated he saw '*a good deal of force*' in the argument (paragraph 72), and Etherton L.J. that he was '*inclined to agree*' with it (paragraph 110). However, notwithstanding the Court could '*see that it is an important point*', it declined to decide it.

## OFCOM's imposition of price controls

H3G's third ground of appeal was rejected. The Court held that the conclusion that H3G had an incentive to charge excessive prices was one which was open to the Tribunal on the facts.

## Conclusions

The outcome of the Court's judgment appears to be that a regulatory obligation applicable to the undertaking with putative SMP will not be taken into account as negating SMP, as to do so will always lead to circularity. A regulatory obligation applicable to the undertaking with putative CBP, however, may be taken into account, since CBP as a matter of fact may be demonstrated in other ways (for example, commercial interests/constraints) and the regulatory obligations of this undertaking do not arise from the putative SMP of the other undertaking. There is therefore no circularity in this latter scenario. It remains to be seen, however, whether the judgment provides sufficient guidance on which obligations will and will not result in 'circularity' for the purposes of the SMP assessment, and whether the issue will resurface in cases where the facts are less squarely on all fours with the Commission's decision.

The Court's conclusions also follow the trend that has emerged in several of its recent judgments about how it will approach second appeals from specialist Tribunals. Its decision not to determine the issue of whether OFCOM could set prices for MCT appreciably above the competitive level, notwithstanding it appears their Lordships thought H3G's arguments were correct, reflects the strong exhortation in the *Floe Telecom* case<sup>4</sup> not to determine matters that are not very strictly necessary for the resolution of the dispute. The decision not to interfere with the Tribunal's findings on whether BT had CBP, and whether there was a risk of H3G charging excessive prices, reflects the deference which the Court indicated most recently in the '*Pringles*' case<sup>5</sup> (an appeal from the VAT & Duties Tribunal concerning the VAT treatment of 'Pringles') it would show for factual assessments reached by specialist Tribunals. The judgment may be considered a reinforcement of these emerging trends, and confirmation of how one may expect appeals from specialist Tribunals to be dealt with in future.

Peter Roth QC and Josh Holmes appeared for OFCOM, and  
Jon Turner QC and Meredith Pickford appeared for T-Mobile UK Limited.

**For more information on Peter Roth QC, Jon Turner QC, Josh Holmes, Meredith Pickford and Laura Elizabeth John please contact the Clerks on 020 7405 7211 or consult the 'Find a Barrister' Section at [www.monckton.com](http://www.monckton.com).**

<sup>4</sup> (1) *Office of Communications*, and (2) *T-Mobile UK Ltd v Floe Telecom Ltd (in liquidation)* [2009] EWCA Civ 47

<sup>5</sup> *Commissioners for Her Majesty's Revenue and Customs v Procter & Gamble* [2009] EWCA Civ 407