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Dear Siobhan

**OFCOM AIRTIME SALES REVIEW CONSULTATION, MARCH-JUNE 2010
THE ADVERTISERS' VIEW**

INTRODUCTION

As the representative membership body for British advertisers, ISBA has been closely involved with successive regulatory inquiries into various aspects of the UK's media markets over the long term.

Of particular relevance is the assistance we have given Ofcom, the Office of Fair Trading and The Competition Commission over the past 18 months in their reviews of the Contract Rights Renewal competition remedy which governs the pricing of commercial airtime on ITV1.

ISBA exists to protect and enhance its members' freedom to advertise, and to do so economically. We have therefore argued, and will continue to argue, for free and effective competition between the media for advertisers' budgets.

The response set out below follows the question format of Ofcom's consultation as closely as possible, though some responses inevitably span more than one question.

GENERAL COMMENTS

Having considered the issues at hand at some length with our members over the past year, **we do not support Ofcom's recommendation to lift the withholding and conditional selling rules.**

We understand the reasons that Ofcom sets out for their removal, but believe that Ofcom has misjudged/underestimated the potential consequences for advertisers from certain broadcasters' manipulation of airtime inventory in order to influence pricing and thus revenues. We believe that the deregulatory thrust which Ofcom is following in this respect is not proportionate to the potential detriments.

We note the extension (from the original deadline of June 8 to the revised date of June 21) offered to give respondents time to consider Ofcom's 'Econometric Analysis of the TV Advertising Market: Final Report, dated May 21, 2010. We have attempted to give this report some early consideration in this response, though its sheer volume (131 pages), its highly-technical nature and the language it is couched in make this difficult.

That said, we are encouraged by what we believe to be its key findings, which reflect our views :

- That a positive relationship exists between the SOCI for a channel and its advertising impact price (reflecting the market power which attaches to large audiences)
- That demand for advertising appears flexible (i.e. inelastic, as defined in the report)
- That demand for programming by viewers is highly inelastic, and changes in advertising minutage will not lead to substantial changes in viewing habits (which brings into serious question the fuss that has historically accompanied any discussion of upward changes to advertising quota limits).

However, we do not believe that the report contains anything which causes us to alter our position with regard to the airtime sales rules under consideration in this consultation.

RESPONSES TO THE CONSULTATION'S SPECIFIC QUESTIONS (**SHOWN IN RED**)

Question 1: Do you agree with our description of the key developments in the TV advertising market since 2003?

Question 2: Do you think we have missed any other recent market developments or trends relevant to competition in the advertising sector?

To Q1, broadly, yes, and we congratulate Ofcom on the thoroughness of certain aspects of its review. To Q2, however, we are concerned that certain other important aspects of broadcaster behaviour appear not to have been given adequate consideration.

We would draw particular attention to developments, realised and potential, in the airtime sales landscape.

Sky Media absorbed Viacom Broadcasting Solutions airtime sales in late 2009 and in June 2010 acquired the airtime sales contract for Virgin Media channels. Sky and Channel 4 also reached heads of agreement for a merger of their airtime sales operations in the event that the CRR undertakings governing ITV were (or still might be) relaxed or overturned.

ITV acquired the final 25% stake in GMTV from Disney in 2009 and is expected to consolidate GMTV's airtime sales fully by 2011. Rumours also continue to persist surrounding M&A activity between ITV and Five's owners RTL. Having spent much of the past decade arguing successfully for regulatory controls over an ITV which represents nearly half the airtime sales market, ISBA's position with regard to a possible merger of ITV and Five is self-evident – we would have no hesitation whatsoever in calling regulators to refer it to the Competition Commission.

Meanwhile, the market generally considers Five's and IDS' positions as standalones relatively weak (especially as the latter will henceforth represent only UKTV's channels).

In short, consolidation in airtime sales is happening and we anticipate that it will continue. Some potential consolidations would, in our view, necessitate extensive scrutiny from competition regulators. *All would be predicated on the promise of improved margins of the merged entities, achieved in large part by increased leverage in the market for airtime sales which comprises the large majority of commercial (free-to-air channels') revenues.*

Question 3: Do you agree that SOCI is a key determinant during contract negotiations - that media buyers are more interested in committing expenditure to broadcasters which have increased their SOCI?

SOCI has clearly become an important determinant factor in commercial television airtime contract negotiations, but it is by no means the only consideration. A broadcaster's, and more importantly a channel's, reach, audience profile¹ and coverage of particular target groups are as important.

¹ *Reach* – the number of people a channel reaches, typically measured over a week, hence 'weekly reach', usually expressed as a percentage of the population

Profile – the composition of a channel's audience, whether up- or downmarket, older or younger, male/female bias, etc.

Coverage – the proportion of any particular target audience which a channel reaches, again typically expressed as a percentage. This not the same as SOCI, which is a gross measure of the total number of impacts, or advertising contacts,

Question 4: Do you believe internet display advertising could increasingly act as a constraint on TV advertising (i.e. become a closer substitute) in the next 3-5 years?

No, we concur with Ofcom's conclusion at and around the consultation's point 4.68. The Competition Commission also found similarly in its recently-concluded review of CRR. We do however, see internet advertising continuing to emerge as a compliment to many forms of offline advertising.

Question 5: Is there any other relevant evidence we should consider in order to examine the ongoing need for the withholding rule?

Question 6: Do you agree with our conclusions that the commercial analogue broadcasters do not appear to have strong incentives to withhold airtime? If not, why?

We understand Ofcom's thinking and reasoning, but are concerned that it is giving objective of deregulation disproportionate importance with respect to the whole picture.

We submit this response as the acknowledged representative body of the advertiser customers of the broadcasters who fund the majority of the medium; as respondents to this and many other consultations; but perhaps most critically as the organisation most likely to be making representations to Ofcom and other regulators if and when things do not go as planned or imagined in future.

Critical to this last point is burden of proof. Broadcasters are currently held to account against the current rules by Ofcom. Their removal shifts the burden of proof, most likely almost entirely onto advertisers. Such a significant shift would in our view be both unwarranted and unacceptable.

As we have observed in a number of our previous responses, our extensive experience is that Ofcom and other interested regulators, for example the OFT, cleave to their consumer protection roles. They tend not to incline to engage with our constituency whose concerns are usually and necessarily of a business-to-business nature.

To the specific question - and very much in line with our responses to Ofcom, OFT and the CC through the CRR review process - we do not subscribe to the view implicit throughout this consultation that because broadcasters do not currently withhold airtime, they will not do so if allowed to in future through the removal of the withholding rules.

ISBA understands that many of the Independent CRR Adjudicator's informal interventions have concerned the conditional selling of ITV's family of channels. Ofcom of course has the necessary access to confirm this understanding.

which a channel delivers. Whilst it relates loosely to SOCI, it is by no means directly proportional to SOCI. A channel with smaller SOCI but greater diversity of programming and viewing can deliver relatively high coverage – Channel 4 (and BBC2) are perhaps the most obvious examples.

Perhaps Ofcom envisages some enhancement to the role of the Independent Adjudicator's Office which oversees ITV1 Contract Rights Renewal to address this major concern?

Nor do we agree that the economic argument to deregulate is either clear-cut or convincing. We believe there are potentially real economic incentives for the owners of the most important airtime assets – particularly ITV and also Channel 4 – to restrict access to key slots by restricting their supply.

We and some of our members with long memories can still remember when commercial broadcasters withheld airtime in order to raise pricing. (We have already cited some specific historical examples in our discussions with Ofcom staff).

Our position has been consistent over the long term – that **all key broadcast assets should be made available for sale as prevailing minutage rules permit, thereby allowing the market to 'clear' at its natural price, not at a constrained or enforced price.**

The current, pre-existing rules accommodate this well. They do not apply to the stations with 'long tails of inventory which commands very low, possibly unmeasurable, audiences which are sometimes unsaleable at a viable (ie covers costs, delivers profit) rate.

They do – and we argue strongly they should continue to – apply to the legacy 'terrestrial PSB' stations. Their early entry, long standing, near-universal distribution and prime positions on receivers and electronic programme guides given them enduring natural advantages in attracting sizeable audiences. As a consequence their inventory is made up of highly-saleable airtime, sometimes entirely and always at least in large enough part to make withholding rules necessary going forwards. We fully understand why broadcasters would like Ofcom to conclude that sufficient economic incentives are in place to prevent price-rigging through withholding, but we do not share this view.

Whilst we understand that the current rules dissolve at full digital switchover, we do not believe that the underlying issue the rules seek to prevent dissolves at that time. Rather the key issue is as ever one of market power.

It is widely acknowledged that key broadcast assets are hard-earned, volatile and often quite unpredictable. It follows that they are therefore also scarce. Their relative scarcity is one of the sources of their owners' dominant market positions, alongside legacy acquisition and distribution advantages.

We believe that the dominant players of today are very likely to hold those positions for the foreseeable future, certainly beyond digital switchover. Broadcaster dominance and market power remain a key source of ongoing advertiser concerns.

The Competition Commission's Final Report on its review of Contract Rights Renewal, published on May 12, 2010, recognised this and concluded that CRR should remain in place but be varied to include exact but timeshifted (eg +1 hour) and high-definition (HD) replica channels.

ITV has expressed its disappointment with this outcome very publicly. It is our firm belief that ITV will redouble its efforts both to minimise the consequences arising from CC's decision by stepping up its efforts to 'massage' and leverage its airtime sales in any way possible. The primary means of doing this which are primarily available to the holders of key broadcast assets : withholding of airtime, conditional selling and manipulation of amount and scheduling of advertising ('COSTA').

(All are subject to Ofcom review during 2010, and we also note Ofcom's May 25th publication of its independent econometric study of the demand for TV advertising, outline of the next steps in its review of current rules on the amount of advertising permitted on television).

We are concerned by the sense conveyed through this substantial consultation document that Ofcom does not appear fully to recognise or acknowledge the linkages between the market's various component workings – notably sales rules, amount and scheduling of airtime, and market leverage (eg CRR). Advertisers and their media agencies clearly understand and believe in these interconnections.

This contrasts with the Competition Commission's clear and welcome grasp of the market's operation. We note that it reiterated its 2003 call for a market review in its May 2010 Final Decision on CRR.

Ofcom is already aware from meetings we have had that we are curious as to why it is reviewing each of the market's components so separately. Nevertheless, we remain prepared to respond to its forthcoming consultation on the 'amount and scheduling' component and the attendant econometric analysis which we understand will accompany it. The theme of our response to that will be pragmatic, supportive and consistent with this one and with our previous submissions, namely :

- that the key issue is market power
- that some broadcasters, notably ITV, continue to retain a level of market power sufficient to allow leverage of a dominant position
- that the amount of advertising sold by all broadcasters should now be harmonised but that any outcome should be 'impact neutral' – in other words, it should not constrain the amount of audience which advertisers can access on aggregate, thereby not distorting fair market pricing

Question 7: Is there any other relevant evidence we should consider in order to examine the ongoing need for the conditional selling rule?

Please see our comments above. Although we acknowledge that the overall landscape has changed significantly, we submit that the tendencies and behaviours of existing and/or putative dominant players have not.

Question 8: Do you agree with our view that there can be both positive and negative effects from bundling (including conditional selling), which means there should not be a blanket ban on conditional selling?

In principle, yes, but in practice, seldom. It is a fact of commercial life that sellers will attempt to leverage their market position to extract the highest revenues from their strongest assets, and manage access to their strongest assets to drive higher revenues for their other assets. Similarly, buyers will seek to mitigate these attempts.

Once again, we believe the issue comes down to market power, and we understand from our competition advisers that successful bundling is one of the most common manifestations of market power.

The current conditional selling rules have relatively little impact on owners of relatively weak assets (as they do not have strong assets against which to leverage the sale of weaker ones).

We submit that the rules have very strong constraining effects on the owners of strong assets who would otherwise leverage their dominance to commercial advantage. We are pleased that the CRR decision will lead to the continuation of the presence of the Independent Adjudicator (CRR), one of whose key roles is to prevent conditional selling being practiced by ITV.

As the number of ways broadcasters can offer advertisers seeking to reach viewing audiences grows, we argue not only that rules to prevent conditional selling should be maintained, but that they should be *extended* to embrace other forms of commercial on-air activity.

Broadcasters – and we understand ITV in particular – not only offer the best trading terms to the advertisers and agencies with whom they enjoy the best trading terms. They also offer them first option on any major/prime sponsorship opportunities. With the current relaxation of regulations, we expect this behaviour to extend to prime paid product placements in the near future. This is also a form of conditional selling, as it involves the leveraging of strong market position for both spot advertisements and prime content asset associations.

Question 9: Do you agree with our proposals to lift both the withholding rule and the conditional selling rule?

No to both.

Question 10: Alternatively, if you think the ASRs should be retained in their current or an amended form, what is your reasoning for this view and, if relevant, how should they be amended?

In ISBA and its members' considered view, rules pertaining to both withholding and conditional selling continue to be necessary for three reasons :

- 1 They have proved durable, flexible, proportionate and effective
- 2 They have addressed a key potential detriment, and would continue to do so
- 3 They are not broken beyond the technicality of their expiry in 2012/3

The very real concerns we have highlighted in this response will continue to prevail for the foreseeable future. We therefore believe strongly that the airtimes sales rules should :

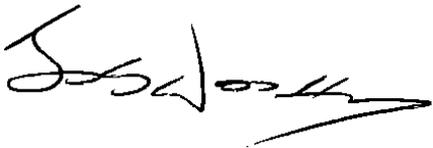
- continue to remain in place
- be refreshed so as not simply to expire at digital switchover, and
- be extended to embrace the new commercial opportunities available to broadcasters and advertisers.

CONCLUSION

For the many substantial reasons set out in this response, **ISBA believes that the withholding and conditional selling rules should not only be maintained but extended** to remain as relevant in a future where we believe they will clearly be needed.

We would be happy to provide further information or comment as required.

Yours sincerely



Bob Wootton

Director of Media & Advertising