

ANNEX 6: SKY'S RESPONSE TO SECTION 12 (REMEDIES – CONTENT RIGHTS) OF THE CONSULTATION DOCUMENT

A. Introduction

- A6.1 In Section 12 of the Consultation Document, Ofcom advocates two “*targeted interventions*”¹ into the way that premium content rights are sold, to address specific concerns which relate to SVoD movie rights² and the next Premier League auction and which, according to Ofcom, would not be addressed by the proposed wholesale must-offer remedy.
- A6.2 Although Ofcom may seek to portray these as interventions designed to address effects that it believes arise from Sky’s alleged market power – citing high wholesale prices and the restricted exploitation of SVoD movie rights – it is clear from Ofcom’s discussion that its goal is to eliminate Sky’s alleged market power, and that it would not be satisfied by simply preventing any detrimental effects that might stem from that market power. This is both inappropriate and outside Ofcom’s statutory remit.
- A6.3 Both interventions would seek to change the way in which rights owners exploit their rights. More specifically, both would fetter rights owners’ abilities to grant exclusive rights. Exclusivity of content is a cornerstone of competition in audiovisual services, providing a key means by which broadcasters and other service providers are able to differentiate their services from those of their competitors and thereby attract and retain viewers (and subscribers, in the case of pay TV services).³ Intervention with regard to exclusive content would, therefore, undermine the basis on which the industry operates.
- A6.4 Ofcom advocates these interventions despite acknowledging that regulators should be very cautious about intervening to change how firms exploit content rights due to the significant risk of stifling innovation.⁴
- A6.5 Below we explain why the alleged concerns that motivate Ofcom’s proposed interventions are baseless. In addition, Ofcom’s proposals raise serious risks of unintended consequences, which Ofcom has failed to recognise.

B. SVoD movies rights

- A6.6 The first “*targeted intervention*” would affect the way in which movies rights are sold. Ofcom proposes the introduction of a requirement to make movies “*SVoD rights*” available separately from “*the linear channel rights*”, possibly

¹ Paragraph 12.5 of the Consultation Document.

² In the case of SVoD movie rights, the implementation of the changes envisaged could require action on the part of the Competition Commission.

³ Exclusive rights to show content are recognised as inherent and legitimate characteristics of the TV industry: see Case 262/81 *Coditel SA v Cine Vog Films (No 2)* [1982] ECR 3381 at [15]-[16].

⁴ Paragraph 12.20 of the Consultation Document. However, Sky does not accept Ofcom’s claim that its proposed downstream intervention involves less risk to innovation.

accompanied by a further rule that the same firm cannot buy “*both sets of rights*”.⁵

A6.7 Ofcom apparently believes that intervention along these lines would remedy two specific concerns:

- (a) its concern that what it sees as Sky’s restricted exploitation of SVoD rights is holding back innovation in the development of VoD services;⁶ and
- (b) its concern that Sky is earning high wholesale margins on its movie channels, which are likely to be mirrored in high retail prices.⁷

As we have already shown in **Sections 6, 7 and 8** of this Response, there is no cogent evidence to support either of these concerns.

A6.8 Ofcom’s very narrow focus on the availability of movies specifically on a SVoD basis within the pay TV window ignores the reality that consumers are well served by numerous realistic options for viewing movies. The fact that some movies may not be available as part of a SVoD service on some or all TV platforms during the pay TV window does not amount to real consumer detriment. As already noted in this Response,⁸ a multitude of other services show the very same movies that Sky broadcasts, both before and after the fifteen-month period during which they are available on Sky’s movie channels; and at any point in time a substantial number of titles (whether first-run or library) are available for inclusion in other SVoD services. On any rational assessment, therefore, the magnitude of the harm that Ofcom is targeting is insufficient to justify the level of intervention envisaged.

A6.9 Notwithstanding our view that Ofcom’s concerns are baseless, we comment below on the intervention that Ofcom envisages.

A6.10 Ofcom would apparently have “*remaining concerns*” about high wholesale margins on Sky’s movies channels specifically⁹ even after implementation of a compulsory licensing obligation of the kind described in the preceding sections of the Consultation Document, presumably because of Ofcom’s belief that Sky generates higher wholesale margins on its movies channels than on its sports channels. Regardless of our view that there is no evidence that Sky’s wholesale margins are high, Ofcom has failed to explain why the proposed wholesale must-offer remedy would not sufficiently address its concern regarding high margins: the new maximum wholesale prices that Ofcom proposes would necessarily substantially reduce Sky’s wholesale margin.

⁵ Paragraph 12.29 of the Consultation Document.

⁶ Paragraphs 12.15, 12.17, 12.21 and 12.28 of the Consultation Document.

⁷ Paragraphs 12.16, 12.19, 12.22, 12.24, 12.26 and 12.28 of the Consultation Document.

⁸ See **Sections 8, 9 and 10**.

⁹ Paragraph 12.24. of the Consultation Document.

- A6.11 Ofcom recognises that *“the current distribution of rights arises from unilateral decision-making by the individual studios”*.¹⁰ The overall structure reflects the windows system which the studios have implemented (in a broadly similar form) across Europe and thus is certainly not peculiar to the UK. It is the business model which the studios have devised to maximise their revenues from these rights. Ofcom is proposing that the studios should be required to make material changes to this business model.
- A6.12 As already noted, Ofcom’s proposal for intervention would involve, at a minimum, a requirement on the movies studios to make rights to exploit first-run¹¹ premium movies on a SVoD basis available separately from rights to show the same content on a linear channel in the pay TV window. This approach would appear to reflect Ofcom’s view that the current way in which rights in the pay TV window are sold involves *“different types of rights being sold together by the Major Hollywood Studios to Sky – in particular SVoD and linear rights”*;¹² elsewhere, Ofcom says that the studios *“bundle [SVoD rights] with the rights to show movies on subscription linear channels and these bundled rights are acquired on an exclusive basis by Sky”*.¹³ What Ofcom does not seem to appreciate is that these are not, in fact, two sets of rights; rather, the studios each license a single right for the pay TV window – the exclusive right to show first-run movies during that period. Consistent with this, as Ofcom is aware,¹⁴ **[CONFIDENTIAL]**.
- A6.13 Sky’s understanding, from its dealings with the studios, is that the studios package their rights as they do so as to control the degree of exposure of their titles in the pay TV window and thus protect their value for subsequent windows. In Sky’s experience, the studios are particularly concerned about over-exposure via SVoD services and the effect that this could have on the value of titles later in their life cycle.
- A6.14 It is incorrect to characterise Ofcom’s proposal as requiring two products previously sold as a bundle to be sold separately in the future; rather, the studios would be prevented from selling exclusive rights for this window. This would fundamentally change the nature of the rights sold. Ofcom’s proposal amounts to an attack on exclusivity and the windows system.
- A6.15 Ofcom is also wrong to think that this remedy brings with it a relatively low risk of unintended consequences.¹⁵
- A6.16 Ofcom is clearly misguided if it believes that the sale of movie rights for a per subscriber fee (rather than a fixed price, as for sports rights) means that *“a reduction in exclusivity should not have the same effect on that fee”* as it would do

¹⁰ Paragraph 12.31 of the Consultation Document.

¹¹ ‘First-run’ refers to the first run **in the pay TV window**: such movies will normally already have been exploited on PPV and VOD.

¹² Paragraph 12.26 of the Consultation Document.

¹³ Paragraph 6.148 of the Consultation Document.

¹⁴ Figure 57 of the Consultation Document.

¹⁵ Paragraph 12.30 of the Consultation Document.

in the case of sports rights which are sold for a fixed price on the basis of cross-platform exclusivity.¹⁶ Indeed, Ofcom appears to believe that removing wholesale exclusivity could in fact generate greater subscription revenues because it could result in a greater number of subscribers.¹⁷ Ofcom's view is that this intervention would generate downward pressure on Sky's wholesale prices; it should, therefore, recognise that there is a clear possibility that removing exclusivity would result in a lower per subscriber wholesale fee and that any increase in subscriber numbers during the pay TV window might not compensate for that reduction in the per subscriber wholesale fee, leaving the studios in a worse position.

- A6.17 In Sky's view, at least two factors would tend to exert downward pressure on the value of the 'linear rights' if separate 'SVoD rights' were made available. The first is obviously the like-for-like competition to which the relevant linear channels would be exposed (in addition to the wider competition which they already face from other means of consuming movies, including other movies services and DVDs).¹⁸ The second is a loss of flexibility to innovate. The current scope of the pay TV rights, which affords the possibility of offering content both on linear channels and via VoD services, allows their holder to offer a movies service which offers consumers a choice of ways to access movies; a broadcaster permitted to exploit rights only on linear channels would no longer be in that position, and would reduce its valuation of the rights accordingly.
- A6.18 Ofcom has also ignored the fact that, for the reasons referred to in paragraph A6.13 above, rights will be worth less in the free window if they have been more exposed in earlier windows.
- A6.19 Ofcom should ask itself the following question: if it is true that a different distribution arrangement on the lines proposed would not risk reducing rights fees and might even increase them, why are the studios not already selling their rights in this way? The studios are undoubtedly better placed than Ofcom to judge how best to maximise the value of their rights.
- A6.20 Furthermore, in reaching its conclusion that the risk of consumer inconvenience from the changes proposed is low, Ofcom appears not to consider the possibility that linear and SVoD services might not both be made available on all platforms. Nor does Ofcom seem to appreciate that there is a real risk that intervention would substantially increase the cost to consumers of receiving both services. Absent intervention, [CONFIDENTIAL]¹⁹ [CONFIDENTIAL]; whereas, under Ofcom's proposal, consumers wanting to have the choice of viewing the content both on linear channels and on a SVoD basis would potentially have to pay for two services.

¹⁶ *Ibid.*

¹⁷ *Ibid.*

¹⁸ In this regard, the rights are no different to sports rights – the reduction in exclusivity reduces the value of the linear rights.

¹⁹ [CONFIDENTIAL] movies content is already available to DTH subscribers on a SVoD basis via Sky Anytime.

- A6.21 Finally, we note that this is not, in any event, a suitable candidate for a market investigation reference to the Competition Commission. Recourse to the market investigation regime is inappropriate for such a limited single issue, where the perceived mischief is so small. If Ofcom does proceed to consult formally on a reference, Sky will make more detailed representations.

C. Premier League rights

- A6.22 Ofcom's proposal to intervene in the way in which Premier League rights are bought and sold is, again, motivated by its desire to address the perceived existence of market power. Sky has explained in previous submissions to Ofcom during the course of its market investigation²⁰ why Ofcom's conclusion that Sky has market power in the wholesale supply of "*Core Premium Sports channels*" continues to be wrong. Furthermore, there is no evidence that Sky's exploitation of the rights to the content included in its sports channels, including Premier League rights, harms competition.
- A6.23 Ofcom notes that the binding commitments given by the Premier League to the European Commission, which covered the last two auctions of Premier League media rights, will not apply to the next such auction, and states its intention to "*review with the FAPL how it intends to ensure that the 2012 auction complies with competition law*".²¹
- A6.24 When the Second Consultation Document was published, Ofcom was of the view that it was not a suitable time to intervene in the way Premier League rights are sold. Now Ofcom apparently considers that it is in a better position to assess the effect of the EC commitments, but its characterisation of those effects exaggerates the benefits of the Commission's intervention while substantially downplaying the consumer detriment caused. Ofcom claims that the EC commitments "*have facilitated the entry of Setanta into the market, and the development of new retail packages, in particular entry-level packages on non-Sky platforms*"²²; in fact, Setanta was already a broadcaster and retailer of premium channels prior to the first auction covered by the EC commitments, and it is unclear on what basis Ofcom attributes the development of 'new retail packages' (whatever these are) to the EC commitments. On the negative side, Ofcom states that "[p]artially offsetting [the benefits Ofcom attributes to the EC commitments], *some existing consumers on Sky's satellite [sic] have had to purchase an additional subscription ... in order to continue being able to view all the FAPL matches*"²³ – in fact, **all existing and new** consumers on the DTH platform had to purchase a Setanta subscription in addition to a Sky subscription in order to view all the Premier League matches.

²⁰ See Sky's Responses to the First and Second Consultation Documents and Sky's submission, "*Additional comments on Ofcom's analysis of market definition and market power in the pay TV review*", of 1 June 2009.

²¹ Paragraph 12.39 of the Consultation Document.

²² Paragraph 12.40 of the Consultation Document.

²³ Paragraph 12.40 of the Consultation Document.

- A6.25 Ofcom then turns to the subject of Setanta's recent demise, observing that *"the consumer benefits which have resulted from Setanta's entry into the market have not proved to be sustainable"*.²⁴ Ofcom cannot take Setanta's financial difficulties as evidence that the EC commitments did not go far enough (which appears to be the implication²⁵). The reasons for Setanta's demise have been widely discussed and reported and many factors have been cited, one of which is its decision to pay substantially more for several important sets of rights than had been paid in the past.²⁶ Setanta's failure has also been linked to the credit crunch which caused its sources of funding to dry up.²⁷
- A6.26 Setanta was not alone in believing that it is sustainable to build a channel based on a sub-set of Premier League rights; ESPN clearly considers that it will be able to exploit the Premier League rights that it has acquired for the current and next contract periods successfully and build a profitable channel.²⁸
- A6.27 Ofcom's assessment of the effects of the EC commitments is not, therefore, a sound foundation from which to consider what commitments (or other intervention) might be suitable in respect of future sales of Premier League rights.

²⁴ *Ibid.*

²⁵ See, for example, paragraph 12.42: *"We would expect to take this evidence into consideration when considering any new set of commitments"*. We note that Ofcom goes on, in the same paragraph, to state: *"We emphasise however that this does not mean that our objective in considering any new commitments would be to intervene more aggressively in order to ensure the success of a successor to Setanta. Rather we would consider as a national competition authority whetherthe collective selling arrangement... distorts competition contrary to Article 81(1)"*. It is telling that Ofcom feels the need to clarify its approach in this way; any intervention that would **ensure** such success would have to be extreme and clearly inappropriate.

²⁶ For example, in 2008 Setanta agreed to pay £125 million for Scottish Premier League ('SPL') rights for four seasons from 2010/11 onwards; this was double the amount that it paid for the rights under its preceding four-year deal with the SPL. Setanta also agreed to pay £150 million for its share of Football Association (FA) Cup rights for four years, with the FA reporting that the price paid, by Setanta and ITV together, was a 42% improvement on its previous deal with the BBC and Sky (FA Press release, 30 March 2007).

²⁷ See *The Telegraph*, 25 June 2009 (<http://www.telegraph.co.uk/finance/comment/5626456/Setanta-leaves-the-field-but-its-game-on-for-Disney-owned-ESPN.html>)

"The Setanta model and approach was in many ways flawed. Setanta's business model only worked when money was available - in other words, not in a recession. Its private-equity backers had a lot of money in good times, but circumstances appear to have changed when the credit crisis hit." ...

"Setanta's business model was not the most secure, but if the group had made the right decisions and not paid too much for less prominent sporting events, it may have had a chance."

²⁸ Those who shared this view include analysts at UBS who stated:

"If anything, ESPN's willingness and ability to acquire rights highlights that Setanta's failure was a function of it paying too much and acquiring too many rights rather than the presence of Sky"

(quoted in *The Telegraph*, 25 June 2009: <http://www.telegraph.co.uk/finance/comment/5626456/Setanta-leaves-the-field-but-its-game-on-for-Disney-owned-ESPN.html>).

- A6.28 More concerning, however, is Ofcom's approach to the question of what intervention on its part would be appropriate given the upcoming expiry of the EC commitments. Ofcom states that it will consider whether the Premier League's collective selling arrangements restrict competition contrary to Article 81 (1) and Chapter 1 of the CA98 "*based on evidence of developments in the market*",²⁹ which would, indeed, be the correct starting point for Ofcom's assessment of whether intervention under its general ex post competition law powers is appropriate.³⁰ It is clear from the discussion that follows this statement, however, that Ofcom is not, in fact, starting from this position.
- A6.29 Ofcom's approach is procedurally unsound. It apparently already holds well-developed views not only on whether intervention is needed, but also on the detailed form that such intervention should take³¹ - despite the fact that it has not yet undertaken an analysis within the proper competition law framework (or at least has not put any such analysis forward for consultation).
- A6.30 Before it can properly form a view on the nature of any intervention that might be required, Ofcom must first conduct a proper competition law analysis to identify whether the collective selling arrangements fall within Article 81(1), and, if so, whether Article 81(1) is inapplicable by virtue of Article 81(3) - it cannot simply assume that it already knows the answer. Then if, having conducted a proper analysis as to the scope of any problem that might need to be addressed, Ofcom concludes that it should intervene, its consideration of the appropriate remedies must be aimed at identifying the minimum intervention required to remedy that problem. There is no place in this approach for a pre-determined 'shopping list' of the kind that Ofcom sets out at paragraph 12.42 of the Consultation Document.³²
- A6.31 We nonetheless comment below on the bullet points at paragraph 12.42 of the Consultation Document (which apparently set out elements that Ofcom would want to be included in and/or delivered by any commitments to be extracted from the Premier League).
- A6.32 Ofcom proposes "*a reduction in cross-platform exclusivity for some matches, most likely achieved by making a subset of matches available on both DTT and existing platforms*".³³ This wording is opaque, but we would note the following.
- A6.33 The removal of cross-platform exclusivity would have profound consequences. Ofcom claims to wish to "*ensure that any reduction in the exclusivity premium*

²⁹ Paragraph 12.42 of the Consultation Document.

³⁰ Given its remarks concerning Sky's market power, Ofcom should note that market power alone is not sufficient grounds for action under Article 81/Chapter 1.

³¹ See, for example, at paragraph 12.42 of the Consultation Document: "*we are **likely** to include consideration of the following*" (emphasis added).

³² We note that Ofcom's consultation questions regarding the Premier League (questions 28 and 29) are consistent with our characterisation of Ofcom's approach: Ofcom cannot properly ask for views on remedies before setting out its competition law analysis.

³³ Paragraph 12.42 of the Consultation Document.

associated with these rights does not artificially depress their value".³⁴ But Ofcom appears not to have given any proper thought to the implications of introducing platform-specific packages, including:

- (a) the bidding incentives of operators of closed platforms if platform-specific packages are created;
- (b) the need for cross-platform broadcasters to create bespoke versions of their channels for different platforms; and
- (c) the potential detriment to consumers (a more serious version of the consumer detriment arising from Setanta's acquisition of Premier League rights, discussed in paragraph A6.24 above).³⁵

A6.34 In addition, to the extent that Ofcom envisages the creation of 'DTT-only' rights packages, we note that Ofcom does not explain why DTT should be granted this special treatment (an approach at odds with technological neutrality).³⁶

A6.35 Ofcom suggests that establishing separate sets of rights for residential and commercial subscribers would protect commercial consumers from "*the detrimental effects of collective selling*",³⁷ but does not explain why this would be the case. Ofcom then asserts that this would not risk damaging rights values. We do not understand how Ofcom feels able to make such a definitive statement; the reason given - that the rights are not substitutes - is not sufficient to rule out the risk that splitting the rights in this way may undermine rights values. Ofcom's starting point should be that the Premier League, as rights owner, commercialises its rights in the manner that it considers maximises their value, and that there are likely to be good reasons why it has chosen not to split the rights as suggested. Once again, however, without any evidence to support its position, Ofcom is substituting its own judgment for that of the rights holder; the Premier League is clearly better placed (and better incentivised) than Ofcom to judge how best to protect the value of its rights.

³⁴ Again, Ofcom's meaning here is unclear. How and when is value "*artificially*" depressed? How does Ofcom envisage that it could "*ensure*" that this (whatever 'this' is) would not happen? These questions are academic, however, since, as we explain in this section, the proposed approach poses a clear and serious risk to rights values.

³⁵ By way of illustration, if Sky were to acquire a 'non-DTT package' of Premier League matches, and was wholesaling or retailing the relevant Sky Sports channel on DTT, it would need to create a DTT-specific version of the channel on which those particular Premier League matches would be blacked out. If the corresponding 'DTT package' was acquired by a broadcaster for inclusion in a pay TV channel, consumers on DTT would need to subscribe to both Sky Sports and this other channel in order to access the same content that viewers on other platforms could view by subscribing just to the Sky Sports channel. Clearly, this is just one permutation that could result from removal of exclusivity, but it indicates the types of issues that would inevitably arise.

³⁶ If this proposal is intended to deal with what Ofcom sees as Sky's restricted exploitation of content rights (non-availability of Sky Sports on DTT) then Ofcom is referred to Sky's comments in **Section 6** above as to the reasons why its premium channels are not yet available on DTT.

³⁷ Paragraph 12.42 of the Consultation Document.

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- A6.36 This proposal could have additional adverse consequences that Ofcom appears not to have considered. For example, if Sky acquired residential rights for Premier League matches but no corresponding commercial rights, Sky's channels distributed for viewing in commercial premises could not include Premier League matches. Commercial customers wishing to have access to the other content on Sky's sports channels, for which there is clearly demand,³⁸ would need to subscribe to both Sky's channels and the channel(s) showing live Premier League matches, and could be obliged to pay more as a result.

³⁸ As Ofcom recognises elsewhere in the Consultation Document (see, in particular, Section 4 of the Consultation Document), live football is by no means the only sports content which is highly valued by viewers.