ANNEX 6

COMMENTARY ON THE CONSULTATION DOCUMENT

In this Annex 6 of Sky's Response we provide a non-exhaustive list of the errors in Ofcom's Consultation Document, which are not identified elsewhere in this Response. The significant number of errors, inaccuracies and misconceptions suggests that Ofcom has an inadequate understanding of the context in which pay TV services are provided in the UK and elsewhere. A proper appreciation of that context is an essential prerequisite to accurate analysis of the sector.

Section 3	**Overview of the UK pay TV market**
¶ 3.13	***"An estimated one million households also receive free-to-view digital satellite."*** This appears to be Ofcom's own estimate of the number of households who use a Sky set-top box to receive television services, but do not subscribe to Sky's DTH pay TV services. (No source is provided for the estimate.) If this is the case Ofcom should note that the estimate of one million households is subject to a wide margin of error, being based, Sky understands, on an arbitrary assumption that a certain (constant) proportion of churners from Sky's DTH pay TV services continue to use their set-top boxes to receive digital free to air television services. It is probable that the actual number of such households is substantially higher than this estimate. Moreover, this reference fails to note that all 8.8 million UK and ROI subscribers to Sky's DTH pay TV service, and subscribers to other DTH pay TV services, also receive "*free-to-view digital satellite*". As set out in Sky's Response to the Complaint, over 9 million UK households receive "*free-to-view digital satellite*". ***"Such households receive channels either by stopping their subscription to Sky's pay services and retaining satellite reception equipment which allows them to pick up free-to-air channels; using satellite reception equipment from other retailers with a viewing card; or taking up Sky's "Freesat from Sky" service. For this latter service customers pay a £150 upfront fee for satellite reception equipment, and can receive around 200 free-to-view channels."*** • A viewing card is required to view only a small number of DTH free to air channels – currently Channel 4, Channel 4 +1, Channel 4 HD, five, five US, five US +1, five Life, five Life +1 and Sky Three. These channels are encrypted to prevent territorial 'overspill'. • Anyone with DTH reception equipment (whether a Sky set-top box or a non-Sky set-top box) - including Sky subscribers, non-Sky DTH pay TV subscribers, households which took the 'freesat from Sky' proposition, former DTH pay TV subscribers, and households who have purchased a DTH set-top box elsewhere - regardless of whether they also have a valid viewing card, can access all free to air channels on DTH other than the nine encrypted free to air channels above. There are well over 200 free to air channels available via DTH. As at 1 April 2008 there were over 220 such channels. • The £150 fee for 'freesat from Sky' is not for "*satellite reception equipment*" alone; the package provided includes reception equipment,

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	installation and a viewing card. (Further examples of erroneous references to the £150 payment being for reception equipment are at Paragraphs 2.12 and 3.89 of Annex 8, and Table 17 of Annex 8.)
¶ 3.37-3.39	***"IPTV and Internet TV"*** See further **Appendix 1** to this Annex.
¶ 3.53 and Figure 9	***"Penetration of pay TV is higher in the UK than Italy and Spain, and broadly similar to France. It is however outstripped by Germany and Sweden, where cable is very widespread. In both countries, cable tends to follow a utility-style model, where it is available almost universally, and the price of access is often included in property rental rates."*** The provision of multi-channel television in the form of a "*utility-style model*", (i.e., entirely or principally free to air channels distributed via cable for a small monthly fee) should not be considered as pay TV. As PwC's report at **Annex 1** demonstrates, penetration of pay TV in the UK is significantly higher than in Germany and around the same level as Sweden (see Pages 50 and 176 of Annex 2 of PwC's report). The situation in Sweden should also be put into context: Sweden has completed digital switchover and so all TV households have been forced to choose a method of receiving multichannel TV.
¶ 3.58	***"In Scandinavia and the US, there remain two satellite platform operators. In both cases they appear not to compete head-to-head."*** The proposition that these operators do not compete "*head-to-head*" is erroneous. It would appear to be based on the fact that they do not offer identical products to consumers. Clearly, competition can still be "*head-to-head*" even though competitors offer different products to each other.
Figure 12	See Sky's comments at **Appendix 4** to this Annex.
¶ 3.65	***"The most significant [sports rights] are those related to live viewing of Football Association Premier League (FAPL) matches."*** Ofcom's claim that FAPL rights are *"the most significant"* sports rights relevant to "*the UK market*" is unsubstantiated. Ofcom provides no reason for believing that FAPL rights are significantly more important than, for example, rights to broadcast the football World Cup or European Championships (particularly when England are involved in those tournaments). There is a range of evidence included in Ofcom's Consultation Document that directly contradicts Ofcom's assertion – for example Figure 37 of Annex 14 and the third bullet point in Paragraph 4.16 of Annex 13.
Figure 16.	***"Relative importance of sports that are regularly watched on TV"*** Figure 16 appears to be intended to support Ofcom's proposition that particular types of content are "*must have*". (See **Appendix 2** to **Annex 2** of Sky's Response for further discussion of this subject.) In particular, it is notable that reference to this chart follows the statement that "*the most significant [sports rights] are those related to live viewing of Football Association Premier League (FAPL) matches.*" If this is Ofcom's intention, then reference to Figure 16 in support of this proposition is erroneous. Figure 16 shows only

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	that 59% of "*all regular sports viewers who watch a particular sport or sports*" (in a sample of 190 people) selected "*must have*" (out of three choices – "*must have*", "*nice to have*", or "*not important*") in respect of "*football*" (i.e. all football – not live FAPL football). Accordingly, if Figure 16 is intended to support Ofcom's assertion in Paragraph 3.65, then it is abundantly clear that it does not do so. If, instead, the purpose of Figure 16 is to show relative preference among viewers of sports on television in relation to different types of sports, the caveat attached to this chart ("*caution – small base sizes for all sports except football*") undermines entirely its usefulness for this purpose.

Section 4	**The Consumer Experience of Pay TV**
¶ 4.9	***"Tiscali's IPTV service is available to only 15% of the population. Availability of BT Vision's IPTV service is higher, following BT's broadband coverage, but only offers a non-linear service."*** This statement is based on a snapshot at a point in time and therefore fails to note that coverage of IPTV networks is increasing over time (as is DTT coverage). Tiscali has stated that it aims to pass 50% of UK homes by summer 2008 and to make its IPTV service available over its entire unbundled local loop network by 2009. The BT Vision set-top box also offers access to linear channels broadcast via DTT. Indeed, BT Vision retails Setanta to BT Vision customers by this means. There is no reason why BT Vision's IPTV network should not carry linear services in the future - as Tiscali's network, and IPTV networks in many other countries, do now. Indeed, BT has hinted that its network could develop in this way in future. In evidence presented by BT before the House of Commons Select Committee on Culture, Media and Sport in 2006, when asked whether it is possible that BT Vision would evolve to provide linear channels, Dan Marks, BT Vision's Chief Executive, said: "*I think it is technically possible, that in the future the network will be engineered for those kinds of capacities. I am really not making a comment about BT Vision's intentions in that area.*"
Figure 22	***"UK coverage of broadcast distribution technologies 2007"*** The bar representing coverage of IPTV in the UK clearly is based solely on the current coverage of Tiscali's IPTV network. As Ofcom itself notes in the statement at Paragraph 4.9 above, inclusion of BT Vision's IPTV service in Figure 22 would increase the figure for total current coverage of IPTV networks in the UK.
Figure 23	***"Availability of distribution technologies by country 2007"*** • Figure 23 lists "*free DTT*", "*pay DTT*", "*free satellite*" and "*pay satellite*" as *"distribution technologies"*. These are not "*distribution technologies*". • It states that the largest platform in the UK in 2007 in terms of proportion of homes on a particular platform was DSat (34%). In fact, DTT was the

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	largest platform in 2007 as indicated in Ofcom's own statistics (see for example *Digital Progress Report, Q2 2007*). • Ofcom should have drawn a distinction between digital and analogue delivery for all technologies, rather than only terrestrial broadcasting. It is clear that in countries such as Germany, Spain and the US, which score highly in terms of cable coverage in Ofcom's Figure 23, cable networks are predominantly old analogue networks. The range and quality of services able to be delivered via digital technologies is far greater than in the case of analogue delivery, and therefore this aspect is likely to be more important than simply the number of different delivery technologies available to consumers. • It is not particularly meaningful to conduct analysis such as this at the level of countries, as – particularly in the case of wire-based delivery technologies - consumers in more densely populated areas are likely to have more delivery options available to them than those in sparsely populated areas. (This appears to be recognised in Paragraph 4.24 of the Consultation Document.)
Figure 24	***"Availability of channels by distribution technology and country 2007"*** • In relation to DTH pay TV channels Figure 24 lists the number of "*entry level channels*" and "*top level channels*". These terms are not defined and it is entirely unclear what they mean. • It is unclear why Figure 24 separates channels delivered via DTT into free and pay TV channels, but does not do so for DTH delivery. • The source of the "*Total channels available*" figures for European countries appears to be the most recently available figures from Screen Digest for the number of channels delivered via satellite in each country, which are for 2005 rather than 2007 as stated in the title of Figure 24. • There has been considerable growth in the number of channels available in the UK since 2005 and this is likely to be true for the other countries mentioned. • There are more channels available in the UK than the 416 stated here by Ofcom. In fact, Ofcom stated in its Communications Market Report of August 2007 that there were 433 channels broadcasting in the UK in 2006.
Figure 25	***"Availability of the most watched channels by platform UK 2007"*** • The list of channels would appear to be based on 2006 data, rather than 2007 as stated. The extent to which it is unsafe to rely on such snapshots in a rapidly changing sector is revealed by comparing Ofcom's 2006 list with an equivalent list for 2007. For 2007 Film 4, Five US and UKTV Drama would appear in the list, replacing CBBC, Hallmark and Discovery. • Figure 25 fails to recognise that the "*most watched channels by platform*" varies from platform to platform. The list of the "*most watched channels*" for each of the "*platforms*" included in Figure 25 would be significantly

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	different from the 24 channels that are listed in the table. • Living, Disney, Discovery and Hallmark are not linear channels on TUTV. TUTV offers a selection of programming from these channels on a push-VOD basis. UKTV Gold is only available as a linear channel to TUTV customers with legacy set-top boxes and only broadcasts from 5pm to 11.30pm. Programming from UKTV Gold is available to all other TUTV customers via their push-VOD service. • Figure 25 indicates that Sky Sports 1 is not available on Tiscali's platform. This is erroneous. Sky Sports 1 is retailed by Sky on Tiscali's platform.
Footnote 19	***"Note that the large number of satellite subscribers will tend to push satellite-only channels up the list of "most watched" channels."*** This is erroneous, as demonstrated clearly by the fact that there are no "*satellite-only channels*" in Ofcom's list. In general, the more restricted is the distribution of a channel the more it would get pushed *down* a most watched channels list.
¶ 4.15	***"For all countries other than the US premium content is skewed towards pay TV..."*** In the absence of any explanation by Ofcom of what it means by "*premium content*" it is impossible to comment meaningfully on this statement, and the following statements from Paragraph 4.15. In any case, it is unclear what Ofcom means by content being *"skewed towards"* pay TV. ***"[there is] only a limited amount of premium content available free-to-air."*** In the UK context this would appear to imply a unreasonably narrow definition of "*premium content*". ***"Within pay TV, premium content is skewed to pay satellite in all European markets."*** Again, what is meant by content being "*skewed towards*" a particular type of service is entirely unclear. In any case, the proposition appears erroneous. If the term "*premium content*" broadcast on pay TV channels is assumed to include live broadcasts of "*top flight*" football matches and films in the pay TV window, the providers of pay channels that carry such content tend in general to distribute them via all available technologies. (See Pages 29 and 52 of Annex 2 of PwC's report at **Annex 1**) ***"there is significant availability of premium content on cable in some markets (UK, Spain) but not others (Germany, France)."*** On the assumption that Ofcom regards, at least, broadcasting of live football and films in the pay TV window as "*premium content*" the statement that there is not "*significant availability of premium content on cable*" in Germany and France is erroneous. (See Pages 29 and 52 of Annex 2 of PwC's report at **Annex 1**.)

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Figure 26	***"Availability of premium sports content by distribution technology and country"*** • No date is given for this table. • Given the absence of any explanation by Ofcom as to what It means by "*premium sports content*" (see further discussion in **Appendix 2** to **Annex 2** of Sky's Response) it is impossible for consultees to comment adequately on Figure 26 or Paragraph 4.16 below. The following comments are made with that caveat in mind. • In general, Ofcom's description of the availability of sports programming in the countries included in Figure 26, set out both in the table and Paragraph 4.16, is poor. For example: (a) in the US context, Ofcom appears wholly unaware of services such as the subscription 'Sunday Ticket' which provides access to Sunday afternoon NFL matches and is available only via Direct TV (i.e. is exclusive to a DTH pay TV service); and (b) in the case of Germany, assuming that "*premium sports content*" refers to Bundesliga matches, it is erroneous to state that these are available "*on pay satellite only*". • Figure 26 states that, in respect of European countries "*Top-flight football leagues are used…as a proxy for premium sports*". Such a statement is wholly unclear. For example, (a) it is unclear how one specific type of content can be regarded as a "*proxy for*" other types of content, and (b) the term "*top-flight football leagues*" is unclear. Ofcom should have instead listed the events it included within the category of "*premium sports*" in each country. • If the term "*Top-flight football league*" in the context of the UK means live FAPL football, then it is impossible to understand why "*cable*" does not fall into the category of "*significant content available*" as in fact ***all*** live FAPL matches are available via cable. • Services such as "*pay DTT*" and "*free satellite*" are not "*distribution technologies*" as indicated in the title of Figure 26. It is entirely unclear why "*free DTT*" has been omitted from Figures 26 and 27, particularly when "*ATT*" is included.
¶ 4.16	***"UK - analogue TV tends not to show any FAPL content apart from a series of clips from the league matches played that week on Match of the Day"*** The first part of this statement is an unusual way of describing the fact that live FAPL matches are not broadcast on free to air channels (whether those channels are broadcast on analogue or digital platforms). The second part of the statement, referring to the BBC's Match of the Day programme is erroneous in two respects: (a) Match of the Day carries extended highlights of FAPL matches, not "*clips*" ("*clips*" are short excerpts used in programmes such as news bulletins) and (b) as its name implied, it typically covers matches played on the day of broadcast, not those that were "*played that week*".

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¶ 4.18	***"The link between content and platform choice was highlighted by the recent dispute between Sky and Virgin."*** The meaning of this statement is unclear.
¶4.23	***"The fact that this dispute [between Virgin Media and Sky] appears to have had a negative impact on both firms involved, as well as on consumers, appears puzzling…"*** The dispute is a commercial dispute over the value of channels and the dynamics of that dispute would not be "*puzzling*" if the effects of the operation of closed platforms were understood. Such disputes are in fact common when broadcasters have no choice but to reach agreement for distribution of their channels with closed platform operators. For example, in the US such disputes – and cessation of carriage – occur regularly as is evidenced by the following examples: • January 2007: Turner/Echostar - dispute over carriage of Court TV network. • February 2006: Mediacom/Sinclair – dispute over carriage of Fox affiliate stations. • August 2006: NFL Network/Time Warner/Comcast – dispute over carriage of NFL Network. • January 2006: EchoStar/Lifetime - dispute over carriage of Lifetime and Lifetime Movie Network. • March 2005: Time Warner/Cablevision - dispute over carriage of MSG Channel and Fox News Net New York. • January 2005: Cox/Nextar - dispute over carriage of NBC affiliate station. • March 2004: Echostar/Viacom - dispute over carriage of Viacom channels, most prominently, CBS. • 2003: Cablevision/Yankees - dispute over carriage of Yankees Entertainment and Sports (YES) network. • January 2001: Echostar/Viacom - dispute over carriage of ABC Family. • May 2000: Time Warner/Disney – dispute over carriage of ABC.
Figure 28	***"Summary of pricing structure of main retail packages"*** The information contained in this table is inadequate as a basis for a proper appreciation of the services and charges for those services that it purports to describe. It comprises a patchy, inconsistent and generally vague description. To cite four examples, which are illustrative rather than exhaustive: • it is stated that there are "*various permutations*" in relation to subscribing to Sky Sports or Sky Movies via Virgin Media, which is a wholly vague statement; • subscription to packages containing Sky's sports channels or Sky's movie channels is described as "*buy-through from basic*" in relation to Sky, but

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	not for Virgin Media or Tiscali; and • things such as "*2mb (sic) broadband*" and "*only available with BT broadband*" are described as "*Main packages available to new customers*"; and • charges reported for Sky's pay TV services are erroneous.
Figure 29	***"Summary of entry price points for premium content in major markets"*** For the UK Figure 29 states that "*one Sky basic mix and Sky Movies*" costs "*€47.13/month*". In fact, the cheapest Sky package that includes a Sky Movie Pack costs £26 per month, which is approximately €35 per month. Figure 29 is inconsistent in its references to PPV services. For example, it refers to PPV football matches in Italy and Spain, and includes movies available via PPV in various countries, but does not mention PPV movie services in the UK.
¶ 4.41	Ofcom's discussion of the advantages and disadvantages of using Average Revenue Per Subscriber (ARPS) as a measure of prices for pay TV services at Paragraph 4.41 of the Consultation Document fails to recognise its fundamental flaw. It is generally difficult (or sometimes impossible) to identify a firm's revenue from providing pay TV services for one of two reasons: (a) firms often provide pay TV services as part of 'bundles' of services – for example cable companies provide packages of TV, telephony and internet access, and (b) firms that provide pay TV services often provide other services to consumers and may not publicly separately identify revenues earned from their pay TV services. As a result the 'revenue' part of ARPS often relates to supply of non-pay TV products and services. Where this is the case, it is entirely clear that ARPS lacks meaning as an indicator of charges for that operator's pay TV services. Moreover, such an approach will have a built-in bias of making multi-product suppliers appear more expensive providers of pay TV services than those firms which are more tightly focused on providing pay TV services.
¶¶ 4.43-4.48	***"We have carried out an initial assessment of [LECG's report commissioned by the Complainants], assisted by Andrew Chesher, a professor of economics, at University College London."*** ***"We put these concerns to LECG. It provided some additional data on features of selected European pay television markets... [and] analysis to support the claim that the results could be interpreted as evidence of a causal link between market structure and average prices."*** Ofcom states, at Paragraph 4.48, that it would "*welcome further evidence*" on its initial assessment of LECG's report. It is, therefore, both disappointing and surprising that Ofcom refused Sky's requests for copies of its "*initial assessment*" and "*additional data*" and "*analysis*" provided by LECG. According to the Consultation Document, LECG appears to maintain that its failure to control for programme quality and the types of services subscribed to by consumers are unlikely to "*significantly affect*" the results of its study. It is impossible to see how that could be the case, and Sky considers that this significantly further diminishes LECG's credibility in the context of this consultation. The report prepared by CRA and Professor John Van Reenen

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	showed clearly that these issues (among others) were fatal to the reliability of LECG's study. Indeed, as recognised by Ofcom at Paragraph 4.47 of the Consultation Document, it would appear contrary to basic common sense to assert that proper measurement of the quality of services is unnecessary in a study that purports to compare charges for services available in different countries, among which there is considerable variation in quality. "***We also put LECG's initial analysis to Sky.***" Ofcom's summary of the critique of LECG's initial analysis that formed part of Sky's Response to the Complaint is wholly inadequate. Ofcom's summary fails to mention the fact that Sky submitted a detailed review of LECG's report prepared by CRA and Professor John Van Reenen (**Annex 3** to Sky's Response to the Complaint), which identified serious flaws in LECG's approach, the data used and the interpretation of the results obtained. The "*technical points raised about the econometric methodology*" to which Ofcom refers are, Sky presumes, the technical errors that CRA and Professor Van Reenen identified, which they concluded rendered LECG's results "*entirely unreliable*" (Paragraph 15 of the Executive Summary). Furthermore, even accepting LECG's approach, when LECG's own specifications are correctly re-estimated, UK average revenues per subscriber (ARPS) are 3.1% below the European average (contrasting sharply with LECG's conclusion that there is a 9% UK premium); assuming (as LECG does) that concentration indices are informative as to the degree of competition, correct calculation of such indices for the UK indicate that the (alleged) UK pay TV market is amongst the more competitive markets in Europe, contradicting LECG's conclusion that the higher ARPS observed in the UK is due to high margins and a lack of competition in the market.

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¶ 5.22	"***The CC's draft decision clearly acknowledges that there has been an increase in competition between free to air and basic-tier TV.***" Far from "*clearly acknowledging*" this, neither the Competition Commission's preliminary report nor its final report say any such thing. "***…the CC emphasised that the question it was seeking to address was whether market power would be increased following a merger, rather than whether any firm had existing market power (which was the focus of previous UK investigations).***" Far from "*emphasising*" that this is the question that it was seeking to address, neither the Commission's preliminary report, nor its final report, made any mention at all of such an issue. Sky notes that when Ofcom was asked for a reference for this claim it referred to Paragraph 4.3 of the Commission's preliminary report which contains no reference to any such subject.
¶ 5.27	"***Our consumer research provides strong indicators that a consumer purchasing a pay TV service which includes premium sports channels is unlikely to regard a non-sports free-to-air service as a close substitute. This is not a surprising result, but it is worth noting some of the specific evidence which supports it. For example:***

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	• ***49% of Sky subscribers say that they are either passionate about sport, or that they follow sport closely, as compared to 27% of basic pay TV subscribers, and 29% of Freeview viewers"*** The "*specific evidence*" cited in this bullet point falls into the trap of the toothless fallacy[1] by focusing on infra-marginal subscribers, rather than marginal subscribers. Of more relevance in the context of market definition is the fact that, as shown by the data from which the figures above are drawn, 35% of subscribers to packages that include Sky's sports channels either have no interest or are "*interested*" in sports, while among all Sky subscribers the equivalent figures are 30% ("*no interest*") and 21% ("*interested*") respectively – i.e. over half of all Sky subscribers. Accordingly, the "*specific evidence*" cited by Ofcom does not support the conclusion that it seeks to draw from that evidence. • ***"…Of those consumers who purchase both premium sport and premium movies from Sky, 47% state that they mainly want Sky Sports, and take the movie channels because of the low additional cost, whereas 23% state that they mainly want Sky Movies, and take the sports channels because of the low additional cost. Another 23% attached equal value to sports and movies."*** This finding contradicts (rather than "*supports*") Ofcom's claim that "*a consumer purchasing a pay TV service which includes premium sports channels is unlikely to regard a non-sports free-to-air service as a close substitute*". The implication of this finding is that there are many marginal subscribers who subscribe to a package containing sports channels because its price is not much higher than a package without sports channels, and that those subscribers are likely to respond to a price increase by terminating their subscription or moving to a smaller package. A similar conclusion would apply to Sky Movies, undermining Ofcom's conclusion at Paragraph 5.45 that "*there is likely to be a narrow retail market for premium movies*" (sic).
¶ 5.28	***"In contrast, the FAPL is the only one of these 'must have' events with matches scheduled regularly throughout most of the year, and therefore capable of forming the basis of a premium sports channel."*** The proposition included in this statement that it is only possible to develop a premium sports channel that is based on a sport that has "*matches scheduled regularly throughout most of the year*" is ill-founded. For example, there is no reason why a premium sports channel could not be developed that included a mix of coverage of different types of sports events that take place at different times during the year. More importantly, however, the context in which this assertion is made is in relation to the question of "*whether sufficient sports content is available free-to-air to significantly constrain the prices charged for pay TV premium sports* (sic)." The issue of what sports are capable of forming the basis of a premium sports channel is *wholly irrelevant* to this question. Instead, the relevant consideration is whether, taken as a whole, the range of sports events on free to air television is sufficiently attractive to constrain charges for pay TV packages that include premium sports channels. In this respect one element of 'attractiveness' is whether free to air television offers the opportunity to

[1] See E(iii) of Part 1 of **Annex 2** to Sky's Response.

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	view sports events throughout the year. Clearly, this is the case.
¶ 5.29	***"FAPL is by some distance the most valuable of sports rights, selling for £669m per year. This is over six times the revenue generated by the next most valuable set of rights, the FIFA World Cup..."*** It is meaningless to compare the "*revenue generated by*" (i.e., price paid for) FAPL rights and rights to broadcast the World Cup in the UK, because the latter is a listed event, which greatly restricts the number of possible bidders. Rights to broadcast the World Cup in the UK have for many years been won by a joint bid from the BBC and ITV, with no realistic competitor. Ofcom concludes from a discussion of the amounts paid for a variety of different sports competitions that "*wholesale channel providers such as Sky and Setanta do not regard any other sports rights package as being a close substitute for FAPL*". In the first instance, rights to a number of the other competitions and events discussed by Ofcom are simply not available to broadcasters such as Sky or Setanta because they are Listed Events, which means that they cannot be substitutes for FAPL rights for Sky or Setanta as a matter of law. Moreover, it is meaningless to consider the substitutability of FAPL rights with other rights by reference to the total amount paid for FAPL rights. Regulation now requires that FAPL rights are sold as six separate packages. As a result, the relevant issue is whether alternative rights comprise an adequate substitute for <u>each of the individual packages</u> of FAPL rights offered for sale. Notwithstanding this, it is erroneous to consider that the price paid for particular inputs is determinative of their substitutability. This commits the errors of (a) assuming that products' characteristics (including prices) must be identical for them to be effective substitutes, and (b) ignoring the trade-offs that purchasers are likely to make between benefits and costs associated with purchasing particular sports rights. Sky continually evaluates the 'value for money' of purchasing different rights configurations – i.e. it evaluates trade-offs between the value generated by purchasing different sports rights, and the price it is likely to have to pay for them. From this point of view, all sports rights, including packages of FAPL rights, are substitutable. [**CONFIDENTIAL**]
¶ 5.30	***"The other key distinction between free to air sports and premium sports relates to the quantity of programming available. A subscriber to Sky Sports would have access to around 14,000 hours of sport during Q3 2007, while only 3,400 hours of sports programming were available free to air on DTT."*** These figures do not appear reliable. Sky has been unable to reproduce them from BARB data. In particular, Sky notes that the figure of 14,000 hours includes the entire output of Sky Sports News and is likely to include hours of teleshopping broadcast on Sky's Sports channels. Ofcom's proposition here appears to be that a service that makes more sports programming available to consumers is inherently superior to one that provides fewer hours, and therefore cannot be an effective substitute. Clearly, such a proposition is unsafe as it ignores the potential of the quality of programming carried on the two services to differ. (Sky notes that the use of

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	the term "*only*" in relation to the number of hours of sport broadcast free to air is inappropriate for this reason.) More importantly, however, it fails to have regard to the trade-offs that consumers make between characteristics of products, including their prices. Clearly, pay TV services offer consumers access to more (and different) programmes than are broadcast free to air. However, that additional choice comes at the price of the monthly subscription charge. The relevant issue in the context of market definition is whether consumers value the additional choice provided by a pay TV service sufficiently to subscribe at the charges set by pay TV operators, or prefer instead to choose from a smaller but cheaper set of programming (having regard to the relative quality of the two sets of programming). (See E(iii) of Part 1 of **Annex 2** to Sky's Response.) Finally, we note that Ofcom's comparison fails to consider the availability of sports programming on basic pay TV channels. (By contrast, this is considered in a similar comparison of hours of sports programming broadcast, in Paragraph 4.12 of Annex 13.)
¶ 5.37	***"…the pay per view and subscription pay TV distribution windows overlap".*** This is erroneous. These windows do not overlap. The PPV movie window typically runs from seven to 12 months after the cinematic release of a title and the subscription window commences 12 months after cinematic release.
¶ 5.38	***"In relation to the question of whether pay per view movies are a close substitute to pay TV subscription services, we note that:*** • ***63% of consumers of pay TV subscription services regard the ability to pay monthly as either 'must have' or 'nice to have'. Such consumers are unlikely to regard a pay per view service as a close substitute…"*** In the first instance, the meaning of this evidence is unclear. Both pay per view movies and subscription services are billed (and therefore paid for) on a monthly basis. Again, however, citation of this evidence falls into the trap of the toothless fallacy. The data in fact indicates that 32% of the consumers surveyed rate the ability to pay monthly as "*nice to have… but it is not required in order to make Sky Movies worth having*". Accordingly, on this basis there would appear to be a very significant number of marginal subscribers. • ***"Wholesale revenues for films in the subscription pay TV window were estimated to be £313m in 2006, as compared to total wholesale revenue for all on demand services of £54m. This suggests that wholesale channel providers do not currently see on-demand services as being a close substitute for subscription pay TV services."*** No source is provided for these figures. They appear to be taken from Screen Digest's report for Ofcom entitled "*Movie Markets in the UK*". Screen Digest provide no basis for these figures, and use of the term "*wholesale revenues"* is unclear. They appear to be the amounts paid for movie rights. In any case: (a) it is erroneous to claim that the amount spent on two different inputs to a business is capable of demonstrating whether they are 'close substitutes' (see further the discussion in relation to sports rights above); (b) Ofcom's focus on 'close substitutes' is erroneous; and (c) as in the case of FAPL rights (see Sky's comments on Paragraph 5.29, above) comparisons of the total

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	amounts paid for all rights to broadcast movies in a particular window is entirely uninformative in relation to the issue of substitutability between different groups of rights when rights are, in fact, sold in smaller packages – for example the pay TV rights to films from a particular studio.
¶ 5.39	***"In relation to the question of whether other movies, either from later distribution windows or from minor studios, are close substitutes to pay TV subscription services, we note that:*** • ***72% of consumers of pay TV subscription services value access to new films, whilst 83% value the convenience of access to a range of films. Such consumers are unlikely to regard a service which is limited to later release windows or minor studios as being a close substitute."*** Again, Ofcom's analysis of this data is subject to the toothless fallacy. Instead of focusing on the preferences of consumers for whom these attributes matters most, Ofcom should have examined those who value such things the least. In relation to "*access to new releases*", for example, over a quarter of the Sky Movies subscribers surveyed said that this was "*not important*" to them. In relation to "*the convenience of access to a range of films*" the figure for those who regard this as "*not important*" is lower, though still significant, at 17%. Accordingly, for those consumers who matter most in the context of market definition, it is clear that the evidence cited by Ofcom does not support the conclusion it seeks to draw from that evidence. We note also that: • the evidence cited appears entirely unrelated to the issue that it is intended to address – "*whether other movies, either from later windows or from minor studios, are close substitutes to pay TV subscription services*". • Ofcom focuses erroneously on the existence of "*close substitutes*". • Ofcom does not appear to have considered whether it is appropriate to regard films which are at least a year old (given that the pay TV window begins 12 months after cinematic release) as "*new releases*". • Ofcom appears to fail to recognise that for consumers for whom "*access to new releases*" is important, cinema, DVD rental and purchase and PPV services clearly provide superior alternatives to pay movie channels. • Ofcom does not appear to have had regard to the range of relevant evidence available to it. In subsequent Ofcom research, only 16% of Sky Movies subscribers listed "*to watch recently released movies*" as a reason for subscribing.[2] • ***"Wholesale revenues for films in the later free-to-air distribution window are £199m, significantly lower than the revenues cited above as being associated with the pay TV window (£313m). This suggests that wholesale channel providers do not see movies in later distribution windows as being a close substitute for movies in the pay TV window."*** See comments on Paragraph 5.38 above.

2 Pay TV Research phase 3, Table 35 (QH2A), multiple answers allowed.

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¶ 5.40	***"In relation to the question of whether movies distributed via DVD are close substitutes to pay TV subscription services, we note that:*** • ***70% of consumers of pay TV subscription services value films being available at all times. Such consumers clearly value the convenience of a broadcast subscription service, and are unlikely to regard a DVD purchase or rental as being a close substitute."*** Again, Ofcom's analysis of this data is subject to the toothless fallacy. Instead of focusing on the preferences of consumers for whom these attributes matters most, Ofcom should have examined those who value such things the least. In relation to "*the convenience of a broadcast subscription service*", 29% of the Sky Movies subscribers surveyed said that this was "*not important*" to them, and a further **43%** rated this feature as "*nice to have*". Moreover, it is surprising that Ofcom resorted to the response to this question, which is only indirectly related to the proposition that it sought to examine. Ofcom actually asked questions specifically related to DVDs in its survey. For example Figure 42 of Annex 14 to the Consultation Document indicates that around a third of the Sky Movies subscribers surveyed rated "*the convenience of not renting a DVD*" as "*not important*" to them. Furthermore, only 20% of DTH Sky Movies subscribers, and 17% of cable Sky Movies subscribers, listed "*Always having movies available at home, without having to order, wait for delivery or collect a DVD*" as a reason for subscribing to Sky Movies. [3] These types of evidence significantly undermine the conclusion that Ofcom seeks to draw from the data cited. ***"Over the last few years sales of pay TV packages including premium movies have increased by [✂] per annum despite large reductions in the price of DVDs and the rapid growth of DVD sales. This suggests that the retail price of DVDs is not constraining the retail price of pay TV packages including premium movies"*** Although the figure for "*sales of pay TV packages including premium movies*" has been excised, we consider the proposition that sales have increased "*over the last few years*" to be erroneous. (See section (ii)(p) of Part 3 of **Annex 2** to Sky's Response.) On its own, this invalidates the conclusion reached by Ofcom. Moreover, Ofcom's analysis is superficial. In the first instance it is another example of a misdirected search for "*close substitutes*", or particular products that constrain charges for pay TV packages. (See E(i) of Part 1 of **Annex 2** to Sky's Response.) It fails entirely to recognise that sales of pay TV packages are affected by a wide range of different factors and, therefore, to isolate the impact of any one particular factor would require complex analysis. (See A(ii) of **Appendix 5** to **Annex 2** of Sky's Response.) The proposition that Product A can be ruled out as being an effective substitute for Product B simply because a fall in the sales of B is not observed when the price of A falls is simplistic. ***"To the extent that the sale of DVDs does constrain retail pay TV services, this will at most result in an indirect constraint on the wholesale prices for movie channels. This is because a retail pay TV provider purchasing wholesale premium movie channels might credibly respond to a price increase by switching to other wholesale movie channels, but not by switching to DVDs."***

[3] Pay TV Research phase 3, Table 35 (QH2A), multiple answers allowed.

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	This proposition misses the point. It is not retailers switching to provide DVDs that produces the operative constraint; it is the threat of consumers switching. Moreover, Ofcom appears here to equate constraints being indirect with them being unimportant. If this is the case, this is erroneous as a general principle.
¶¶ 5.41-5.42	***"The biggest consumer response to a SSNIP on these movie channels was simply to drop the movie element of the sports/movie/basic package. At face value, these results might be interpreted as evidence that basic-tier TV services are a close substitute for Sky Movies."*** The more plausible interpretation is that a combination of (a) free to air television services, (b) going to the cinema, (c) buying and renting DVDs, (d) using PPV/VOD movie services and (e) basic pay TV services, is an effective substitute for pay TV packages that include Sky Movies. To regard ceasing to subscribe to Sky Movies as a switch to "*basic-tier TV services*" is erroneous. (See section E(i) of Part 1 of **Annex 2** of Sky's Response.)
¶ 5.44	***"prices for premium movies*** **(sic)** ***have risen steadily in real terms while subscriber numbers have also continued to rise"*** Both parts of this statement are erroneous. We assume that the first part of the statement is intended to refer to charges for pay TV packages that include Sky's movie channels. These have not "*risen steadily in real terms*". (See section (ii)(k) of Part 3 of **Annex 2** to Sky's Response.) Subscriber numbers have not continued to rise, they are declining. (See section (ii)(p) of Part 3 of **Annex 2** to Sky's Response.)
¶ 5.49	***"Additionally, there are some specific pay TV channels (Sky 1, UK Gold, Discovery) and programmes which are cited by a significant number of consumers of pay TV as being important. It is possible that these consumers would not regard other free-to-air services as being a close substitute."*** Again, Ofcom's analysis of this data is subject to the toothless fallacy. Moreover, the actual evidence appears to belie Ofcom's proposition that the number of consumers who cite specific pay TV channels and programmes as being important is "*significant*". For example, UK Gold is cited by only 5% of pay TV subscribers as being important, Discovery 9% and Sky One 12% (see Figure 18).
¶ 5.51	***"If basic and Freeview were economic substitutes, we might expect basic take-up to be reduced as the Freeview product offering and customer base have grown, and/or an inability of retailers of basic packages to increase prices without losing subscribers to Freeview."*** This proposition is overly simplistic. In order to identify the impact on basic pay TV subscriptions of Freeview, it is necessary to take into account all other factors that impact on demand for basic pay TV subscriptions. As Ofcom recognises in its analysis in Annex 13 of the Consultation Document, at a minimum it is necessary to take into account changes in the quality of the services offered, and charges for basic pay TV packages. Moreover, as set out in Section A(ii) of Appendix 5 of **Annex 2** to Sky's Response, in light of the fact that pay TV take-up was growing over this period, the expectation in terms of subscriber numbers over time would be a reduced

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	rate of growth rather than absolute declines in subscriber numbers. The econometric study provided to Ofcom by Sky enables the impact of Freeview on demand for basic pay TV subscriptions to be separated from other factors that affect this demand. It shows clearly that the availability of Freeview substantially reduces demand for basic pay TV subscriptions, which provides strong and compelling evidence that the two services are substitutes.
¶ 5.52	"***Freeview provides an increasingly close substitute to basic pay TV services. However, it still cannot match the range of channels which pay TV provides.***" It is entirely unclear what the second of these sentences means. If it is intended to be a comparison of the number of free to air television channels available via DTT with the total number of basic pay TV channels available, for example, via cable or DTH, then the comparison is spurious. The DTT platform is subject to obvious capacity constraints which limit the number of television channels that can be broadcast. If the proposition is that there are fewer free to air television channels available in the UK than basic pay TV channels, then it is erroneous. The number of free to air channels available via DTH (which is the only fully open platform available to broadcasters in the UK) outnumbers by some margin the number of pay TV channels available on that platform. It is also overly simplistic simply to evaluate the comparative strengths of two different types of television services by comparing the number of television channels in each. More importantly, however, this proposition fails entirely to consider the trade-offs involved in choosing between the options available to consumers. Subscribing to pay TV increases a consumer's choice of television channels at the cost of the monthly subscription charge. The relevant question is whether lower priced services with a smaller choice of programming might be an adequate substitute for a higher priced service with a greater choice of programming. (See E(iii) of Part 1 of **Annex 2** to Sky's Response.)
¶¶ 5.72	***"...A similar effect can be observed downstream, in relation to the contracts which govern the supply of wholesale channels to retail service providers. These contracts tend to be for anything from three to eight years, suggesting a barrier to entry for any new retailers wishing to assemble a selection of the top channels."*** The proposition that "*these contracts tend to be for anything from three to eight years*" in duration is misleading. Carriage contracts longer than 3-5 years in duration would be highly exceptional. Some carriage contracts have rights of extension, which mean that they have the potential to run for longer than 3-5 years. However, these are not common. Accordingly, taking into account the duration of contracts alone, Ofcom exaggerates the effect on barriers to entry at the retail level. Moreover, Ofcom fails to distinguish properly between (a) entry by retailers on new platforms, and (b) new retailers entering on existing platforms. In relation to (a), carriage agreements tend to be non-exclusive as between different platforms. This is illustrated by the fact that platform exclusivity for television channels in the UK (i.e. where a pay TV channel is only available on a particular platform) is rare – if indeed it occurs at all other than as a result of

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	capacity constraints. Accordingly, existing carriage agreements comprise no barrier to entry whatsoever to retailers entering via new platforms. In relation to (b), given that only Sky's DTH platform is genuinely open, the proposition can only relate to entry by a new retailer onto the DTH platform. In this context, issues of contract duration and differing end-dates of existing contracts, which are discussed in the paragraphs preceding Paragraph 5.72, are irrelevant. Instead, the key issue is the fact that licensing multiple retailers of channels on the same platform is not in any channel provider's interests, and therefore unlikely to occur in practice. (See Section 3.2 of **Annex 4** of Sky's Response.)
¶ 5.97	***"Bundling may also be more efficient than offering all channels on an à la carte basis for two other reasons. First, bundling might reduce consumer confusion ... Second, bundling might result in cost savings (by avoiding transaction costs resulting from multiple consumer purchases)."*** Ofcom fails to consider other benefits of bundling for both consumers and retailers. These include: • enabling sampling; • other categories of cost savings for suppliers (e.g., savings in marketing costs); and • most importantly, supporting a greater range of television channels. For further discussion, see Sky's response to Questions 13 and 14 of Ofcom's information request of 18 July 2007. Ofcom does not appear to have had due regard to Sky's response to that information request.
¶ 5.101	***"A consumer wishing to purchase premium sports (sic) from Sky faces an entry-level price of £34 per month."*** This is erroneous. The lowest priced package that includes one of Sky's premium sports channels is currently £26 per month.
¶ 5.112	***"Having considered the generic switching barriers, we now document some evidence of actual switching behaviour in the market... our market research suggests lower levels of switching in multi-channel television compared to other communications markets. For example, only 2% of multi-channel television customers say they have switched service provider in the last 12 months, compared to 13% of mobile phone customers."*** Ofcom's discussion of these matters is unclear. In particular, it is unclear whether the "*switching*" discussed includes switching between pay TV and free to air television services, or only among different pay TV services. If it includes the former, then Ofcom's estimates of the numbers of customers who "*switch*" appear to be erroneous. [**CONFIDENTIAL**]. Sky considers that comparing switching among pay TV providers with the behaviour of mobile phone customers is not a sensible comparison. The mobile sector is characterised by extensive switching driven by consumers' desires for heavily subsidised equipment upgrades at the end of minimum term contracts. Such a situation does not pertain in the pay TV sector. Moreover, Sky questions the view that a situation in which large numbers of

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	customers move regularly between suppliers should necessarily be regarded as a good indicator of a market that delivers benefits for consumers. If switching is low, it is necessary to distinguish carefully between alternative reasons for that outcome. In particular, it is necessary to distinguish between (a) a situation in which there are significant numbers of customers who are unhappy with the services they receive from a particular supplier but consider it too difficult to switch to make switching worthwhile, and (b) a situation in which switching is easy, but few people switch because they are satisfied with the services they receive from their existing supplier.

Annex 7	**Legal framework and regulatory environment**
¶¶ 3.1-3.2	In its quotations from the European Commission's FA Premier League Commitments Decision, March 2006, Ofcom consistently misquotes the rights available as "*TV*" rights (e.g., "*The offer for sale by FAPL of packages of: (i) live TV rights; (ii) near-live TV rights…*") The rights in question are, in fact, 'audio-visual' rights, not "*TV*" rights. This qualification is significant as the definition is not determinative of the method by which the licensee broadcasts or transmits the content to customers.

Annex 8	**Pay TV market overview**
General comments In broad terms, Ofcom's overview of the "*Pay TV market*" (which includes substantial discussion of digital free to air television services) provides a reasonable description of a range of aspects of the television sector in the UK. That said, however: (i) it includes numerous inaccuracies and errors. In this section we have not commented fully on all these, as many of them are of relatively minor importance in the overall context of Ofcom's consultation; and (ii) there are significant misperceptions in relation to (a) the nature of Freeview, and (b) the roles played by various entities in the sector. We discuss the former in **Appendix 2** (Freeview) and the latter in **Appendix 3** (Ofcom's misperception of roles in the sector).	
¶ 2.22	***"Most notably, since 2003, Sky's channels have lost audience share – from 11.7% in 2002 to 8.7% in 2006. This is partly explained by the fact that only three Sky channels are available on the rapidly growing Freeview platform."*** It is unclear why Sky's audience share is singled out for note in this paragraph. Ofcom's 'partial explanation' for this decline is erroneous. Neither the fact that "*only three Sky channels*" are available via DTT, nor the fact that the number of DTT households grew rapidly in this period, can explain (whether partly or otherwise) the loss in viewing share of Sky's channels. An increase in the number of DTT households would be expected to increase the aggregate viewing share of Sky's channels (as more people have access to some of Sky's channels). The above facts would only reduce the viewing share of Sky's channels if there had been a net transfer away from platforms with more Sky channels to platforms with fewer; in fact, the net transfers have been from analogue terrestrial to DTT and DTH, both of which increase the ability of viewers to watch Sky's channels, and so other things being equal, viewing of Sky's channels should have increased. A major reason for the decline in viewing of Sky's channels is likely to be the increased strength of the free to air proposition over this period, notably the success of the terrestrials' new digital sister channels.
¶ 2.31	***"There may be considered to be three types of pay TV channel:...*** • ***Premium channels without unique content, where an additional subscription is required for one channel or a small package of channels. Viewers are likely to have a choice between two or more channels with similar content (e.g. channels showing Adult/pornographic material);*** • ***Unique premium content, where additional subscriptions are required for one channel or a small package of channels and the content available on those channels may be exclusive or otherwise unique (e.g. channels showing particular sports content or events such as Premier League football matches, and channels showing first run Hollywood films)."*** Ofcom's distinction between "*premium channels without unique content*" and "*unique premium content*" in this paragraph is both bizarre and inchoate.[4]

[4] Even though Ofcom refers to "*unique premium content*" in its third type of pay TV channel, we have assumed from the context that Ofcom is instead referring to 'channels with unique premium content'.

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	At best, as far as Sky is able to discern, Ofcom seeks to draw a distinction between premium channels such as Sky Sports 1 and Spice Extreme (Ofcom's sole example of "*premium channels without unique content*" is "*channels showing Adult/pornographic material*") on the basis that the former has *particular programmes* (such as *particular* live FAPL matches) which are not available on any other channel, whereas (in Ofcom's formulation), although the *particular programmes* broadcast on Spice Extreme are not available on any other adult channel, there is pornographic programming on other adult channels. This appears to amount therefore to a proposition that either: (a) premium channels such as Sky Sports 1 carry programmes in a *genre* that is not available on any other television channel – which is clearly erroneous; or (b) premium channels such as Spice Extreme do not carry any programmes that are unique to that channel. This is also erroneous. Accordingly, to the extent that the meaning of this distinction drawn by Ofcom can be discerned, it appears to be erroneous. Moreover, it appears to fail to appreciate one of the basic facts of television broadcasting: that competition between broadcasters occurs by broadcasting television programmes that are not found on any other channels. This is the case whether the channel in question is a free to air channel, a basic pay TV channel, a premium sports channel or an adult channel.
¶ 2.37	***"Pay TV retail service providers may also make content from their channels available to viewers using retail VoD services. For example, Sky allows its Sky Movies channel subscribers to download certain movies to their PC and/or set-top box free of charge."*** Sky does not have a free (or pay) pull-VoD to the set-top box service. (Sky subscribers with a Sky+ or HD set-top box are able to store movies purchased from the Sky Box Office DTH NVoD service on their set-top boxes for a limited period of time.)
Table 2	**"*Arrangement for key wholesale services by distribution technology*" (sic)** The Virgin Media column states that Virgin Media does not provide platform services and transmission to third parties. We do not believe that this is the case given the provision of the FilmFlex services on Virgin Media's network. This point has already been raised with Ofcom in a letter to Steve Unger, dated 9 January 2008. Ofcom provided a cursory response to Sky's query in a letter dated 17 January 2008, stating that "*On Filmflex, our understanding is that Virgin Media remains the retailer, and Filmflex effectively operates as a wholesale supplier sitting between the studio and Virgin Media.*" Sky expects that Ofcom will pursue its undertaking in this letter to "*look into [this matter] further*". It is unclear why platform services and transmission are listed as "N/A" for Tiscali given that Sky retails channels on Tiscali's platform.

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¶ 2.45	***"The channel owner will normally be paid a proportion of the subscription revenue (commonly based on the actual or envisaged success of the channel)".*** Sky is not aware of any channel providers that are paid a proportion of subscription revenues. It is certainly not a "*normal*" practice. All amounts paid to pay TV channel providers naturally reflect the "*actual or envisaged success of the channel*".
Table 11	***"Monthly prices for Sky's basic and premium channel package mixes"*** Ofcom has excluded from this table a range of Sky's pay TV packages on the basis that "*the prices are not normally advertised by Sky*". This is a spurious reason for failing to include these packages. The fact is that these packages exist and people subscribe to them. Moreover, Sky chooses to emphasise different packages in its marketing at different times. Ofcom's reporting of the services made available by Sky to consumers should not depend on its marketing strategy at particular points in time.
Table 17	***"Summary of services available to Freesat from Sky and Sky Digital customers"*** Table 17 includes a number of peculiarities. For example: • it includes Sky News, Sky Three and Sky Sports channels in a category of basic pay TV channels. Sky News and Sky Three are free to air channels.[5] Sky Sports channels are premium pay TV channels; • it includes under the heading of "*DSat FTA-only households*" households who subscribe to non-Sky DTH pay TV services (such as Setanta's DTH pay TV service). Clearly, such households are not "*FTA-only households*"; and • it lists set-top boxes as "*services*".
Table 33	***"Availability and cost of Setanta Sports channels by platform"*** Neither NASN (which is owned by ESPN) nor LFC TV are Setanta channels. Sky also understands that Racing UK and Racing World are not Setanta channels. Setanta does, however, retail those channels via DTH.

[5] Sky Three is encrypted and can be viewed by any DTH household with a Sky set-top box and valid viewing card.

Annex 9	**Summary profiles of pay TV in France, Germany, Italy, Spain, Sweden and the United States**

General comments

Annex 9 of the Consultation Document suffers from two significant flaws. First, its data on "*pay TV subscribers*" is drawn from Screen Digest, whose measure is inappropriate for some countries (within this sample, notably Germany and Sweden): it includes households paying a nominal fee for cable access to a small number of predominantly free to air channels.

Second, it reports "*prices*" in each country without explaining what those "*prices*" represent, how they are calculated and why they are valid and relevant for international comparisons. If, as seems most likely based on the other data presented, they are a measure of average revenue per subscriber ("ARPS"), then they suffer from at least three problems:

(i) ARPS is a poor measure of "*price*" of pay TV (see further the discussion in relation to Paragraph 4.41 of Section 4 above);

(ii) in some countries the calculation includes households which are not true pay TV subscribers, as described above; and

(iii) it makes no attempt to address the differences in quality between countries - as the report implicitly recognises when saying that the "*price*" difference in Germany is "*at least, in part, a reflection of the differences in the services (UK offerings, especially for cable are richer)*".

(For further discussion of these points see the review of LECG's study by CRA and Professor John Van Reenen, at **Annex 3** to Sky's Response to the Complaint.)

There are also consistent errors in Annex 9 in relation to the provision of pay TV services in France. In particular, there is considerable confusion between (a) the roles of Canal+ and CanalSat and (b) the services they provide. Canal+ produces the "Le Bouquet" package of premium sports and film channels, and *retails* that package via DTH, DTT, IPTV networks and cable. (It does not, as stated on Page 12 of Annex 9, offer the package "*on a wholesale basis*" to other operators.) Canal+ also retails a single channel pay TV service via the analogue terrestrial platform. CanalSat operates the DTH platform and retails a package of basic channels on a range of platforms – DTH, DTT and IPTV networks. (See the country annex on France in PwC's report at **Annex 1** for further details.)

p. 13	***"Pay television services [in France] are significantly cheaper than in the UK"*** This is erroneous. See Figure 4 of PwC's report at **Annex 1** of Sky's Response.
p. 19	Premiere is listed as a platform in a table of major players, but it is also a major cross-platform retailer, as is Unity Media (and other cable operators). Cable platforms are open in Germany and a range of retailers can offer pay TV services over the same network.
p. 21	***"Pay TV penetration is higher in Germany (63%) than in the UK (46%)"*** As the report goes on to note, this high penetration is largely due to the widespread provision of effectively free to air channels (similar to the set of channels available free to air on other platforms) via cable for a very low monthly fee. In its report at **Annex 1** of Sky's Response, PwC estimates that genuine pay TV penetration in Germany is less than 10%.

p. 72	***"Swedish pay TV penetration, at 89% of TV households, is almost twice that in the UK, which stands at 46%... mainly due to widespread adoption of basic cable services (similar to the German market)"*** As the report correctly notes, a large proportion of "*pay TV*" households are actually paying a nominal fee to receive predominantly FTA channels over the cable network. PwC estimates true pay TV penetration in Sweden as approximately 50%, very similar to that of the UK. This should also be put into context: Sweden has completed digital switchover and so all TV households have been forced to choose a method of receiving multichannel TV.
p. 83	***"Unlike in other European markets, no single sports property is the key driver for pay TV"*** The proposition that there is a "*single sports property*" that is "*the key driver*" for pay TV in other European markets (or the UK) is facile. All available evidence – including much evidence in Ofcom's Consultation Document – suggests that there is a wide range of drivers of demand for pay TV services. In particular, it is evident that 'sports properties' are not "*key drivers*" for the 5.4 million UK households that subscribed to basic-only pay TV packages at the end of 2007.

Annex 10	**Summary of UK sports rights**
General comments Sky notes that this Annex appears to have been updated since it was first published by Ofcom. Sky considers that, in the interests of transparency, if Ofcom makes post-publication changes to consultation documents it should indicate these clearly to consultees – not least to ensure that consultees are commenting on the most up-to-date version of a consultation document.	
p. 3	***"… 2012 Summer Olympics ~£71 million, estimate based on assumption of BBC paying 25% of EBU fees"*** Given that there are 52 other EBU members representing at least six major broadcasting markets, we suspect that the assumption of the BBC paying 25% of the EBC fees is a significant overestimate.
p. 8	***"This lack of exposure can have a knock-on effect at grass-roots level and affect the overall health of [Six Nations rugby and cricket]"*** We note that this is a 'reported' criticism only, and does not necessarily reflect Ofcom's views. Nevertheless, such criticisms are generally ill-founded. For example, in respect of cricket, in a press release dated 25 January 2008 the ECB stated that grass-root participation in cricket increased by 29% during 2006-7. In relation to rugby, the RFU and Premier Rugby stated in a press released dated 30 April 2007 that attendance at matches in the Guinness Premiership has improved year on year. In the 2006-7 season, average attendance rose to 11,000 for the first time, a rise of 7.4% on the previous season with demand outstripping the size of the venues. Furthermore, as noted in the subsequent bullet point on Page 8 of Annex 10 to the Consultation Document, sports bodies must also weigh the very significant benefits to both the "*grass-roots*" and "*overall health*" of their sports that arise from an improved ability to invest in their sports which arise from higher income from television rights. For example, in January 2008 the ECB announced a £30 million investment in facilities and club cricket, the most significant ever injection of funding in cricket in England and Wales.
p. 11	***"There are three main models for how rights are sold"*** The "*models*" in this section oversimplify the process of how sports rights are sold. Furthermore, a distinction should be drawn between (a) the way rights are assembled for sale and (b) the way rights are sold. The first two "*models*" on this page represent the ways in which rights are assembled for sale, while the third "*model*" is an example of a way in which rights are sold (there are other ways of doing so).
p. 15	***"UEFA agreed a new joint selling agreement, starting with the 2003/04 season, whereby*** **[Champions League]** ***rights in each territory would be sold to more than one broadcaster"*** This is inaccurate. UEFA agreed to package Champions League rights in such a way that they *could* be sold to more than one broadcaster, but did not commit to selling to more than one. For example, Premiere bought all of the German

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	rights and the Modern Times Group bought all of the Scandinavian rights.
p. 16	The report claims to review sporting events "*with the greatest appeal to broadcasters and viewers*". The basis of the selection of these events is not stated, but it does not appear to result in a list of events "*with the greatest appeal to broadcasters and viewers*". Most notably, the selection includes only a subset of Listed Events which are, by definition, sports events of the "*greatest appeal to broadcasters and viewers*". The following A Listed events are notably absent: the Grand National, the Derby, Wimbledon, the European Football Championship Finals Tournament and the Rugby World Cup. Non-Listed Events which are also of the "*greatest appeal to broadcasters and viewers*" that are notably absent from the list include: the World Snooker Championships, The US Masters golf tournament, the Ryder Cup, Royal Ascot horse racing, Grand Slam tennis tournaments, the Cambridge-Oxford Boat Race, the London Marathon, Scottish Premier League football, the World Professional Darts Championship, boxing matches, and Tour de France among numerous others. Inclusion of the Rugby League Super League in the list is strange and appears to be motivated more by the early history of the Super League than the criterion of being of the "*greatest appeal to broadcasters and viewers*". Its inclusion is all the more unusual in view of the omission of the events above.
Chapter 1	This chapter purports to profile a selection of football "*events of significant importance to UK broadcasters and/or viewers*". It is particularly surprising that the UEFA European Football Championship is not included in this chapter. The UEFA European Football Championship is the second largest sporting event in the world. Viewing figures for Euro 2004 were higher than for any other single sporting event broadcast in the UK; over 24 million people in the UK watched England lose to Portugal in a quarter-final match during that tournament.[6] The absence of this event from consideration in this chapter of the report is, therefore, puzzling.
p. 37	***"Since 2003, the [UEFA Champions League] rights have been sold in smaller packages to at least two broadcasters in each country"*** This is inaccurate. As noted above, UEFA agreed to package Champions League rights in such a way that they *could* be sold to more than one broadcaster, but did not commit to selling to more than one. For example, Premiere bought all of the German rights and the Modern Times Group bought all of the Scandinavian rights.
p. 48	***"UEFA owns the rights from the quarter-finals onwards, but rights to the early rounds of the UEFA Cup are owned by the clubs"*** It is evident that the Spectrum/ Value Partners report predates the adoption by UEFA of collective selling in November 2007, to apply from 2009/10 season.[7] Accordingly, the information presented in the slide on Page 48 is now of

6 "TV ratings climb for Euro 2004", International Herald Tribune, 5 July 2004 <http://www.iht.com/articles/2004/07/05/tv05_ed3_.php>.

7 "UEFA Executive Committee approves changes to UEFA club competitions", UEFA Press Release, 31 November 2007, <http://www.uefa.com/newsfiles/630630.pdf>.

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	historical interest only.
p. 50	**"*In 2001/02, the Football League achieved a fourfold increased in the value of its rights - however, when ITV Digital failed, 57% of this revenue remained unpaid... Rights were returned to the Football League and were then acquired by Sky for less than 25% of the amount paid by ITV Digital*"** This is erroneous. Sky paid [**CONFIDENTIAL**] % of the amount previously paid by ITV Digital.
pp. 56, 65, 72	**"*The BBC's interactive channel, BBCi, allows it to compete with its multi channel pay TV rivals in bringing comprehensive live Olympics coverage*"** **"*Broadcasters Channel 4 and Sky have been particularly innovative in their coverage of live Test Match cricket*"** **"*Since regaining exclusive rights to the Six Nations in 2003, the BBC has been innovative in its presentation of the games*"** The report greatly underplays Sky's substantial contribution to innovative broadcasting in sports other than cricket, notably in relation to the improvements in the coverage of football that it has introduced.

Annex 11	**Movie markets in the UK**
¶¶ 9 and 54	***"Studios receive around 50 per cent of net VOD revenues. Their share of nascent Internet-based digital rental is about 31 per cent of net revenue."*** Sky understands that studios typically receive around 60% of VoD revenues. Similarly, Sky understands that the studios' share of digital rental is much higher than that claimed here. In addition, FilmFlex is owned by two studios, which effectively increases the proportion of total revenues ultimately received by studios.
¶ 36	***"In line with most pay TV platforms, BSkyB is understood to licence films for pay TV for a maximum of three years."*** A distinction must be drawn between library titles and current titles. Current titles are licensed for a maximum of 15 months, whereas the licence period for library titles can vary greatly. Sky licenses films in its capacity as a broadcaster, not platform operator.
¶ 37	***"Today more than 5m (about two thirds) of Sky Digital subscribers take the premium Sky Movies package... but we anticipate that proportion will slightly decline in the future..."*** [**CONFIDENTIAL**] The report fails to appreciate that the number of such subscribers is already declining.
¶ 38	***"Of the £673m of subscriber revenue that can be attributed to premium movie channels in 2006"*** It is impossible to attribute subscription revenue to premium movie channels in any meaningful way as such channels are provided to consumers in packages that include (among other things) other types of channels. They do not, therefore, have separate retail prices from which estimates of subscription revenues could be derived. Accordingly, the figure of "*£673m*" is spurious.
¶ 39	***"The number of film transmissions on the five major terrestrial channels has declined significantly in the last decade..."*** Screen Digest's own numbers (as shown in Figure 141) show no evidence of a systematic decline, let alone a "*significant*" one, since 2000. A decline prior to 2000 is of little relevance to the current inquiry. In any event, it is wholly misleading to omit from such a consideration the increasing number of films broadcast on free to air channels other than the five major terrestrial channels. ***"...movies are no longer achieving top audience ratings."*** This statement is contradicted by the statement, in the same paragraph, that "*blockbuster films can still deliver mass audiences*", and Paragraph 395 which states that "*Films still offer a way of generating large audiences [for the terrestrial channels]*". ***"Compared with other genres of programming, films are not seen as cost-effective."***

Annex 11	**Movie markets in the UK**
	This is contradicted by the reference at Paragraph 41 to increasing demand for films amongst broadcasters, the existence of dedicated movie channels, and the large number of films broadcast on a wide range of channels.
¶¶ 106-112	Various distributors' market shares are given for 2006. Distributors' market shares can fluctuate significantly from year to year depending on the release cycle, and so the situation at one point in time may not give a representative picture.
¶ 216	***"All rental stores sell on previously viewed titles (PVTs) when a title is no longer new enough to justify retaining a high number of units on the shelves. We have not included revenues from this source in our rentailer level model since they are not included in industry analyses of consumer spending on rental nor do they have any impact on distributor level revenues."*** These are spurious reasons for excluding sale of ex-rental DVDs from the analysis. For consumers, they are a viable substitute to DVD retail and rental, and an alternative to viewing of films on a PPV basis or on linear channels. Significantly, these DVDs are likely to go on sale during the pay TV window, at the time the same films are first shown on Sky's Movie channels.
¶ 220-1	***"This is not to suggest that the online DVD rental market is cannibalising traditional rental. In fact, our analysis indicates that there is little in the way of a correlation between the decline in offline rental and the growth of its online equivalent – traditional bricks and mortar rental is deteriorating at a far quicker rate than online DVD rental sector. (sic) Indeed given that online subscription DVD rental offers such a different consumer experience to 'over-the-counter' DVD rental, it might instead have the potential to expand the pie."*** This is an ad hoc approach to the assessment of substitutability between different ways of viewing films based on impressions rather than rigorous analysis. The growth in online subscription rental is likely to be at the expense of a range of other forms of viewing, not just offline DVD rental. This growth has occurred at the same time as a decline in subscriptions to Sky's movie channels and it is very likely that the two are linked: so although the DVD "*pie*" might expand, this would be at the expense of other "*pies*" such as pay TV subscriptions.
¶ 220-5	***"From a consumer perspective, rental has traditionally been a pastime of the lower socio-economic classes..."*** No source is provided for this assertion. The BVA annual report (based on TNS data) shows that the rental demographic is significantly more affluent than retail.
¶ 245	***"LoveFilm, which boasts some 40,000 titles..."*** This is erroneous. LoveFilm offers over 65,000 titles.

Annex 11	**Movie markets in the UK**
¶ 268	***"We estimate that revenues from TV-VOD services in the UK in 2006 totalled £248m. Movie transaction revenues (pay-per-view payments) for nVOD and VOD represented roughly 60:40, and £70m came from indirect non-transactional revenues (subscription, set-top box rental fee). The latter revenues decreased significantly compared with 2005 when they totalled £100m because Sky stopped charging a PVR rental fee for its premium package customers."*** It is erroneous to include charges for set-top boxes and Sky+ charges in VoD revenues. Such revenues have nothing at all to do with revenues from VoD services. Sky has never charged a "*PVR rental fee*", whether for premium customers or otherwise. (Sky assumes that this is referring to the charge of £10 per month, which was a charge for the use of the PVR functionality of Sky+ set-top boxes.)
¶ 285	***"BSkyB launched 'Sky Anytime on PC' as a PVR-based push-VOD service".*** As its title suggests, Sky Anytime on PC is not a "*PVR-based*" service. Ofcom appears to be referring to the Sky Anytime TV service. ***"The movies (and other selected TV programmes) are 'pushed' to the box after their first transmission on Sky channels..."*** Some programmes are broadcast and recorded by the set-top box prior to their first transmission on a channel. Sky Anytime programmes come from a variety of content providers and therefore do not necessarily appear either previously or subsequently on "*Sky channels*".
¶ 306	***"...retailers and rentailers, online and offline, are exploring the provision of movie downloads as an attempt to compensate for the slowdown in the physical video business. Online DVD rentailers such as LoveFilm have been the quickest to move, launching movie download services in an attempt to re-position themselves as 'one-stop shops' for entertainment."*** Rather than attempting "*to compensate for the slowdown in the physical video business*", LoveFilm is growing its DVD subscription business; digital downloads form an additional revenue stream.
¶ 337-1	***"Apple launched digital retail in the US in September 2006 through its iTunes Store and almost immediately became the number one movie service in the US..."*** Sky notes that iTunes now operates a movie rentals model as well as a retail model in the US. It also has recently started to carry content from BBC Worldwide.
¶ 342	***"Typically, majors will agree a 50:50 split of revenues for new releases and a 40:60 split (in favour of the service provider) for catalogue titles."*** As noted above, Sky believes that the studios' revenue share is typically closer to 60% for new releases.
Figures 124-127	[**CONFIDENTIAL**]

Annex 11	**Movie markets in the UK**
Figures 126 and 127	Figure 127 estimates that Sky's movie channels currently have around 5.7 million subscribers (on DTH and cable) and predicts that this figure will gradually increase over the next four years. [**CONFIDENTIAL**]. Figure 126 estimates the net revenue earned from movie channel subscribers. As noted above (see comment on Paragraph 38), this calculation is spurious.
¶ 376	***"The total amount spent by BSkyB on film rights has declined in recent years because it has negotiated more favourable contract terms and the value of the US dollar has declined against the pound. We have taken the view that because these contracts have been renegotiated fairly recently (many of them in 2006), there will not be a significant worsening in terms from BSkyB's point of view when they are renewed."*** This assumption is not well-founded. [**CONFIDENTIAL**]. In addition, since Sky must make payments under its agreements with Studios in US dollars it is continually exposed to the potential for terms to worsen as a result of changes in exchange rates.
¶ 378	***"…we have estimated the number of movie subscribers at year-end. We believe it was close to 5.5m at the end of 2006."*** It is wholly unclear from this paragraph whether Screen Digest is referring to total Sky Movies subscribers or the number of DTH subscribers to packages that include its movie channels. [**CONFIDENTIAL**]
¶¶ 394-1 and 433	***"In the UK the window that follows premium pay TV, is shared between Free-to-air terrestrial TV and basic cabsat TV."*** This should say that the window that follows the subscription pay TV window is shared between free to air and basic pay TV channels; inclusion of the terms "*premium*", "*terrestrial*" and "*cabsat*" in this statement is erroneous.
¶¶ 395-421	The focus almost exclusively on the five terrestrial channels in the section on "*Free-to-air TV*" belies the vast increase in the number of films shown on other free to air channels (including dedicated free to air movie channels) in the same period, available to a growing audience as the number of people on the satellite and DTT platforms increases.[8] For example, Figure 144 is titled "*Movies on FTA TV*" but relates only the five terrestrial channels. This greatly understates the true number and variety of films shown on free to air channels, even before considering basic pay TV channels.[9] This section bases estimates on the number of movies broadcast on TV on data from the UK Film Council. The UK Film Council is not a standard source

[8] In 2001 there were 3,126 screenings of movies on free to air channels tracked by BARB. In 2006 there were 21,936 screenings on such channels. This includes Film4 only after it became free to air in July 2006. Figures exclude timeshift channels and second screenings of the same movie on the same day on the same channel.

[9] In 2006 there were a further 10,044 films shown on basic pay TV (excluding Sky channels). Again, figures exclude timeshift channels and second screenings of the same movie on the same day on the same channel.

Annex 11	**Movie markets in the UK**
	for this sort of data: BARB is the industry standard.
¶ 410	***"In fact, movies today are mostly considered as 'loss-leaders' from the point of view of broadcasters."*** Sky disagrees with the categorisation of films as "*loss-leaders*" for broadcasters; see comments on Paragraph 39 above.

Annex 13	**Market definition and market power in pay TV**
¶ 2.6	***"Pay-per-view has also consistently been deemed to be in a separate market from subscription pay TV services [in EC decisions]."*** This is erroneous. For example, in *Bertelsmann/Kirch/Premiere*, the Commission stated: "*The market for pay-TV also includes pay-per-channel and pay-per-view.*"[10]
¶ 3.15	***"We recognise that the price offered to [Sky subscribers] also includes a "free" 2Mbps broadband service for customers within Sky's broadband network. However, we estimate that only about 3% of Sky's UK customers currently take up this 'free' service. We therefore believe that ignoring the cost of providing this "free" service is unlikely to have a material effect on the analysis."*** The relevance of broadband to an assessment of both the hypothetical monopolist test and the changing quality of Sky's services over time is not in terms of the cost of provision, but the benefits achieved by Sky subscribers. Ofcom (a) fails to acknowledge that Sky's charges for broadband services are substantially lower than those of many other ISPs and thus provide significant additional value to the pay TV and broadband packages offered by Sky; and (b) fails to recognise that take-up of Sky Broadband is increasing rapidly and so the number of subscribers at a point in time fails to reflect the impact of the product going forwards.
Figure 1	***"Features of television services containing sports programming"*** • The information contained in this table is inadequate as a basis for a proper appreciation of the services and charges for those services that it purports to describe. It comprises a patchy, inconsistent and generally vague description. • The meaning of the title of the table is unclear. Sports programming on subscription TV services (Ofcom's table does not address pay per view services) is generally offered as part of a broader package of services, and so, for example, any discussion of packages including sports programming offered by Sky to DTH subscribers should also discuss non-sports features of those packages – for example basic pay TV channels, PVRs, broadband and telephony. • The description of the table claims that it "s*ummarises the wide variety of premium sports content that is available on the various TV platforms*", but this is not an accurate description either, since the table addresses more than just content, and it is not clear that all the sports programming mentioned is "*premium sports content*" since Ofcom does not define this term. • The organisation of the table is highly confused: some rows appear to relate to television channels or broadcasters (e.g. Sky Sports, Setanta Sports, stand-alone channels); others relate to pay TV packages (e.g. Sky basic tier, Virgin basic tier); while another relates to a particular service –

[10] Paragraph 18, Case IV/M.993 *Bertelsmann/Kirch/Premiere* (1999), Official Journal L 053, Pages 1-30.

Annex 13	**Market definition and market power in pay TV**

	BT Vision.
	
	• The column that purports to describe the programming broadcast on different channels is particularly inadequate. For example, in the case of Setanta Sports, no mention is made of the following programming on channels carried in Setanta's DTH packages or its PPV services:
	
	  • Scottish Premier League;
	  • Blue Square Premiership;
	  • Bundesliga, French Ligue 1, Dutch and Portuguese leagues;
	  • various boxing events;
	  • Magners League rugby;
	  • major golf events including the US PGA Tour;
	  • horse racing coverage from the UK and US;
	  • various Irish sports;
	  • a variety of North American sports (including Major League Baseball, National Hockey League and NASCAR Racing);
	  • channels dedicated to various football clubs: Rangers, Celtic, Liverpool.
	
	• Since the publication of the Consultation Document Setanta has added live rights to the Indian Premier League cricket competition, and rights to distribute Arsenal's football channel to its portfolio.
	
	• Setanta Sports can also be viewed via the internet on a subscription basis.
	
	• The list of channels described as being "*included in Sky basic tier*" packages omits Real Madrid TV and Motors TV. None of the programming broadcast on the channels carried in "*Sky basic tier*" packages is mentioned. For example, British Eurosport's rights include the Beijing Olympics; tennis' French Open, US Open and Australian Open; the three major Cycling Tours: Tour de France, Giro (Tour of Italy), and Vuelta (Tour of Spain); snooker (all World Snooker events); UEFA Euro 2008 near live matches (all 31 games); Le Mans 24 hour race; and live MotoGP. Motors TV offers live coverage of a wide range of motorsports events including V8 Supercars, World Superbikes and Formula 3. Attheraces shows live and highlights of races from tracks throughout the UK, Ireland and North America, including Ascot, Chepstow and Lingfield Park.
	
	• The list of channels described as being "*included in Virgin basic tier*" packages omits Extreme Sports. As with the channels in Sky's basic packages, none of the programming broadcast on this channel is mentioned.
	
	• The programming mentioned in relation to free to air television reflects only a small selection of the range of major rights held by free to air broadcasters. For example, it omits:
	
	  • The US Masters
	  • The French Open tennis tournament
	  • horse racing including the Grand National, Royal Ascot and Goodwood
	  • US Super Bowl
	  • The London Marathon
	  • The British Open golf tournament

<table>
<tr><th>Annex 13</th><th>Market definition and market power in pay TV</th></tr>
<tr><td></td><td>
European Tour golf (live coverage on Saturday and Sunday for BMW PGA Championship, The Barclays Scottish Open, The Quinn Direct British Masters and the HSBC World Match Play Championship) (as part of Euro PGA Tour deal shared with Sky)
Six Nations rugby
Rugby World Cup
Formula 1 motor racing
Football League, including Carling Cup matches
Tour de France
British Super Bikes
University Boat Race
One free to air dedicated sports channel has launched since the publication of the Consultation Document: The Fight Network, a channel devoted to boxing, wrestling and similar sports.
</td></tr>
<tr><td>¶ 4.12</td><td>“Analysis of BARB data for Q3 2007 shows that, of the channels surveyed, there were about 16,900 hours of sports programming broadcast in Q3 2007. Subscribers to Sky Sports would have access to about 14,000 hours of sport (the remaining 2,900 hours are largely broadcast on Setanta). If consumers dropped down to a basic package they would have access to 6,600 hours of sport and if they downgrade to a free-to-air service on DSat they would have access to only 1,300 hours. On DTT, Sky Sports News currently broadcasts free-to-air and provides a further 2,100 hours of programming.”

See Sky’s comments on Paragraph 5.30 of Section 5, above.</td></tr>
<tr><td>¶ 4.16</td><td>“We also commissioned some more detailed consumer research which sought to identify the key drivers of demand for premium sports channels. The research found that:...
The five most important individual events cited by consumers are all football events: the FIFA World Cup (55%), FAPL (52%), Champions League (36%), FA Cup 35% and the European Championships (33%). The most important nonfootball event is Wimbledon, which is cited as ‘must have’ by 29% of our sample;”
Ofcom appears to fail to recognise that five of the six events and competitions cited here are shown either exclusively or to a significant extent on free to air television. Given this, it is difficult to see how reference to them assists in an identification of “the key drivers of demand for premium sports channels.”

Moreover, Ofcom fails to have to regard to the fact that the responses cited are unreliable due to small sample sizes in the survey, as stated in the footnote to Figure 37 of Annex 14. (Ofcom also fails properly to describe the base for this data, which was consumers who regularly watch sport on TV in order to watch a <u>specific competition or event</u>. When the question that was put to these consumers is asked of consumers in general, non-football events – such as Wimbledon and the Olympics – are much more prominent.)

Sky comments further on this data – which is wholly unreliable as support for the point that Ofcom seeks to make - in Appendix 4 of this Annex 6.</td></tr>
</table>

Annex 13	**Market definition and market power in pay TV**
Figure 3	***"Pay TV packages containing premium movie channels"*** • The information contained in this table is inadequate as a basis for a proper appreciation of the services and charges for those services that it purports to describe. It comprises a patchy, inconsistent and generally vague description. • Its title does not accurately describe the table, which includes many different means by which movies can be viewed at home. • "*Sky Premium Movies*" – the channels given for the Movies Mix omits Sky Comedy and Sky Movies Premiere +1, and lists "*Sky Movies*" which actually consists of two channels, at the time the Consultation Document was published named Sky Movies SD1 and Sky Movies SD2. • The description of "*programming*" on Sky's movie channels is erroneous. Sky Movies shows movies from the six major Hollywood studios which have met certain performance criteria, but not their entire output. Sky Movies also shows movies from independent studios, made-for-TV and straight-to-video films, and a large number of library titles outside the pay TV window (see Figure 6 in **Annex 2**, of this Response). • "*Movies from the DVD rental window*", "*Movies DVD retail window*" – there is a single DVD window, rather than separate windows for retail and rental. • "*Free-to-air*" – this section makes no mention of a range of free to air movie channels other than Film Four, including Zone Thriller, Zone Horror, True Movies, True Movies 2, Movies4Men and Movies4Men 2.
¶ 4.57	***"Online subscription DVD rental services may appeal to those consumers who value the convenience of paying monthly or not having to go to a DVD shop. However, they currently represent only 13% of the DVD rental market."*** Online DVD subscription rental services represented 13% of the DVD rental "*market*" in 2006, but this is a young and fast-growing product: it is unsafe to draw conclusions based on data at a point in time, more than a year ago.
¶ 4.68	***"We note in particular the relatively low level of switching to pay-per-view and DVD rental."*** Of the 29% of subscribers who would drop Sky Movies in response to a small increase in the 'incremental price', around a quarter of them would view more PPV movies or rent more DVDs. Sky considers that this does not comprise a "*relatively low level of switching*".
Figure 4	***"Additional channels on the L or XL bundle are not available on free-to-air services."*** This is not correct. For example, Film4+1 is in the L and XL packages and is available free to air via satellite and DTT. Channels such as Zone Reality, Zone Horror, Bliss, Scuzz and Flaunt are in Virgin Media's XL package and are available free to air via satellite.

Annex 13	**Market definition and market power in pay TV**
¶ 4.101	***"Our analysis of product characteristics suggests that: ...*** • ***Although free-to-air channels, and Freeview in particular, share some of the characteristics of basic-tier pay TV packages, basic-tier pay TV packages offer a substantially greater number and range of channels than are available on Freeview;..."*** See Sky's comments on Paragraph 5.52 of Section 5, above.
¶ 5.22	***"The large majority of the most attractive live sports is still only available through Sky's retail packages."*** This statement is not supported by analysis or Ofcom's own survey evidence and ignores sporting events available on free to air channels and on Setanta, including FAPL, international football, UEFA Champions League, FA Cup, Formula 1, international rugby, horse racing tennis, snooker and live coverage of many other sports events.
¶ 5.23	***"Sky offers Sky Sports as part of a bundle including basic pay TV content, whilst Setanta offers its own premium sports channels as a stand-alone product."*** Setanta offers one of its premium sports channels (Setanta Sports 1) as a stand-alone product only via DTT – a fact which is likely to have more to do with the broadcast capacity available to Setanta on DTT than to its preferred business model. On DTH Setanta offers its premium sports channels as part of a package of both Setanta's and third parties' channels.
¶ 5.66	***"Pay-per-view movies, although growing in popularity, remain small in relative terms with a current annual turnover of £80 million. Screen digest estimate that Sky account for over 50% of income generated by pay-per-view movies..."*** Sky's turnover from PPV movies was approximately [**CONFIDENTIAL**] in 2006/07 (excluding revenue from adult PPV services). The majority of the remainder comes from Virgin Media, with a far lower number of subscribers and a far lower proportion of movie subscribers. This suggests that there may be a significant number of Virgin Media subscribers who purchase PPV movies rather than subscribe to movie channels.
Footnote 68	***"The main differences between the basic packages of Sky and Virgin Media are that (a) Sky's basic channels are unavailable to Virgin Media's subscribers, and (b) the Setanta Sports suite is available at no extra charge to subscribers to Virgin Media's XL package."*** Other significant differences between the packages include: (a) the broader range of choice available to Sky subscribers in choosing which basic channels to subscribe to, (b) the tying of a Virgin Media subscription to a Virgin Media phone line, and (c) the range of VoD content offered.
¶ 6.20	The view that there is "*little prospect of supply-side substitution widening this market further*" is inconsistent with the recent expansion of Tiscali TV, entry of BT Vision, announced entry by Orange, and, internationally, the recent launch of many IPTV networks, notably in France. All these examples are of telecommunications operators extending their businesses into pay TV services.

Annex 14	**Summary of quantitative consumer research**
See **Appendix 4** for general comments in relation to Annexes 14 and 15 of the Consultation Document.	
¶ 2.11	***"Figure 3 shows that over four in five consumers are satisfied with the overall service of their MCTV provider. However, these levels of satisfaction are significantly lower than for fixed-line and mobile telephony."*** Ofcom fails to mention in this summary that the proportion of customers who are "*very satisfied*" is higher for digital TV than for any of the other services. (See further Sky's response to consultation Question 1 and Paragraphs 4.4 to 4.8 of **Part 3** of Sky's Response.)
¶¶ 2.24-2.26	***"Our analysis of communications services markets shows that a majority of consumers have neither switched, nor considered a new provider, in the past 12 months. Activity is, however, notably more common for those with broadband as a single service (35% involved in switching or considering) and those with a bundle of services (also 35%), and notably less common among those with pay TV as a single service (12% involved in switching or considering)."*** The answers given in relation to television appear to be limited to multichannel households, excluding analogue terrestrial households. The latter group is important as potential customers for both pay TV retailers and multichannel broadcasters, especially in the lead-up to digital switchover, and will affect pricing and content decisions accordingly. It is relevant to know both how many have switched away from multichannel television and how many have considered a new provider. This point also applies *inter alia* to Figure 14.
¶¶ 4.3-4.5, Figure 24	See Sky's comments on Figure 12 of the Consultation Document in **Appendix 4**.
¶ 4.6 and Figure 25	***"'Must have' types of content "*** As is recognised in the text (e.g. in Paragraph 4.9) this chart is of aspects of content that respondents regarded as being "*important*", not "*must have*" as stated in its title. Furthermore, contrary to the statement in Paragraph 4.6 that the base used for the chart was respondents who regarded "*content*" as "*must have*" the base was in fact respondents who regarded "*content*" as being "*important*".
Figure 41	***"Frequency of watching films... Base: All MCTV households (1970) except [for Sky Movies channels] Sky Movies subscribers (551)"*** It is not appropriate to use a different base for Sky Movie channels than for, among others, "*DVDs – rent by post*". If the objective is to compare the absolute viewing via various means, the base for Sky Movies should be all households. If the objective is to compare frequency of viewing by those able to do so, a valid comparison would be (a) viewing of Sky Movie channels by Sky Movies subscribers with (b) viewing of DVDs rented by post by subscribers to a postal DVD service.

Annex 15	**Summary of focus group research**
¶ 7.3	***"Viewers were also reminded that a premium package subscription such as Sky Sports currently costs £34 - £37. (Interestingly, this came as news to many of those who currently subscribe to premium content, who believed the cost to be less.)"*** Charges for Sky packages that include premium channels are currently between £26-£45 per month. This may explain the comment in parentheses in Paragraph 7.3.

Annex 16	**Summary of competition investigations involving pay TV in other jurisdictions**
The most notable feature of this annex is how little attention is paid by Ofcom to the actual analysis of relevant markets and competition issues in its summaries of the cases cited. Instead, Ofcom's focus is notably almost entirely on the interventions made by regulators in other countries in relation to pay TV services. This balance of emphasis is particularly of note given (a) the importance placed by Ofcom on "*past precedent*" as a starting point for its own approach to the assessment of market definition and market power (evidently without assuring itself that past findings are of relevance to the current case) (see B(iv) of Part 1 of **Annex 2** of Sky's Response) and (b) Ofcom's inappropriate search for potential future problems which may require regulatory intervention in spite of clear evidence that the sector is producing good outcomes for consumers (see Section 3 of **Part 2** of Sky's Response). We note also that the section on a number of regulatory interventions that apply in the United States does not comprise a "*summary of competition investigations*" in the US as the title of this annex would suggest. It is also erroneous to assert that the 1992 Cable Television Consumer Protection and Competition Act was introduced as a result of a "*review of the pay TV industry*" in 1992. Indeed, such a short period of time between a policy review and the introduction of significant legislation in the US context would be remarkable. The background to the introduction of the 1992 Act – which was in significant part a legislative reaction to significant increases in charges for cable pay TV services that occurred following deregulation in the 1980s – is well known.	

APPENDIX 1: AUDIOVISUAL PROGRAMMING DELIVERED VIA THE INTERNET

1 Introduction

1.1 Ofcom's Consultation Document fails to appreciate the importance of programming delivered via the internet. [11]

1.2 Ofcom's ambition in the Consultation Document is to be forward-looking. Yet in relation to an area of the sector that, according to Ofcom's own statements elsewhere, is developing rapidly and of key importance for the future, its discussion is both meagre and focused entirely on the present.

1.3 The inappropriateness of this approach is demonstrated by the significant developments, notably the success of the BBC's iPlayer, which have already taken place since publication of the Consultation Document.

2. Current state of play

2.1 Already over 10 million UK households have broadband internet access, which enables them to download and stream audiovisual content via the internet.

2.2 The internet is increasingly being used to deliver audiovisual programming to end-users both by existing players in the market (such as the BBC, ITV, Channel 4, Sky etc.), and also a host of new entrants, among which the most well-known are Amazon, Apple, Babelgum, Brightcove, Google, Hulu, Joost, Microsoft and Yahoo.[12] They offer a vast range of both free and paid-for content, the scope of which can be seen by looking at examples of the activities of just a few major broadcasters:

- The BBC reported[13] that over 17 million programmes were streamed or downloaded via its iPlayer service in March, and over 42 million since its Christmas launch. It has on average 1.1 million users per week, watching programmes from the BBC's catch-up library of over 400 hours (regularly refreshed) of content.

  The BBC's success can be attributed to content and cross-promotion: the BBC has a powerful library of popular content and has promoted the iPlayer extensively from its broadcast channels and websites. But other services have also demonstrated an increasing acceptance of and demand for internet delivery as they expand their content libraries.

- Channel 4's service, 4oD, has delivered over 100 million programmes since launch in December 2006, including domestic productions, US

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11 Sky also notes that the heading "*IPTV and internet TV*" preceding Paragraphs 3.37-39 of the Consultation Document inappropriately associates these two very different services. We assume this is an error as the distinction appears well-recognised by Ofcom elsewhere in the Consultation Document (e.g. in Paragraph 2.40 of Annex 8).

12 Internet-based movie download services are available from (among others) iTunes, Amazon, Lovefilm and AOL UK (now part of Carphone Warehouse).

13 http://www.bbc.co.uk/pressoffice/pressreleases/stories/2008/04_april/09/iplayer.shtml.

television series and a selection of films and content from the National Geographic Channel, FX and Discovery.

- ITV's service on itv.com was re-launched in August 2007. It delivers around 2 million streams per month, and offers around 140 hours of "catch-up" viewing, together with hundreds of hours of "best of ITV" programming.

- Sky offers around 600 movies, over 1,000 sports highlights, clips from Sky News, and episodes of programmes drawn from channels including Sky One, The Biography Channel, Sky Real Lives, Sky Arts, National Geographic, The History Channel and Crime & Investigation Network.

2.3 This strong trend towards internet delivery can be expected to increase further in 2008 with the launch of Kangaroo, which will offer some 10,000 hours of programmes from the BBC, ITV and Channel 4, and the continued expansion of the range of content offered by other providers such as iTunes, Microsoft, Sony and Lovefilm.

2.4 The UK may also see entry from operators currently active in the US, such as Hulu, a free, advertising-supported service claiming to offer "*the web's most comprehensive selection from more than 50 content providers including FOX, NBC, MGM, Sony Pictures Television, Warner Bros., Lionsgate, and more to deliver premium programming across all genres and formats, television shows, feature films, and clips. Watch full-length episodes of current primetime TV shows such as The Simpsons and The Office the morning after they air, classics like Miami Vice and Buffy the Vampire Slayer, and clips from Saturday Night Live, Nip/Tuck, and others.*" Hulu also offers full-length feature films and a range of HD video clips, noting that "*Widespread High Definition video through the internet is fast approaching. Hulu is committed to the High Definition revolution online.*"[14]

2.5 The internet is also being used to deliver linear channels. For example:

- The BBC simulcasts both BBC News and BBC3 on its website;

- Setanta makes three of its channels (Setanta Sports 1 and 2 and Setanta Golf) available for subscription directly as simulcasts or on demand via the internet;

- Sky simulcasts the Sky News channel and much of its live sport content on the internet;

- The England and Wales Cricket Board recently launched ECBtv, a subscription broadband channel broadcasting live coverage of home Test and one-day international matches to territories where TV rights have not been sold. The ECB and similar bodies have the option to retain internet distribution rights when negotiating the sale of TV rights, or even to launch their own television channels.

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14 www.hulu.com.

2.6 Consumers are displaying an increased willingness to view content on PCs and laptops, associated with the increase in quality and decrease in cost of large PC monitors and laptop screens, increased PC penetration and increased portability of laptops.

2.7 For those consumers who prefer to watch content on television sets, there is a wealth of new technology which can connect television sets to the internet. This includes:

- an increasing number of television sets which can easily be connected to a PC via a cable to act as a monitor, "plug and play" style with no advanced computer skills required[15];
- hardware which can link televisions to PCs using wireless networks, including Apple TV, specialist media centres, and next generation games consoles (such as the Xbox 360 and PS3, each of which is already in more than 1 million UK homes);
- the availability of internet content delivered directly to games consoles such as the Nintendo Wii, PS3 and Xbox 360[16]; and
- add-ons and technology within television sets to allow direct internet connection. Television manufacturers including Sony, Panasonic and Sharp are releasing internet-enabled television sets, which will connect to either the open internet or walled garden audiovisual services.[17]

2.8 While the foregoing clearly provides a brief snapshot of current services and their use by consumers, there is a wealth of similar evidence available which Sky is more than willing to provide if Ofcom remains unsure of the current and future importance of the role of delivery of audiovisual programming via the internet.

3. The informed consensus is that the internet is increasingly important in content delivery

3.1 A wide range of figures in industry – at PSBs, pay TV operators, and hardware manufacturers – as well as regulators and industry commentators have remarked on the growing importance of the internet as a means of content delivery. This section collects a sample of their views.

- The Director General of the BBC described the launch of its own internet download service as "*as big a redefinition of what TV can be, what radio*

15 For example, the 4OD website offers a simple guide on "*How to connect your PC to your TV*".

16 This includes both open internet content available via browers within the console, and additional content delivered specifically to consoles. For example, the BBC recently made its iPlayer service available via the Wii, and Microsoft has added titles from Paramount and Warner Bros to its Xbox Live Video Marketplace in the UK and Ireland. Xbox 360 owners will be able to download titles in SD or HD on a rental basis. Consoles are also converging with other services: from mid-2008 any BT Vision customer will be able to access programming through an Xbox 360 instead of a BT Vision STB.

17 "*Top TV Makers Add Internet Option*," Screen Digest, February 2008.

can be, what broadcasting can be, as what colour television was 40 years ago" and further as the start of "*the video over the internet revolution.*"[18]

- Ashley Highfield, BBC Director of Future Media and Technology (who will shortly become chief executive of Kangaroo), commented on the iPlayer's performance three months after launch:

  > "*Its initial performance proves the case not only for BBC iPlayer, but for all video-on-demand services over the internet, and benefits both our audiences and the industry as a whole. We continue to work closely with the internet service providers with a view to driving the next generation of broadband internet access.*"[19]

- A recent report for the DCMS on the future of broadcasting regulation, which was based on interviews with a range of well placed industry participants, stated:

  > "*Most interviewees were confident that broadband would have a profound impact on the market, leading to radical changes in patterns of distribution, consumption and content type.*"[20]

- ITV has stated:

  > "*Suddenly new media isn't so new any more. The broadband wagon is rolling. Streaming is mainstream. Itv.com includes full streamed access to all ITV channels, catch-up, clips and exclusive content. Within weeks of relaunch, it was attracting over 6 million users in a single month.*"[21]

- Neal McCleave, managing director of media services at Tiscali recently said:

  > "*The price and sophistication of mobile phones, iPods and **internet-compatible TVs** means they're becoming more accessible. Our ultimate aim is for all programming to be platform neutral, so that consumers can choose the way they want to view.*" (emphasis added)

- Nick Colsey, general manager of business planning for Sony Electronics' television group, talking about the internet adaptor developed for use with Sony Bravia television sets, said:

  > "*We think this is what the consumer wants – free video content on the TV screen that complements the free programming that is*

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18 See http://news.bbc.co.uk/1/hi/technology/6245062.stm.

19 http://www.bbc.co.uk/pressoffice/pressreleases/stories/2008/04_april/09/iplayer.shtml.

20 DCMS Report on Future Broadcasting Regulation, January 2007, Page 16 (http://www.culture.gov.uk/NR/rdonlyres/A86E7A41-52F2-452B-B9BF-EB08B5E0EFFF/0/FutureBroadcastingRegulation.pdf).

21 Page 14 of ITV's 2007 Annual Report.

> *already there... That's all part of our idea that internet video will eventually become commonly accepted as part of the TV viewing experience.*" [22]

- Brightcove, a US online video syndication company which entered the UK market in 2007, recently wrote an open letter to the consumer electronics industry, saying the internet was becoming "*the new distribution platform for video content and a clear rival to cable, satellite and terrestrial broadcast*" and that "*the sheer volume of commercial and original video content on the open internet is vastly outstripping any prior platform for video distribution.*"[23]

- Screen Digest predicts that more than 1.5 billion TV shows and specialist programmes will be downloaded or streamed in the UK this year. One of its analysts says that:

> "*It is expected that the success of the BBC's iPlayer open web streaming model, and future 'viral syndication' strategies, will encourage UK commercial broadcasters to enter a long-term reassessment of how they deliver programming to users.*"[24]

- A report on the future of television in The Guardian said:

> "*Long-standing assumptions about the bitter rivalry between TV and the internet are being swept aside as Britain's terrestrial broadcasters venture more online TV on demand, streaming content and near-live simulcasting via the web. ...more people are using the net to catch up on or rewatch their favourite shows, scheduling their own programme of content sourced from the major broadcast outlets. The screen may be smaller, and the range of programming not yet up to that of live channels, but that hasn't halted growth in the range of online services offered by broadcasters such as ITV and C4. Where viewers go, broadcasters must follow.*"[25]

- The Economist has stated:

> "*But as with telephony, the internet is unpicking service delivery from network ownership. Joost, YouTube, iTunes and Netflix do not need their own networks to supply their video services: they can piggyback on fast internet links provided by others.*"[26]

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22 New Media Markets, 22 February 2008.

23 New Media Markets, 22 February 2008.

24 "*iPlayer driving online TV, report says,*" *The Guardian*, 6 February 2008. http://www.guardian.co.uk/media/2008/feb/06/bbc.digitalmedia

25 The Guardian, 3 March 2008. Sky notes that The Guardian's comment that "*the screen may be smaller*" is not correct in the context in which it is made – content delivered via the internet can be viewed via full-sized television sets.

26 The Economist, February 8 2007.

- Ofcom's own publication entitled "*Communications – The Next Decade*"[27] explores the implications of the massive changes occurring in the sector and, in so doing, provides a reasonable overview of such changes – foremost among which is the distribution of content online. The following extract is illustrative of the theme of its contents:

  > *"**Life after broadcasting***
  >
  > *"Note that when I say that broadcast TV is declining, I am not saying that it will disappear.... Only a broadcast model can deal with something such as a World Cup final or news of a major terrorist attack – when the attention of the world is focused on a single event or a single place. But broadcast will lose its dominant position in the ecosystem, and that is the change that I think will have really profound consequences for us all.*
  >
  > *"What will replace it? Simple: the ubiquitous internet.*"

- And, above all, there is Ed Richards' recent comment that:

  > "*The future will never be about linear television alone, but a rich mix of linear TV and new and diverse forms of content and delivery*"

  and one of his "*relevant questions for today*":

  > "*How the value of existing broadcast PSB output can be enhanced by making current and archive content available on demand and in different forms through a variety of media*".[28]

4. Ofcom's reasons for dismissing the importance of the internet in delivering programming to end-users are ill-founded

4.1 Against a background of rapidly evolving services, and widespread commentary about the importance of such services, Ofcom's Consultation Document on the "*pay TV market*" barely mentions them. When it does consider them it simply notes a number of alleged problems with delivery of content via the internet and concludes that:

> *"We do not therefore regard such services as currently providing a credible alternative for pay TV consumers.*" [29]

4.2 The reasons given by Ofcom for dismissing delivery of programming via the internet are technological in nature, as opposed to a lack of demand by consumers or incentive to supply on the part of providers. From that point of view, Ofcom's approach is self-evidently short-sighted.

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27 http://www.ofcom.org.uk/research/commsdecade/. For completeness, Sky notes that it does not endorse all the views set out in that book, but considers it to be useful background to this current consultation.

28 Both quotes are taken from a speech on "The Future of Public Service Broadcasting", March 2008, published at http://www.ofcom.org.uk/media/speeches/2008/03/rtspsb.

29 Paragraph 4.10.

4.3 Ofcom asserts that:

> "*Whilst such services could feasibly begin to compete with the traditional distribution platform, (sic) picture quality, end to end network reliability and capacity limitations of broadband connections may reduce their impact*";[30] and
>
> "*However, the quality of content delivered by this means is likely to be poor, due to the limited bandwidth and high levels of contention associated with current generation broadband services.*"[31, 32]

4.4 Accordingly, Ofcom's alleged problems with "*current generation broadband services*" are as follows :

- issues concerning "*end to end network reliability*";
- capacity limitations of broadband connections; and
- high levels of contention.

The results of these problems are said to be "*poor picture quality*" and poor "*quality of content delivered by this means*".

4.5 Once again, the cursory nature of Ofcom's analysis of relevant issues in the Consultation Document is notable. The quotations above represent the full extent of the 'analysis' of the issues in the Consultation Document – no justification of these propositions is provided, for example in terms of data on bandwidth available to consumers or contention ratios.

4.6 All the alleged problems in delivering content to end-users raised by Ofcom are belied by the simple fact that video over the internet services are already well-established and being used by millions of people in the UK today – as Ofcom is aware.

4.7 Ofcom appears to fail properly to distinguish in its assertions between (a) content <u>downloaded</u> via the internet, and (b) content <u>streamed</u> via the internet. In general, content downloaded via the internet is likely to be as high quality as content delivered via any other digital media and in some cases is HD quality. For example, the video on Channel 4's 4OD download internet service is advertised, correctly, as being "*DVD quality*". Viewing downloaded content does not suffer from problems of 'jerkiness' or buffering, and issues such as capacity limitations and contention affect only the time required to download a piece of content.[33] In the following, therefore, we

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[30] Paragraph 3.39

[31] Paragraph 4.10.

[32] It is not entirely clear whether this criticism is intended, as stated, to be a criticism of the quality of programming available to view via the internet, or the quality of the viewing experience. Given the broad range of high quality content available for viewing already via the internet we have assumed that Ofcom must have intended the latter.

[33] Clearly, if consumers have inadequate hardware then it is possible that the viewing experience may be poor. The same criticism could be levelled, however, at poor quality TV sets; in other words, it is not a meaningful criticism.

have assumed that the problems raised by Ofcom are alleged to arise in relation to streamed delivery of programmes via the internet.

Flaws in Ofcom's analysis of technological problems with delivery of content via the internet

Current provision

4.8 Both DSL and cable services are able to deliver sufficient bandwidth to enable end users to watch content streamed over the internet and it is evident that millions of UK consumers currently do so. ADSL2+ is able to deliver bandwidth of up to 24MB/s under good conditions. However, provision of, for example, 8MB/s connections – which is more than sufficient for the delivery of high quality streamed video services – is therefore well within the capacity of the technology (and capable of being delivered to most users within most local exchange areas). Accordingly, if the types of problems that Ofcom alleges exist currently, it is evident that they are insufficiently significant to have any meaningful impact on either (a) firms' incentives to provide streamed video over the internet services, or (b) consumers' demand for them.

4.9 Streamed video may be (but is not necessarily) of lower picture quality (in terms of clarity of on-screen images) than broadcast television. For many consumers the quality of the picture available via a streamed service is as good as their current digital television service, and potentially somewhat better than they received via analogue television. Moreover, differences in picture quality between broadcast digital media and streamed internet services – to the extent that they exist – are likely to be removed in the medium to longer term with expansions in network capacity and improvements in compression technology.

4.10 To the extent that there may be issues such as 'jerkiness' or buffering associated with watching programming streamed via the internet, it is apparent that Ofcom has overlooked two key factors.

4.11 First, Ofcom ignores the trade-offs that consumers are willing to make between different characteristics of services. To the extent that picture quality or reliability of a streamed internet service is lower than a broadcast television service, consumers may be prepared to trade this off against other attributes, including: the ability to access content that better meets their viewing preferences at any point in time; the ability to 'catch up' with missed broadcast programming; the ability to watch content on portable devices (such as laptops) around the home; and the ability to access content via a range of devices in the home (such as their PC or games console). Early data on usage of the BBC's iPlayer – where the ratio of streamed to downloaded content is around 8:1 – suggests that streamed picture quality is acceptable to large numbers of people. In this regard, Sky notes that evidence suggests that many consumers are not particularly picture quality conscious – for example, the quality of picture on many large television sets sold today suggests that many consumers prefer a larger screen to a crisper picture.

This would tend to suggest that consumers might also be willing to trade off other features against an idealised standard of picture quality.

4.12 Second, Ofcom ignores the fact that there are already technical solutions that are being used to overcome the types of problems that it alleges exist. For example, developments such as ongoing improvements in compression technologies, progressive download, and use by content providers of Content Distribution Networks, among numerous others, are continually improving firms' ability to stream video via the internet and the consumer experience.

Future provision and consumption

4.13 To the extent that Ofcom's arguments have any meaningful content, the issue is whether "*current generation broadband services*" would be able to cope with far greater levels of delivery of programming to end-users in the future – i.e. a scenario in which such a method of consumption became a more significant part of consumers' viewing behaviour than at present.

4.14 In this regard, it is evident that the very high levels of usage of the BBC's iPlayer since its relaunch in January 2008 are already provoking concerns among ISPs as to whether they currently have the capacity in their networks to cope with predicted levels of demand. In theory, large increases in the amount of audiovisual content being delivered over the internet (both streamed and downloaded), all else being equal, have the potential significantly to degrade the service available to end users – for example due to increased contention of backhaul in DSL networks, or in the 'last mile' on cable networks,

4.15 However, Sky considers that to maintain that this is likely to be an issue in the medium to long term would be misconceived. The capacity of broadband networks is likely to be enhanced over time through a mix of additional investment (both in 'core' and 'access' networks – including the potential for investment in 'next generation' access networks) and improvements due to technological change – for example due to adoption of technology such as progressive download for streamed services, and improvements in compression technologies.

4.16 In relation to network investment, it would be unrealistic to consider that a market as competitive as that for the provision of broadband services would fail to respond to consumer demands for the capacity required to receive audiovisual programming via the internet – particularly when one of the key players in that market, Virgin Media, is already upgrading its network to offer very high speed broadband services to end-users and clearly seeking to use its claimed comparative advantage in enabling its users to access audiovisual programming via the internet as a unique selling point for its services.

HD services

4.17 Ofcom also observes that "*the delivery of HDTV over broadband connections is particularly slow with current-generation broadband*".[34] The meaning of this statement is unclear. For example, it is unclear whether it refers to the longer time required to download content that is HD quality in comparison to SD quality video, or whether it is referring to the ability to view content in HD via streamed services.

4.18 In any case, Sky considers that this is an unreasonable criticism as, currently, HD is the 'gold standard' of audiovisual services and therefore an unreasonable benchmark against which to measure the performance of an alternative service. Sky notes that current limitations on the ability to deliver HD services (to the extent that any such limitations exist) are shared with cable - Virgin Media carries only the BBC's test HD service – and the DTT platform, where no programming is available in HD.

4.19 Again, in the medium to long term it seems improbable that the internet will not be an important means by which HD-quality programming is delivered to end-users.

5. Substitutability with pay TV services

5.1 One of Ofcom's reasons for rejecting online delivery of programming as competing with pay TV services is a proposition that, anyone wishing to compete with pay TV services must provide a "*credible alternative*" to such services. Clearly, given the brevity of this statement, which is not elaborated on by Ofcom, it is difficult to ascertain what Ofcom means by it.

5.2 It is important to note, however, that it is not necessary for online delivery of content to be able fully to replicate a broadcast pay TV service in order to affect demand for such services. All else being equal both (a) increasing availability of programming for free via the internet and (b) increasing availability of programming on a VoD basis via the internet would be anticipated to reduce demand for subscription pay TV services. In particular, for many consumers a combination of free to air linear channels and on demand programming (both on a paid-for and free basis) would be a credible replacement for a pay TV subscription. Accordingly, if this was what Ofcom intended in its reference to such developments not being a "*credible alternative*" to subscription pay TV services, then it is erroneous.

6. Conclusion

6.1 Ofcom's failure to appreciate the current and future importance of programming delivered via the internet flies in the fact of consumer trends and the opinion of industry insiders and experts. Such programming is clearly a substitute for content delivered via linear channels and will form an increasingly important constraint on pay TV operators as trends in the range of content available, consumer take-up, network investment and technological improvements continue.

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[34] Paragraph 3.39.

APPENDIX 2: FREEVIEW

1 Ofcom makes various references in the Consultation Document, particularly in Annex 8, to Freeview being a "*platform*" or broadcasting channels. For example:

- "*Freeview broadcasts c. 40 FTA television channels and c. 30 radio channels from a variety of channel owners.*"[35]

- "*BT Vision offers VoD in combination with linear channels carried over Freeview/DTT.*"[36]

- "*only three Sky channels are available on the rapidly growing Freeview platform.*"[37]

2 Although the term Freeview has become synonymous with DTT and/or digital free to air television services in popular parlance, Sky considers that Ofcom, as the sectoral regulator, should adopt a more precise approach.

3 'Freeview' is a brand name, owned by a joint venture company called Digital Television Services Limited ("DTVSL"), which is used in the marketing of the availability of free to air television and radio services available via DTT. It is an 'umbrella brand' and covers any free to air television and radio channel broadcast via DTT, whether or not their broadcaster is a shareholder in DTVSL.

4 Broadcasters which broadcast channels via DTT do so entirely independently of both (a) each other and (b) any broader organisation (particularly DTVSL). In order to broadcast a channel via DTT a broadcaster needs capacity on one of the six DTT multiplexes. Broadcasters either own (e.g. BBC, ITV, Channel 4, five), or lease (e.g. Sky, Setanta), DTT multiplex capacity in their own right and broadcast their channels themselves.

5 DTVSL uses the Freeview brand in two main ways: (a) in its own promotional activities (e.g. its website (www.freeview.co.uk)), and (b) licensing use of the brand to others (such as equipment manufacturers and retailers).

6 Ofcom's reference to the origins of Freeview in Annex 8 is also erroneous. Ofcom states:

> "*In 2002, Sky launched a joint bid with the BBC and Crown Castle (now National Grid Wireless) as a shareholder in the Freeview consortium for the DTT spectrum vacated by ITV Digital.*"

7 The bid for the former ITV Digital multiplex capacity was made by the BBC and Crown Castle alone. One of the commitments given by the BBC and Crown Castle to the ITC in bidding for the multiplex capacity was that they would

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35 Paragraph 3.11 of Annex 8.

36 Paragraph 2.1 of Annex 8.

37 Paragraph 2.22 of Annex 8.

establish a joint venture company (denoted in the bid as 'ServiceCo'), which would include Sky as a joint venture partner. The principal proposed role for ServiceCo (which became DTVSL) was to encourage consumers to purchase the equipment required to receive digital terrestrial television services.

8 Ofcom also appears to equate Freeview in its Consultation Document with free to air multichannel television. Clearly, to the extent that this is the case, it is erroneous, given the very extensive range of free to air channels available via DTH. In this respect, Sky notes that DTH free to air television should not be confused with 'freesat from Sky'. 'freesat from Sky' is an equipment and installation product offered by Sky. The more than 9 million UK households who receive DTH free to air television services are no more "*customers*" of 'freesat from Sky' than households who have purchased a television and paid their licence fee are "*customers*" of analogue terrestrial broadcasting.

APPENDIX 3: OFCOM'S MISPERCEPTION OF ROLES IN THE SECTOR

1. Introduction

1.1 Annex 8 to the Consultation Document indicates a considerable ongoing confusion on Ofcom's part in relation to the roles performed by different entities in the sector.[38] For example, the following statements are erroneous:

- *"Wholesale channel provision - the principal source of revenue for pay TV channels is the channel/channel package fees."*[39]
- "*Retail service provision layer*" - "*This layer involves companies that provide consumers with access to a particular TV platform.*"[40]
- "*The main wholesale services which may be required by retail service providers for broadcasting channels on the different TV platforms include…[satellite capacity], access to masts and antennas used for analogue and DTT broadcasts, satellite uplink services*" [41]
- "*The retail TV service provider arranges for transmission of the channel(s).*"[42]
- "*There also appear to be hybrid 'wholesale' arrangements, whereby channel owners receive all the subscription revenue for their channels, but contract with vertically integrated platform operators and retail service providers to manage some or all of the pay TV arrangements for the channels.*" [43]
- "*Third parties (such as Setanta and Zee TV also retail channels and packages to Sky Digital and Sky Freesat customers).*" [44]

1.2 We discuss these statements further below.

1.3 This confusion is somewhat surprising in view of (a) the length of time that Ofcom has been looking at these issues and (b) the fact that one of the issues that is central to the Consultation Document is vertical integration. Without a proper understanding of the functions performed by entities operating at each

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38 These issues have been discussed with Ofcom on a number of prior occasions, and discussed in Sky's responses to information requests. For example, Sky provided Ofcom with a simple table which explained these issues in relation to the DSat platform at a meeting on 15 February 2007. At the meeting at which that table was provided Ofcom assured Sky that it understood the issues being discussed. We have attached that table again as Appendix 5 to this Annex.

39 Paragraph 2.33 of Annex 8.

40 Paragraph 2.35 of Annex 8.

41 Paragraph 2.44 of Annex 8.

42 Paragraph 2.45 of Annex 8.

43 Paragraph 2.46 of Annex 8.

44 Paragraph 3.67 of Annex 8.

level of the sector, it is difficult to see how Ofcom would be able to reach well-informed judgments in relation to this issue.

1.4 Sky has provided a simplified schematic overview of the roles of different types of operators in relation to DTH, DTT and cable delivery of television services in the UK at Appendix 6 to this Annex.

2. Ofcom's decision not to refer to broadcasters

2.1 Ofcom's proposition that it needs to dispense with the use of the term "*broadcaster*" on the basis that it is 'imprecise' is particularly odd. Ofcom states:

> "*In order to be precise about particular business activities, we have refrained from using the term 'broadcaster'.*"[45]

2.2 Sky considers that such an approach is surprising in view of Ofcom's responsibilities in relation to broadcasting generally, and the apparent ease with which it uses this term in a large range of other issues with which it deals – for example the term is used extensively in Ofcom's review of public service broadcasting. To cite but one example, at Paragraph 1.36 of the Executive Summary of the PSB Review consultation document, Ofcom states:

> "*Those channels have detailed content requirements set out in legislation, but in some genres – arts, religion, children's programmes, drama – ultimately **individual broadcasters** can decide how much they provide.*"

2.3 It is difficult to understand why the term is considered 'imprecise' in relation to the Pay TV Review, but sufficiently precise to be used extensively in the PSB Review.

2.4 The term "*broadcaster*" is, in fact, not 'imprecise'. It corresponds to the function that Ofcom has chosen to label "*wholesale channel provision*" for the purposes of the Pay TV Review.

3. The roles of broadcasters and pay TV retailers

3.1 The distinction between broadcasters and pay TV retailers is relatively straightforward. In broad terms, these entities and the roles they perform are as follows:

- **Broadcasters** – produce television channels (both pay and free to air) and broadcast them.[46] The main types of inputs they require are (a) television

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[45] Paragraph 2.25 of Annex 8.

[46] The sole complication in this respect is in relation to closed 'wire-based networks', such as cable and IPTV networks. In relation to these networks, broadcasters deliver their television channels to the network operators' headends (normally via satellite), and the network operators then **re-transmit** the signal over their networks. In this limited sense, on such networks, the integrated platform operator/retailer **also** undertakes functions that on other platforms are undertaken solely by broadcasters, due to the fact that on these platforms it is not possible for broadcasters to broadcast their signal directly to peoples' homes.

programming, (b) broadcast capacity, (c) broadcast-related services, such as playout and uplink, and (d) channel marketing services.[47]

Alternative ways of referring to broadcasters are as 'channel providers' or 'channel producers', both of which capture the fact that such entities produce television channels (though they fail to capture fully the fact that such entities also broadcast those channels).

It would be misleading to refer to 'pay TV broadcasters' or 'free to air broadcasters'. This is because, while some broadcasters specialise in producing either pay TV channels or free to air channels, there is no reason why broadcasters cannot produce both types of channel – and many do so. For example: (a) Sky, Virgin Media and UKTV all produce both pay TV and free to air channels; (b) in the past, both Channel 4 and ITV companies also produced both pay TV and free to air channels and (c) BBC channels are provided as pay TV channels outside the UK.

Free to air channels: In the case of free to air channels, there is no 'retail' function required – their broadcasters simply broadcast them and those channels are able to be received by anyone with the appropriate reception equipment. Commercial free to air channels are financed from advertising and sponsorship revenues, while the BBC finances its channels from a combination of the Licence Fee and profits earned from its commercial activities.[48]

Pay TV channels: Pay TV channels are 'wholesaled' by broadcasters to pay TV retailers, who on-sell them to subscribers. Pay TV channels are financed from a mix of (a) advertising and sponsorship revenues and (b) carriage fees received from pay TV retailers. (Carriage fees are also known as 'wholesale charges'.) It may be the case that Ofcom is confused by the term 'carriage' in this context. 'Carriage' does not refer to transmission or broadcast of television channels; it refers to the rights conferred on pay TV retailers to 'carry' channels in their pay TV packages.

In a small number of cases television channels are simultaneously pay TV channels and free to air channels – for example, E4 is a pay TV channel via DTH, and a free to air channel via DTT.

Details of the broadcasters that provide television channels in the UK are readily available to Ofcom, as such broadcasters must pay fees to Ofcom each year. They include the BBC, ITV, Channel 4, five, Sky, UKTV, Virgin Media, Setanta, Discovery, Nickelodeon, Jetix, National Geographic, Fox, ESPN, Disney, Turner Entertainment Networks, Sci-Fi, History Channel, Sparrowhawk Media, E Entertainment, Current TV, Fashion TV, Zonemedia, Dolphin, Emap, Chart Show Channels, Manchester United Television, Chellomedia, Sony Entertainment Television, STAR, Playboy TV, and so on.

[47] In relation to the DTH platform only, certain broadcasters encrypt free to air channels in order to prevent them being received in countries for which they do not hold programming rights.

[48] As Ofcom notes correctly, other types of free to air channels are used to generate revenues from sales of products and services to consumers – e.g. home shopping channels or adult chatline services.

- **Pay TV retailers** sell subscriptions to packages of pay TV channels to consumers.[49] They finance their activities from subscription revenues received from their subscribers. Pay TV retailers arrange the encryption and decryption services for the channels they are licensed to carry, in order that only subscribers who have paid the fees necessary to receive their services do so (and that subscribers receive the channels to which they are entitled).

  The main inputs required by pay TV retailers are pay TV channels (licensed from broadcasters), subscriber management services,[50] marketing services (i.e. to attract and retain subscribers) and conditional access services (encryption and decryption).

  The following table sets out the pay TV retailers that (to the best of Sky's knowledge) operate currently in the UK, the methods by which they retail pay TV services, and whether in each case they are integrated into broadcasting.

Table 1.

Pay TV retailer	Methods by which they retail services to consumers	Integrated into broadcasting?
Sky	DTH, Tiscali's IPTV network, 3G networks (jointly with 3G network operators), the internet	Yes
Virgin Media	VM's cable network	Yes
Tiscali	Its own IPTV network	No
Setanta	DTH, DTT, the internet	Yes
Top Up TV	DTT	No
BT	Its own IPTV network	No
Sony Entertainment Television (SET) Asia	DTH	Yes
Aastha Broadcasting Network (UK)	DTH	Yes
Wightcable	Cable	No
Smallworld	Cable	No
Asia TV	DTH	Yes
Ben-Set Limited	DTH	Yes
Channel Punjab (UK)	DTH	Yes
Horizon TV Network	DTH	Yes
GEO TV Limited	DTH	Yes
Nollywood Movies Limited	DTH	Yes
Playboy TV UK / Benelux Limited	DTH	Yes
Portland Enterprises	DTH	Yes
RHF Productions	DTH	Yes
The TV Group Limited	DTH	Yes

49 In order to focus this explanation we have abstracted from services such as pay per view services.

50 E.g. maintaining a database of subscribers and the pay TV channels they are entitled to receive, billing, corresponding with subscribers, answering queries etc.

3.2 For further discussion on the difference between broadcasters and pay TV retailers, see Sky's response to Question 3 of Ofcom's Consultation Document, at **Part 3** of Sky's Response, and Section 3.1 of **Annex 4** of Sky's Response to the Complaint.

4. Vertical integration between broadcasters and pay TV retailers

4.1 A number of operators in the UK are vertically integrated as between broadcasting/channel production and pay TV retailing. As set out in **Table 1**, Sky, Virgin Media and Setanta both produce TV channels and retail pay TV services (which include both their own channels and those of third parties) in the UK, as do a range of broadcasters of Asian and adult channels.

4.2 Ofcom appears to fail to recognise that, where platforms are open, broadcasters are able to retail both their own and third party channels to households that have the ability to receive services via that platform. (The fact that the platform in question may have been developed and is operated by a firm that is itself a broadcaster and/or pay TV retailer is irrelevant to this issue.) Accordingly:

- the arrangement whereby Sky retails pay TV services to households connected to Tiscali's IPTV network is not a 'hybrid wholesale' arrangement. Households that are connected to Tiscali's network who subscribe to Sky's pay TV services are Sky subscribers; and

- the "*direct retail model*" described by Ofcom at Paragraph 2.47 of the Consultation Document is not a different category from the activity undertaken by (a) Sky on DTH and Tiscali's IPTV network, (b) Setanta on the DSat and DTT platforms and (c) Virgin Media on the cable platform. The "*direct retail model*" is simply another way of saying that broadcasters integrate vertically into retailing pay TV services. (The fact that some also choose to license third party channels for inclusion in their packages, as in the case of Sky, Setanta and Virgin Media, is irrelevant.)

5. Technical services used by television broadcasters and pay TV retailers

5.1 The key area of complexity in the sector arises in relation to the provision and procurement of the wide variety of different technical inputs used by both TV broadcasters and pay TV retailers - including inputs such as satellite capacity, terrestrial transmission capacity, conditional access, EPG listings, playout, customer management services etc. Complexity arises in relation to these types of services for a range of reasons, including the facts that:

(i) each television platform operates differently. For example, in relation to Sky's DTH platform, Sky controls and manages aspects of the platform such as the software in Sky set-top boxes, viewing cards and the systems that are used to provide services such as conditional access and EPG listings. It does not, however, own satellites or the set-top boxes in consumers' homes. By contrast, on Virgin Media's cable systems, Virgin Media both owns the transmission capacity of those networks, and the set-top boxes it provides to subscribers;

(ii) there is a significant element of 'two-sidedness' to television platforms such as Sky's DTH platform and cable networks. Platform operators potentially provide technical services to pay TV retailers and television broadcasters, as well as providing services (e.g. dealing with technical queries) and equipment (e.g. set-top boxes) to consumers;

(iii) integration among platform operators and pay TV retailers and/or pay TV broadcasters may obscure the particular roles that each plays. This is evident, for example in relation to Ofcom's attribution to "*retail service providers*" of the provision of equipment such as set-top boxes to end-users. Such integration by broadcasters and/or pay TV retailers into the provision of technical services is commonplace, and principally reflects the costs and benefits to operators as between 'make' and 'buy' decisions. For example: (a) until 1997 the BBC was also integrated into the operation of terrestrial broadcast networks, via its Home Service Broadcast Transmission Division, which was sold to Crown Castle; and (b) Sky is integrated into the operation of call centres, whereas pay TV retailers such as Setanta and Portland Enterprises choose to buy-in such services from a specialist third party provider; and

(iv) in many cases such services may be procured on behalf of other operators. For example, Sky procures listings in Sky's EPG on behalf of channels carried in its packages – normally this would be broadcasters' responsibility. Similarly, operators such as Globecast lease satellite transponder capacity from satellite operators and on-sell it (normally as part of a package of broadcast services) to broadcasters. This can cause confusion as to which entity is usually responsible for procuring particular inputs.

5.2 In general, however, Sky considers that Ofcom's fixation on technical services used by broadcasters and pay TV retailers, and its evident desire to place such services within neatly labelled categories of its own devising, is disproportionate. Such issues are of little or no relevance to Ofcom's consultation and appear only to distract from the key task of achieving a proper understanding of the roles of broadcasters and pay TV retailers.

6. Specific comments on statements in Annex 8 of the Consultation Document

¶ 2.33	***"Wholesale channel provision – the principal source of revenue for pay TV channels is the channel/channel package fees."*** The principal sources of revenue in relation to pay TV channels are (a) carriage fees (or 'wholesale charges') and (b) advertising and sponsorship revenues.
¶ 2.35	**"*Retail service provision layer*" – "*This layer involves companies that provide consumers with access to a particular TV platform.*"** Pay TV retailers do not "*provide consumers with access to a particular TV platform*". Where such a role exists, it is undertaken by platform operators.

¶ 2.44	***"The main wholesale services which may be required by retail service providers for broadcasting channels on the different TV platforms include…[satellite capacity], access to masts and antennas used for analogue and DTT broadcasts, satellite uplink services"*** Such services are required by broadcasters, not "*retail service providers*". Ofcom's failure to appreciate that broadcasters are responsible for broadcasting television channels rather than pay TV retailers is particularly surprising in view of the fact that Sky discussed this specific issue with the Ofcom Pay TV Review case team in relation to Ofcom's information request of 18 July 2007. [**CONFIDENTIAL**]
¶ 2.45	***"The retail TV service provider arranges for transmission of the channel(s)."*** As noted above, broadcasters arrange the "*transmission*", or broadcast, of their channels. In the case of wire-based networks such as cable and IPTV networks, their operators retransmit broadcast signals to their customers' homes.
¶ 2.46	***"There also appear to be hybrid 'wholesale' arrangements, whereby channel owners receive all the subscription revenue for their channels, but contract with vertically integrated platform operators and retail service providers to manage some or all of the pay TV arrangements for the channels."*** These are not "*hybrid 'wholesale' arrangements*". These are retail arrangements.
¶ 3.67	***"Third parties (such as Setanta and Zee TV also retail channels and packages to Sky Digital and Sky Freesat customers)."*** Third parties such as Setanta and Zee TV retail channels and packages to Setanta and Zee TV subscribers. The fact that the addressable base of households comprises households that subscribe to Sky's DTH services, DTH free to air-only households, and subscribers to other DTH pay TV services, is irrelevant.

APPENDIX 4: ANNEXES 14 AND 15 OF THE CONSULTATION DOCUMENT: SUMMARIES OF QUANTITATIVE CONSUMER RESEARCH AND FOCUS GROUP RESEARCH

1. Introduction

1.1 Annexes 14 and 15 summarise the quantitative consumer research and focus group research undertaken by Ofcom.[51]

1.2 The most surprising feature of those annexes is the extent to which they undermine some of the key positions taken by Ofcom in Annex 13 of the Consultation Document in relation to the concepts of "*must have*" content and channels, and the key drivers of pay TV subscriptions. Certainly, they do not provide strong and compelling evidence that either live FAPL football or films broadcast in the pay TV window are "*must have*" content or the "*key drivers*" of consumers' subscription decisions. (See Appendix 2 to **Annex 2** of Sky's Response for further discussion of the "*must have*" concept.)

1.3 Instead, Sky considers that when the evidence is assessed objectively, in the round, it supports the more intuitively appealing propositions that:

(a) while there is a relatively small proportion of dedicated fans of particular types of programmes (which includes football in general, and live FAPL football in particular) among the general population, there are large numbers of people who have little or no interest in those types of programmes, and reasonably large numbers of people who have a moderate degree of interest (i.e. there is a downward sloping demand curve for most types of programming);

(b) there are many dedicated fans of football, live FAPL football and sports in general among Sky Sports' subscriber base. (Since these consumers are those at whom the Sky Sports channels are targeted, this is hardly revelatory.) Equally, however, there are many Sky Sports subscribers who have a moderate interest, or little interest in these types of programming;

(c) most households take up pay TV subscriptions for a variety of reasons, which differ among households; and

(d) for most households, and most pay TV subscribers, neither Sky's sports channels nor Sky's movie channels are "*must have*", in the sense of those channels being of critical importance to the household, or being "*the key driver*" of their subscription decisions.

1.4 A further notable feature of the research results is the relatively narrow gap in response to many of the issues examined in the research between pay TV subscribers and non-pay TV subscribers, and the evident strength of preference

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[51] Sky notes that a substantial proportion of the focus group research is taken up by a wholly redundant discussion of the value to those taking part of the ability to subscribe to pay TV channels on an à la carte basis, which goes as far as hypothesising charges at which pay TV channels would be offered to consumers à la carte.

– even among pay TV subscribers – for free to air channels and programming carried on those channels.

1.5 Sky considers that the gap between the evidence reported in these Annexes and the evident level of attachment on Ofcom's part to concepts such as "*must have*" content suggests that Ofcom has approached these issues from a position of firm preconception, rather than adopting an evidence-based approach. (See **Part 1** of Sky's Response.)

1.6 Finally, these Annexes provide further evidence than that cited by Ofcom in the main body of the Consultation Document about consumer satisfaction with the outcomes delivered by the pay TV sector in the UK.

2. Ofcom's tendency to replace "*important*" with "*must have*"

2.1 Throughout Annex 14 Ofcom tends to use the term "*must have*" when in fact the research results it is reporting relate to questions where consumers were asked whether something is "*important*" to their household. For example, this occurs in relation to Figures 25 – 30 and Ofcom's discussion of those figures.

2.2 Sky considers that this translation of terminology is inevitably misleading. Ofcom should report precisely the questions that were put to consumers.

2.3 We have not repeated this point in relation to each of the erroneous references to consumers saying that certain things are "*must have*" in the quotations below.

Figure 12 in Section 3 and Figure 24 in Annex 14 of the Consultation Document

2.4 In one particular instance, Ofcom's tendency to replace "*important*" with "*must have*" leads to a highly confusing presentation of results.

2.5 One of the questions in Phase 1 of Ofcom's research asked consumers to state those elements that were "*important to their household*" from a list of options – including content, an EPG, interactivity, [the service] provider, bundling, DVR and price/cost.

If they indicated that something was important, Ofcom then asked them whether that element:[52]

- *"must be part of TV services to make it worth having;*
- *[is] really good to have as part of the TV services; or*
- *[is] nice to have as part of the TV services."*

2.6 In reporting the results of this question – in Figure 12 of Section 3 and Figure 24 in Annex 14 - Ofcom reports the percentages of respondents who said that these things are "*important to their household*". Ofcom then, however, introduces a significant degree of confusion in the presentation of this

[52] Ofcom did not ask the follow-up question in relation to price/cost, as it would be nonsensical to do so.

information by stating that these are the "*proportion of consumers who cite elements of their TV service as 'must have'*" – giving the appearance that consumers said that things such as "*content*", or "*price/cost*" are "*must have*" (which would be nonsensical).[53]

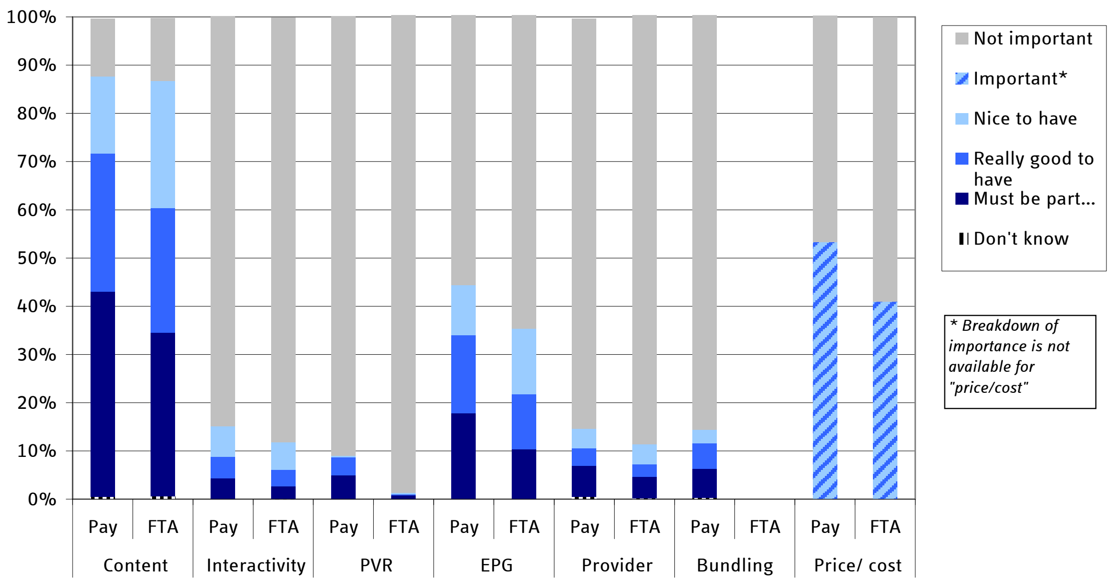
2.7 Given that respondents were asked, however, whether something *"must be part of TV services to make it worth having"*, it is possible to report sensible results in relation to this issue for some elements which were provided as options. It is clear, however, that the percentages of respondents citing particular things as needing to be part of TV services to make them worth having are far smaller than the percentages reported in Figure 12. For example,

- 44% of pay TV subscribers said that an EPG was "*important to their household*". However, only 18% of pay TV subscribers stated that it *"must be part of TV services to make it worth having"*;[54] and

- 15% of pay TV subscribers said that "*interactivity*" was "*important to their household*". However, only 4% of pay TV subscribers surveyed said that it *"must be part of TV services to make it worth having"*.

2.8 An accurate depiction of this survey data is set out in Figure 1, below.

Figure 1: Responses to Ofcom's questions about desirability of particular elements of television services



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53 In Paragraph 4.4 of Annex 14 Ofcom states that it regarded a consumer as stating that a particular element is "*must have*" if they answered **either** that it "*must be part of TV services to make it worth having*" **or** "*[is] really good to have as part of the TV services*". Clearly, given that consumers have been offered the option of stating that something "*must be part of TV services to make it worth having*" adding a less definitive response to the category of "*must have*" is bound to mislead. In any case, the percentages reported were not the sum of these two categories as Ofcom appears to believe.

54 Sky finds this result – particularly in comparison with the lower levels of attachment to PVRs - contrary to the evidence available to Sky. The extent of take-up of Sky+, together with evidence as to the value that consumers place on Sky+, both suggest that Ofcom's survey is likely to be unreliable.

3. Problems associated with small sample sizes

3.1 In a number of the charts reported in Annex 14, the sample sizes become very small. For example, the number of Freeview households that comprise the basis for the results reported in Figure 35 ("***Main reasons for watching sport on TV (multi-coded) by type of consumer***") is 98, while Figure 37 ("***Relative importance of specific sports events regularly watched***") is based on 106 respondents.

3.2 In some places, such as in relation to Figure 37, Ofcom indicates that such results may not be reliable due to a small sample size. It does not, however, apply that approach consistently. Moreover, it is disingenuous to cite results about which there is a significant concern as to their reliability.

3.3 In the following sections, we have not commented on results which may be unreliable due to small sample sizes.

4. Evidence in relation to the importance of particular types of content and channels to consumers

4.1 This section sets out some of the evidence included in Annexes 14 and 15 which suggests the types of conclusions set out in Paragraph 1.3, above, as opposed to the types of conclusions that Ofcom draws from that evidence.

- Figure 23 ("***Main reasons for subscribing to pay TV (2005) – spontaneous***") contains the following results:

	Sky subscribers	Cable subscribers
Live FAPL	4%	2%
Sports channels	22%	25%
Film channels	10%	6%
Documentary channels	2%	4%
Kids channels	10%	5%

  This shows that as many Sky subscribers take pay TV services for children's channels as movie channels; and documentary channels appear to be as important as live FAPL in motivating pay TV subscriptions. Only a relatively small minority (22%-25%) of pay TV subscribers cite sports channels as their main reason for subscribing to pay TV.

- Figure 23 also indicates that by far the reason cited most frequently by Sky subscribers for taking a pay TV subscription is "*more channels*" (in general), at 42%.

- Figures 25 - 29 relate to the responses of the same set of consumers, who stated that "*content*" was "*important to their household*".

- In spite of being labelled erroneously as "'***must have' types of content***" Figure 25 again points to a significant degree of heterogeneity of preferences among both pay TV subscribers and non-subscribers in relation to the importance of specific programmes, genres of programmes, specific channels and genres of channels.

- In Figure 26 ("***Spontaneous channel mentions amongst those for whom content is "must have"***") among pay TV subscribers Sky Sports ranks alongside Discovery (with only 9% of consumers mentioning these channels), and behind BBC1 (25%), E4 (15%), Sky One (12%), and ITV1 (11%). It is marginally ahead of Channel 4 at 8%. Sky Movies is mentioned by only 2% of pay TV subscribers.

- Figure 27 ("***Spontaneous programme mentions among those for whom content is 'must have'***") reports spontaneous mentions of particular programmes. The preponderance of programmes carried on free to air channels is striking – only two out of twenty programmes reported are carried solely or mainly on pay TV channels - as is the absence of sports programmes other than the BBC's Match of the Day.

- In Figure 28 ("***Spontaneous mentions of channel genre among those who say content is 'must have'***"), which reports spontaneous mentions of <u>channel genre</u>, only 25% of pay TV respondents cited sports channels, and film channels (12%) rank alongside children's channels (11%), and documentary channels (9%). Ofcom notes that: "*no other type of channel was mentioned by more than one in ten*",[55] which strongly suggests a wide variety of interest in different types of television channels.

- In Figure 29 ("***Spontaneous mentions of programme genre among those who say content is 'must have'***"), which reports spontaneous mentions of <u>programme genre</u>, one third of pay TV respondents cited sports programmes, and 18% cited films. By comparison, 27% of pay TV respondents cited soap operas and 16% cited documentaries. Only a slightly smaller number of free to air respondents cited sports than pay TV respondents (31% versus 33%), while slightly more free to air respondents cited films than pay TV respondents (21% versus 18%). Again, this evidence points to (a) heterogeneity in preferences and (b) the absence of any particular "*key drivers*" in terms of programme genres.

- Figure 32 ("***Interest in sport in general***") shows that only one third of Sky Sports subscribers describe themselves as "*passionate*" about sports in general – slightly more have either "*no interest*" or are "*interested*" in sport. Among the general population the percentage of people describing themselves as passionate about sport falls to 16%, with a third having "*no interest*". Roughly 30% of those surveyed are "*interested*" – i.e. can be taken to have a moderate degree of interest - in sport; the equivalent figure for Sky Sports subscribers is only marginally higher at 33%.

[55] Paragraph 4.13 of Annex 14.

- Figure 34 ("***Main reasons for watching sport on TV (multi-coded)***") shows that only around one third of "*regular sports viewers*" cite "*specific sport or sports*" as their main reason for watching sport on TV, while around 20% of respondents cite a "*specific competition or event*". Again, it is notable that a relatively small minority of people state that they watch sport on TV in order to watch specific sports or competitions, which accords with a view that many people have a broad interest in sports in general.

- Paragraph 6.5 of Annex 15 states:

  > "*Broadly, pay TV viewers divided into two groups: those who valued range per se and those who valued pay TV…for specific channels or content that would be unavailable elsewhere.*"

  While this seems somewhat over-simplistic, it is notable that this indicates that significant numbers of people "*value range per se*" – i.e., value the increased choice of programming that is provided by a pay TV subscription, and are not motivated to subscribe for very specific reasons.

- Paragraph 6.6 of Annex 15 states:

  > "*In addition to premium content (sic) such as Sky Sports and Sky Movies, a number of other subscription channels were also spontaneously mentioned as reasons to subscribe to pay TV, including, in no particular order, Sky One, Living, UKTV Gold, Discovery, Animal Planet, National Geographic and the Disney Channel.*"

  This provides evidence that people are motivated to subscribe to pay TV services as much for basic channels as the premium channels available, contrary to Ofcom's view.

4.2 Aspects of Ofcom's commentary on the survey results reported in Annex 14 are also of note in view of the extent to which they undermine some of the key propositions put forward in the remainder of the Consultation Document. For example:

- "*Specific and broad types of programme (sic) were a little more important than channels but* ***no one element stands out.***"[56] (emphasis added)

- "*Those who rated programmes or channels as important to their take-up of TV services were asked to spontaneously name what, specifically, was most important to them.* ***Preferences were heterogeneous and tended to be spread over a wide range of content.***"[57] (emphasis added)

- "*Few specific programmes are consistently mentioned by those consumers for whom such content is 'must have'.*"[58]

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56 Paragraph 4.9 of Annex 14.

57 Paragraph 4.10 of Annex 14.

58 Paragraph 4.12 of Annex 14.

- "*As Figure 38 shows, terrestrial channels have a significant share of sports viewing, even on pay TV platforms.*"[59]

- "*Basic and free-to-air TV channels are by far the most popular way to watch films*"[60]

4.3 The extent to which Ofcom is prepared to stretch the interpretation of some of the data reported in an attempt to support its "*must have*"/ "*key driver*" beliefs in relation to live FAPL football is indicated by Paragraphs 5.14 and 5.15 of Annex 14.

4.4 Paragraph 5.14 states:

> "*The importance of sport as a driver of pay TV subscriptions is underlined by the spontaneous reasons cited by existing pay TV customers when explaining their decision to switch. More than two in five said that sports channels were a main reason, second only to more channels in general.*"

4.5 In spite of this evidence being adduced to support the proposition that it 'underlines' "*the importance of sport as a driver of pay TV subscriptions*"[61] no supporting information is provided in relation to these statements. It is unclear what the term "*decision to switch*" refers to, which survey these results are taken from, or what the base of respondents was. Moreover:

(a) the statement indicates clearly that sports channels come second to "*more channels in general*" as a reason for (Sky assumes) taking up a pay TV subscription that includes sports channels; and

(b) it is particularly notable that the paragraph refers to "*sport*" as a driver of pay TV subscriptions rather than live FAPL football.

4.6 Paragraph 5.15 states:

> "*Figure 38 reinforces the importance of football as the most important element of sports content.*"

(Although the statement refers to "*football*" it is evident that it is referring to live FAPL football.)

4.7 Yet, only around one third of the 162 Sky Sports subscribers surveyed indicated that "*live FAPL matches*" were the main reason that they subscribed to Sky Sports. The response that received the greatest level of support was "*took the whole package*" which appears to refer to the value that subscribers place on the whole range of programming provided to them in pay TV packages that include Sky's sports channels.

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59 Paragraph 5.16 of Annex 14.

60 Paragraph 5.19 of Annex 14.

61 Presumably this is intended to mean that "*sport*" is considered to be a driver of take-up of pay TV packages that include premium sports channels, rather than a reference to channels such as British Eurosport or Motors TV driving take-up of basic pay TV packages.

5. Further evidence in relation to consumer satisfaction

5.1 Section 4 of the Consultation Document reports some evidence of consumer satisfaction amongst users of digital TV services. However, Ofcom fails to include in this section a range of further indicators that consumer satisfaction levels are generally very high, and certainly comparable with other communications services.

5.2 For example, Figure 20 of Section 4 suggests that 89% of consumers using Freeview are satisfied, 86% of Sky's customers, and 78% of Virgin Media's customer are satisfied. In Annex 14, however, Ofcom states:

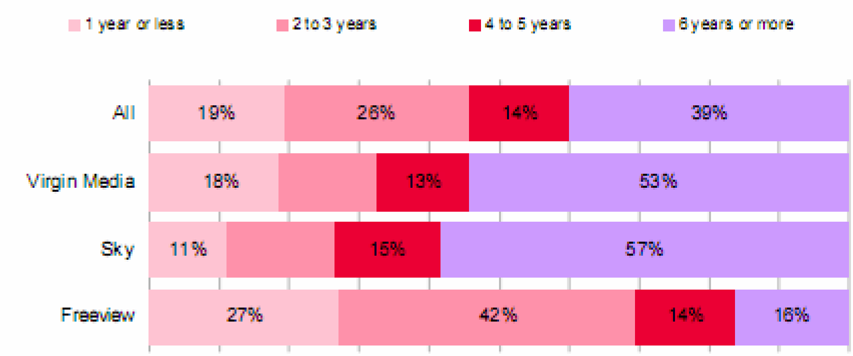
> "*Among those with MCTV as a single service [rather than as part of a bundle], pay TV customers are **significantly more likely than Freeview customers** to say that they are happy with their current provider.*"[62] (Emphasis added)

5.3 Given that a large majority of pay TV subscribers do not currently take bundled services (particularly DTH pay TV subscribers), this is a very important finding.[63]

5.4 Other research reported in Annex 14 also strongly suggests that consumers are satisfied with pay TV, and below we cite several examples.

- The majority of pay TV customers have been receiving multichannel television for 6 years or more. This would normally be taken as an indication that consumers are satisfied with the services they are receiving.

Figure 5: Length of time consumers have received MCTV services



- The large majority of multichannel TV customers have not considered switching, largely because they are satisfied with their current service. Figure 14 shows that 82% of households are not interested in a new supplier. And Figure 12 shows that of those who have not considered switching, 73% are sufficiently satisfied with their current supplier that they have not given the matter any consideration.

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62 Paragraph 2.39 of Annex 14.

63 Given that most cable customers take bundles of services, and cable operators have for many years had well-known customer service problems, it would seem likely that they are dragging down the average in terms of pay TV customers being "*happy with their current provider*".

Figure 20: Likelihood of switching supplier in the next 12 months

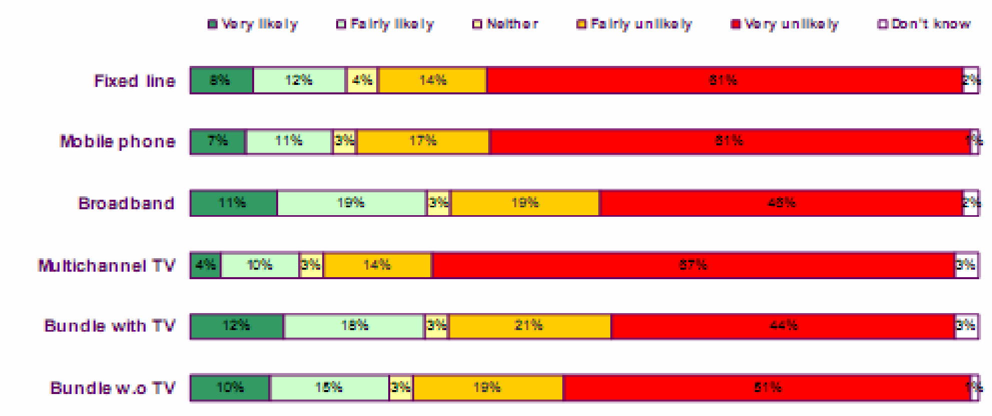
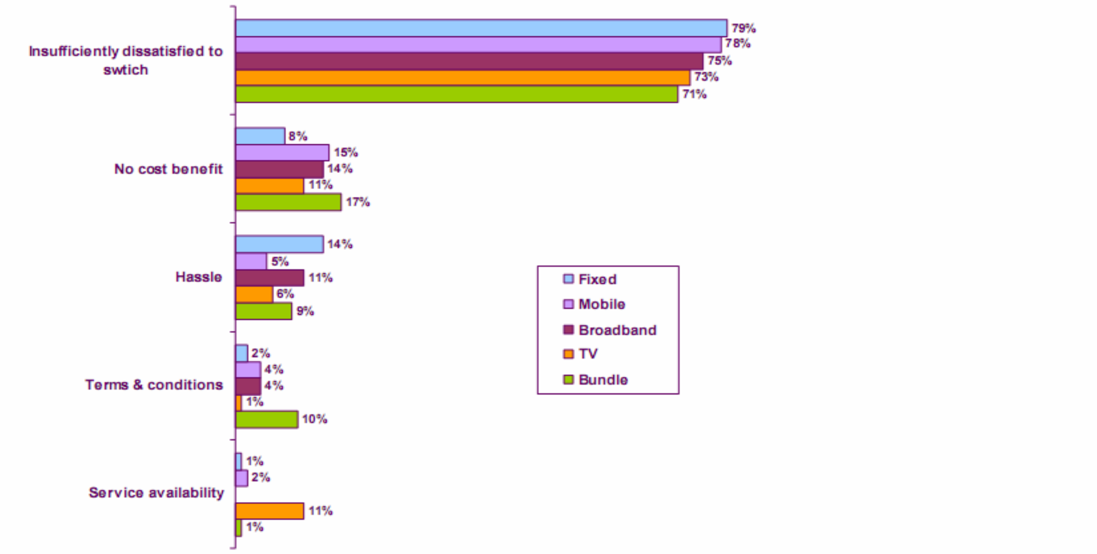
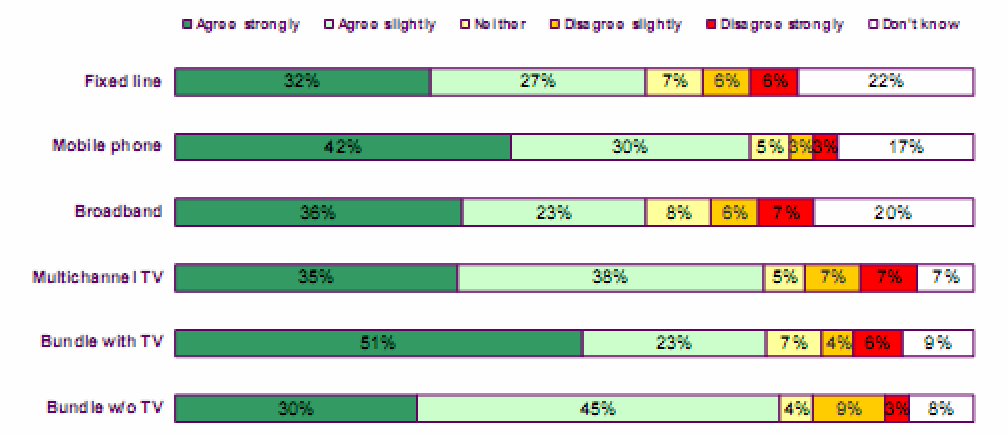


Figure 12: Cross-market comparison of reasons for not considering switching in the past 12 months



- Figure 15 compares the extent to which all consumers for each service agree or disagree with the statement "*Their prices are competitive with other suppliers*". Only 14% of multichannel television customers disagreed with this statement, and amongst those taking a bundle of services including pay TV, only 10% disagreed.

Figure 15: Attitudes towards the competitiveness of current supplier



- Further, Ofcom compares competitiveness of different products and observes at Paragraph 2.49 that:

  "*…consumers with MCTV as a single service have the greatest certainty that they are with the most competitive supplier, and those with bundled TV are particularly emphatic. This helps to explain the lower levels of reported switching in this market.*"

- The qualitative research carried out appears to support this conclusion. In its overview, Ofcom reports that:

  "*The digital TV market was seen as complicated, but viewers were broadly satisfied that the market enabled them to access the content that they wanted to watch.*" [64]

[64] Paragraph 1.3 of Annex 15.

APPENDIX 5: ROLES IN RELATION TO THE DTH PLATFORM

A. Satellite operators

	Typical outputs/ products & services sold		Typical key inputs/ services purchased	
Example(s)	**Description**	**Provided to:**	**Description**	**Purchased from:**
SES Astra, Eutelsat	Transponder capacity	Broadcasters Other transmission services providers In a minority of cases, a distributor may provide transponder capacity to a broadcaster as part of a carriage agreement	(not directly relevant)	(not directly relevant)

B. Other transmission services providers

	Typical outputs/ products & services sold		Typical key inputs/ services purchased	
Example(s)	**Description**	**Provided to:**	**Description**	**Purchased from:**
Arqiva, Globecast, Sky	Services such as uplink, multiplexing, playout Transponder capacity[65]	Broadcasters	Transponder capacity	Satellite operators

[65] Typically, larger broadcasters acquire transponder capacity directly from satellite operators whereas smaller operators are likely to acquire it from a transmission service provider as part of a package of broadcast services.

C. Broadcasters

	Typical outputs/ products & services sold		Typical key inputs/ services purchased	
Example(s)	**Description**	**Provided to:**	**Description**	**Purchased from:**
BBC, ITV, Channel 4, five, RTE, S4C, TG4, Sky, Setanta, Zee TV, Disney, Discovery, UKTV, Simply Media TV Limited, ARY Digital UK Ltd, Sparrowhawk Media Ltd, Racing UK, Flextech, Music Choice Europe Ltd., Emap, Viacom, Hollywood TV Ltd., 4D Telecom Ltd, Geo TV Ltd., Dolphin Broadcast Services Ltd.	Television channels	Viewers, in respect of free to air channels Distributors/ retailers ("wholesale supply") in respect of pay TV channels: (i) where the broadcaster is integrated vertically into distribution/retailing provision of channels is on a self-supply basis (ii) where the broadcaster does not also act as a distributor/retailer, channel supply is in accordance with terms included in **distribution/ carriage agreements** under which the broadcaster licences its channel(s) to a distributor in return for **carriage fees**	Transponder capacity	Satellite operator
			Playout, uplink (and potentially transponder capacity)	Other transmission services providers
			EPG listings	Sky
			Programming, programming rights	Rights providers Internal supply (i.e. programme production)
			Distribution/ carriage of channels	Either third party distributors/ retailers, or distribution/carriage provided internally
			Regionalisation	Sky
			Interactive application signing services (an access control service)	Sky
			Authentication services (Note: platform provider (Sky) supplies wholesale authentication services to retail providers of authentication services)	Authentication services provider (may be internal supply). Current authentication service providers are Sky, QVC and DTPC.
	Advertising airtime	Advertisers (either directly or via an airtime sales house)		

D. Pay TV distributors/ retailers[66,67]

	Typical outputs/ products & services sold		Typical key inputs/ services purchased	
Example(s)	**Description**	**Provided to:**	**Description**	**Purchased from:**
Sky, Setanta, Zee TV, Northern & Shell, Playboy, RHF Productions Ltd	• Carriage • Channel packaging and pricing • Marketing of pay TV services • Subscriber management (e.g. inquiries, billing)	Broadcasters	TV channels	Broadcasters
			EPG listings	Sky
			Conditional access services (e.g. encryption/decryption)	Sky
			Customer management services (CMS)	CMS provider (e.g. Sky, MGt, Appletree)
			Marketing	Advertising agencies + internal supply
	Pay TV packages	Subscribers		

66 In principle free to air broadcasters also undertake a distributor/ retailer function, distinct from their role as a provider of television channels. For example, the BBC and ITV both produce channels (e.g. BBC1, BBC2, ITV1, ITV2) and distribute them via the analogue terrestrial, DTT and DSat platforms. We have omitted reference to distribution of free to air channels in order to simplify the exposition.

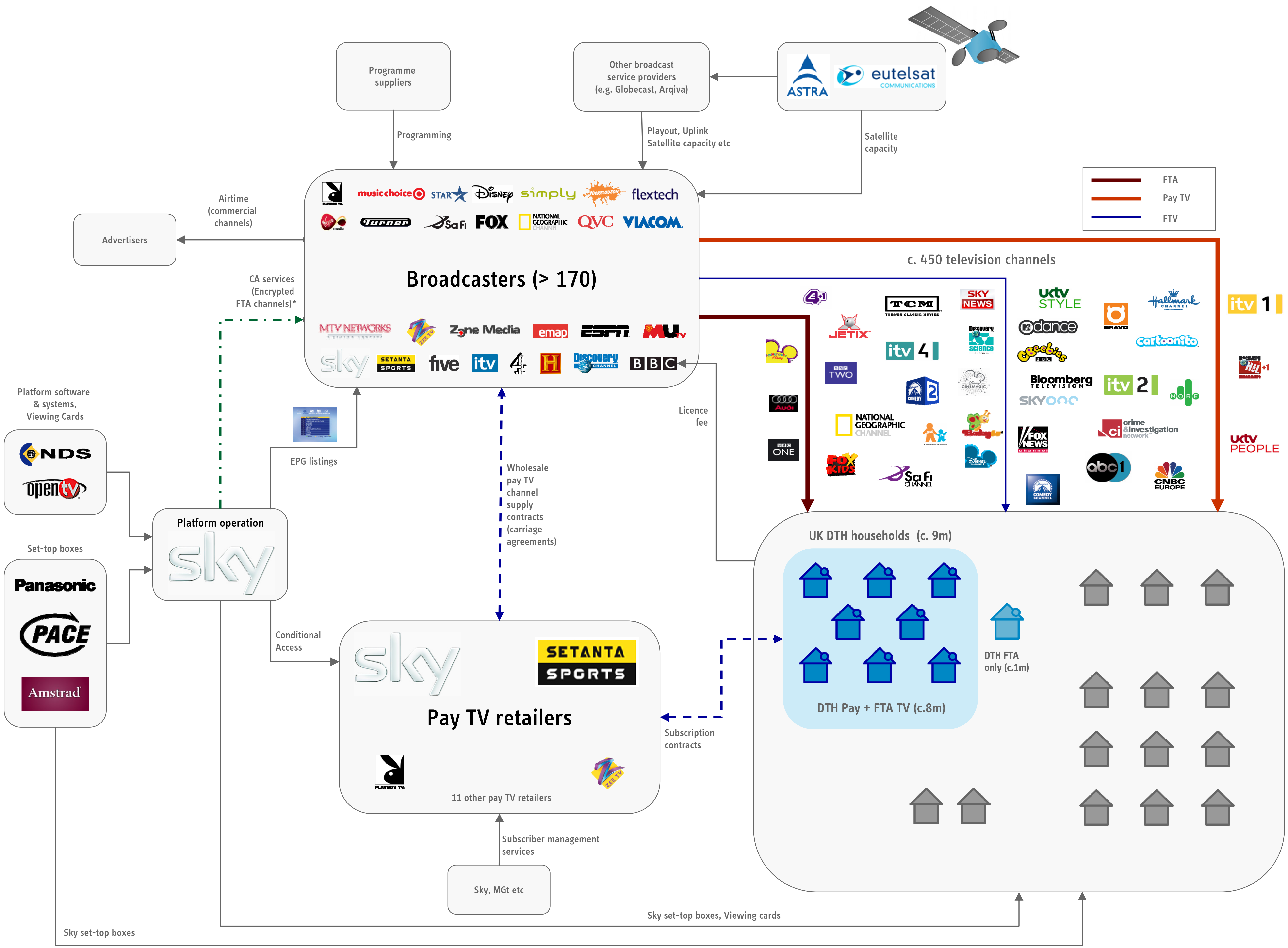
67 The terms distributor and retailer are interchangeable.

E. Platform operator

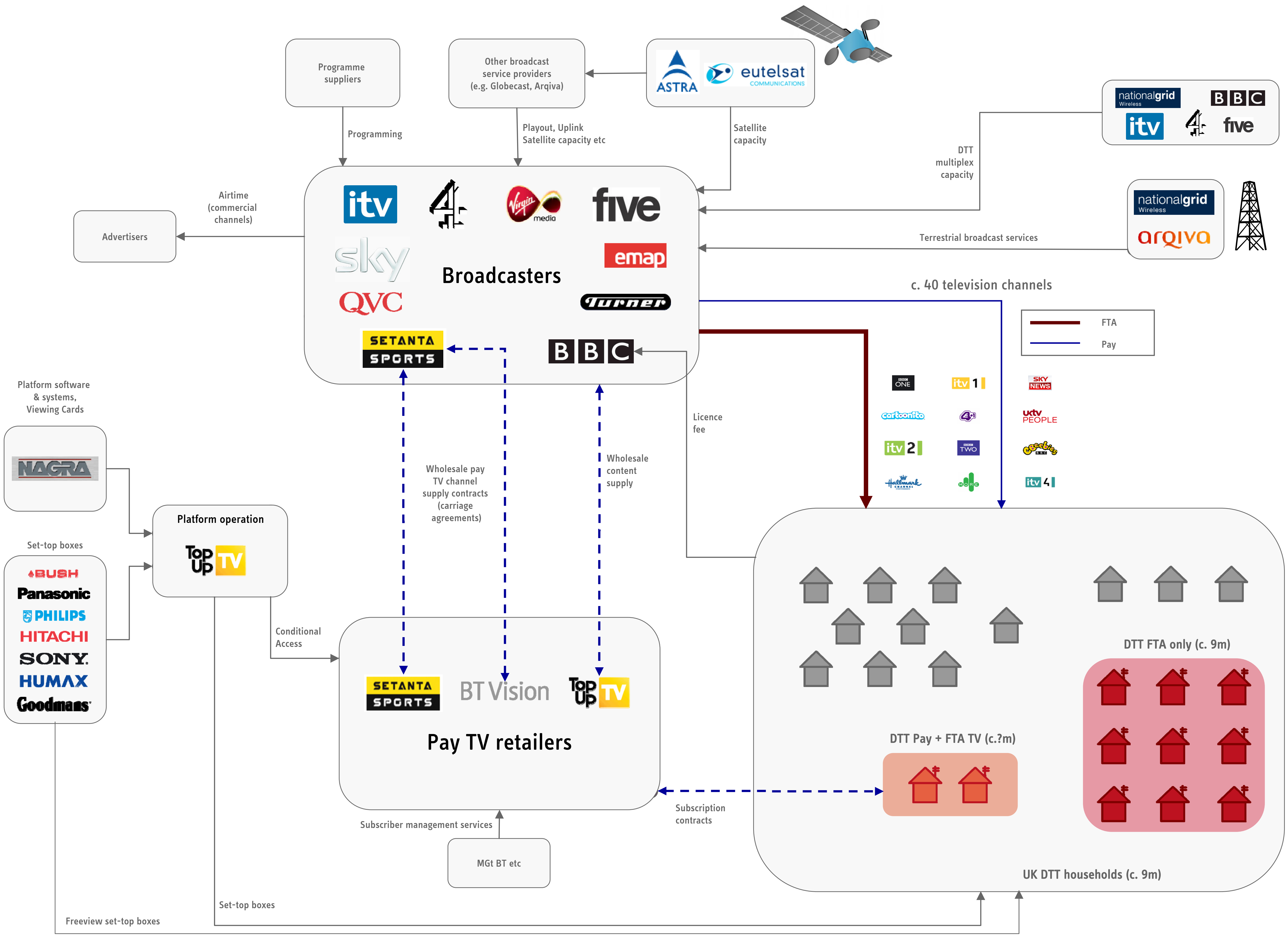
	Typical outputs/ products & services sold		Typical key inputs/ services purchased	
Example(s)	**Description**	**Provided to:**	**Description**	**Purchased from:**
Sky	EPG listings	Broadcasters Distributors/retailers	EPG system	Self supplied
			Transponder capacity	SES Astra
	CA services	Distributors/ retailers	CA system, CA technology	Self supply/ NDS
	Regionalisation services	Broadcasters	CA system, CA technology	Self supply/ NDS
	Access control services	Broadcasters Authentication service providers	AC system Authentication servers POP network	Self supplied
	EPG	DTH households (NB: not "subscribers" – these are also provided to customers of the freesat from Sky service, and former subscribers to pay TV services retailed on the DSat platform)	EPG system	Self supplied
	Set top boxes, dish & LNB		Set top boxes	Set top box manufacturers
	Viewing cards		Viewing cards	NDS
	Platform marketing		Marketing	Advertising agencies Self supplied
	Platform user management (e.g. dealing with technical queries)		Call centre services	Self supplied

APPENDIX 6: SCHEMATIC REPRESENTATION OF ROLES IN RELATION TO DTH, DTT AND CABLE DELIVERY OF TELEVISION SERVICES IN THE UK

Roles in relation to the DTH platform in the UK



Roles in relation to DTT in the UK



Roles in relation to cable in the UK