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OFCOM'S PROPOSAL TO REGULATE ACCESS TO PREMIUM
TELEVISION CONTENT: SOME THOUGHTS

Pablo Ibáñez Colomo

EUROPEAN UNIVERSITY INSTITUTE, FLORENCE
DEPARTMENT OF LAW

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PABLO IBÁÑEZ COLOMO

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Abstract

In September 2008, Ofcom submitted a consultation document dealing with the regulation of access to premium television content in the UK. Ofcom's proposal reflects some tensions in the electronic communications sector which are in part the consequence of the choice made in 2002 to exclude television content from the scope of the Regulatory Framework adopted at the Community level. The British regulator proposes a solution based on the imposition of a compulsory licensing obligation on BSkyB—the leading supplier of pay television services in the UK. In essence, this approach amounts to extending to premium television content the mandated access regime that currently applies to the telecommunications infrastructure under the Regulatory Framework. The present piece provides a critical account of the regulatory proposal and details some reasons why this move may not be justified. In addition, its likely impact on the electronic communications sector at large is examined.

Keywords

audiovisual policy - competition law - economic law - European law - law regulation - telecommunications policy - UK

Ofcom's Proposal to Regulate Access to Premium Television Content: Some Thoughts

Pablo Ibáñez Colomo*

Introduction

In September 2008, Ofcom—the regulatory authority with jurisdiction for the regulation, *inter alia*, of the television and the telecommunications in the UK—issued a consultation document (the “consultation document”) in the context of its market investigation into the functioning of the pay television segment.¹ The document proposed that BSkyB, the largest pay television supplier in the UK, makes its premium television channels available to its downstream competitors on regulated terms.² Ofcom's proposal comes as a response to the submission made in 2007 by a number of BSkyB's competitors (BT, Setanta Sports, Virgin Media and Top Up TV) asking the regulator to submit a market reference to the Competition Commission.³

The joint submission revolved around the competition conditions in the markets for the acquisition and exploitation of premium television content (top-flight sports events, in particular English football championships, and recent film releases), in which BSkyB has been dominant for more than a decade in the UK. The parties went as far as to request the “functional divestiture” of BSkyB, i.e. the splitting up the company into a wholesale arm, in charge of the exploitation of premium television channels and a retail arm, in charge of exploiting the pay television platform.⁴

The proposals finally endorsed in Ofcom's consultation document were received by analysts as a middle-way between the demands of these competitors and BSkyB's commercial interests.⁵ Instead of structural measures, the regulator expressed a preference, from a substantive perspective, for behavioural remedies—which lead, in practice, to a similar outcome—and, from a procedural perspective, did not find it necessary to submit a reference to the Competition Commission. In this regard, the regulator found it more appropriate to deal with the concerns expressed in the submission through its own power to promote competition under the 2003 Communications Act—more precisely Section 316 thereof.⁶

While disagreements between BSkyB and its downstream competitors (in particular, cable operators) regarding the conditions for the supply of premium television content are not new,⁷ several

* Researcher, European University Institute. E-mail: pablo.ibanez@eui.eu. I am grateful to Filomena Chirico, Heike Schweitzer and Bruno de Witte for their helpful comments and their interest.

¹. Ofcom, *Pay Television Consultation – Access to Premium Content*, 30 September 2008, available at <http://www.ofcom.org.uk> (hereinafter, “Ofcom's consultation document”).

². Ibid., Section 8, pp. 170 et seq.

³. Submission to Ofcom on the need of a market investigation into the pay TV industry, 3 July 2007, available at <http://www.ofcom.org.uk> (hereinafter, the “Joint Submission”).

⁴. Ibid., pp. 37 et seq.

⁵. See e.g. Andrew Hill, “Ofcom sets up a challenge for Sky”, *Financial Times*, 30 September 2008.

⁶. Ofcom's consultation document, pp. 178 et seq.

⁷. In 1996, the OFT accepted undertakings from BSkyB following an investigation see The Director General's Review of BSkyB's Position in the Pay TV Market, December 1996. In 2002, the OFT closed proceedings against BSkyB for an alleged abuse of a dominant position after it found no evidence of anticompetitive behaviour by the company; see the Decision of the Director General of Fair Trading, No CA98/20/2002 – BSkyB investigation: alleged infringement of the Chapter II prohibition, 12 December 2002.

developments explain why Ofcom has been involved in these disputes once again at this point in time. As a consequence of technological evolution, the number of actual and potential downstream competitors to BSkyB had already significantly increased in 2007. It can be expected that in such a context pressure mounts on the regulators to make BSkyB's premium channels more widely available.

Among the delivery technologies that are growing in importance, broadband Internet via telecommunications platforms—generally relying on xDSL standards—is the most promising one. In several Member States of the EU, most notably in France, DSL operators have captured the majority of new subscriptions to pay television services in the past three to four years.⁸ In the UK, BT has launched, with little success so far,⁹ its own hybrid terrestrial-DSL pay television service. BT is one of the operators which has not reached an agreement with BSkyB for the supply of the latter's premium television channels. Another one is Setanta Sports. The latter has emerged largely as a result of the intervention of the European Commission in the context of the *Premier League* case, in which the football league was required to make at least one of its live packages of television rights available to one of BSkyB's competitors.

More decisive than technological evolution is probably the inability of *ex ante* regulation to cope satisfactorily with these developments. Of particular importance is the fact that the current EU Regulatory Framework for electronic communications (the "Regulatory Framework") ignores the growing interplay between broadband, voice telephony and television services (the so-called "triple play"), since the choice was made to exclude "television content" from its scope.¹⁰ So long as telecommunications operators were not active in the provision of television services—and this possibility was not an immediate prospect in 2002—the limited scope of the Regulatory Framework was unproblematic. In a changing environment, however, it is likely that television content has an impact on competition in electronic communications markets, without the Regulatory Framework providing for an adequate response.

For instance, with the evolution of xDSL technologies, the incumbent telecommunications operator in a given Member State may protect its dominant position in the downstream broadband market by exploiting television rights on an exclusive basis, as it is not obliged to share them with new entrants under the Regulatory Framework. This is the strategy seemingly followed by Belgacom in 2005, when it acquired the exclusive rights for the Belgian football championship.¹¹ By the same token, a new entrant in the broadband Internet segment may rely on the Regulatory Framework to gain access to the incumbent telecommunications operators' infrastructure, but will remain free to exploit its premium television channels at will. Unsurprisingly, telecommunications incumbents such as BT have claimed that the latter scenario, which corresponds to BSkyB's strategy, is a source of "regulatory asymmetry".¹² At first glance, it may indeed seem awkward that the incumbent telecommunications

⁸. For a recent review of market developments in France, see *La Lettre de l'Autorité*, No. 63, September/October 2008, available at www.arcep.fr.

⁹. Andrew Parker, "Pitch battle starts as BT eyes BSkyB's net gains", *Financial Times*, 14 October 2008. By the end of 2008, BT Vision had around 350,000 subscribers to its service.

¹⁰. See in this regard the Preamble of Directive 2002/21/EC of the European Parliament and the Council on a common regulatory framework for electronic communications networks and services ("Framework Directive"), OJ [2002], L 108/33, referred to supra: "[...] It is necessary to separate the regulation of transmission from the regulation of content. This framework does not therefore cover the content of services delivered over electronic communications networks using electronic communications services, such as broadcasting content, financial services and certain information society services, and is therefore without prejudice to measures taken at Community or national level in respect of such services, in compliance with Community law, in order to promote cultural and linguistic diversity and to ensure the defence of media pluralism. [...]".

¹¹. Decision n. 2005-IO-40 of 29 July 2005, *Telenet v Belgacom*, Rep. 2005/03, p. 27.

¹². Sarah Arnott, "BT challenges Sky's dominance of pay TV", *The Independent*, 15 July 2008. In this article, the chief executive of BT Vision was reported as saying: "There is a real problem in the regulatory regime in the converged

operator is required to share its infrastructures on a non-discriminatory basis but new entrants are relieved from similar obligations regarding valuable inputs.

Finally, BSkyB's commercial practices, which have been perceived as being aggressive may have contributed to the opening of an investigation by Ofcom. In 2006, the pay television operator acquired a 17.9 percent stake in the terrestrial operator ITV, in what was perceived by many as a strategy aimed to frustrate a similar move planned by the cable operator Virgin Media.¹³ Some months later another dispute saw BSkyB pulling its basic television channels out of Virgin Media's line-up.¹⁴ BSkyB's plans to make some of its premium channels available via the DTT platform Freeview were also perceived with reluctance by Ofcom and its downstream competitors.¹⁵

The present piece examines Ofcom's proposals in their regulatory and economic context and evaluates their consequences of on the electronic communications sector at large. When compared to other Member States, the regulatory landscape concerning pay television services in the UK is peculiar in many ways. This will make the first part of the paper, together with a summary of Ofcom's proposals. The second part of the paper explains why Ofcom's intervention would depart from well-established principles under competition law. In addition, some directions for regulatory intervention in the pay television sector are proposed.

An Overview of Ofcom's Proposals

A Peculiar Regulatory Landscape in the UK

The launch of satellite pay television services represented, in the 1990s, a major development in those countries, such as UK, France, Italy and Spain, in which the vast majority of its citizens relied on analogue terrestrial television at the time. From a technological standpoint, the number of available channels increased substantially, and particularly so following the rapid digital upgrade of pay television during the mid-1990s. Other consequences were less obviously beneficial for viewers, in spite of the quality improvements resulting from them. In particular, the quick "migration" of top-flight sports events, with the exception of those of "major importance" for society,¹⁶ towards pay

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market—the rules that apply to telecoms and to pay TV are completely asymmetrical”.

¹³. See, in particular, Competition Commission, Acquisition by British Sky Broadcasting Group of 17.9 Per Cent of the Shares in ITV plc, Report sent to the Secretary of State (BERR), 14 December 2007.

¹⁴. Virgin brought an action against BSkyB before the High Court for an alleged abuse of dominance, see “Virgin Media Challenges Sky's Anti-Competitive Behaviour in the High Court”, 12 April 2007. The dispute was resolved in November 2008, when BSkyB agreed to resume the provision of its basic channels on pay TV.

¹⁵. In April 2007, BSkyB proposed Ofcom to replace the channels its offers via Freeview with a selection of its premium channels Sky Sports and Sky Movies. Ofcom decided to link the approval of these services to the outcome of the market investigation into pay television. A consultation document dealing with BSkyB's proposals regarding its premium television service via DTT was also issued in September 2008, see Ofcom, “Proposed BSkyB Digital Terrestrial Television Services”, 30 September 2008, available at www.ofcom.org.uk.

¹⁶. When the Television without Frontiers Directive was amended in 1997, an “anti-siphoning” mechanism was provided for to prevent the migration of some types of television content towards pay television. Article 3(j) of the current Audiovisual Media Services Directive (Council Directive 89/552/EEC of 3 October 1989, as modified by Directive 97/36/EC of the European Parliament and the Council of 30 June 1997 and by Directive 2007/65/EC of the European Parliament and the Council of 11 December 2007 on the coordination of certain provisions laid down by law, regulation or administrative action in Member States concerning the pursuit of television broadcasting activities, OJ (1989) L 298/23) reads as follows: “Each Member State may take measures in accordance with Community law to ensure that broadcasters under its jurisdiction do not broadcast on an exclusive basis events which are regarded by that Member State as being of major importance for society in such a way as to deprive a substantial proportion of the public in that Member State of the possibility of following such events by live coverage or deferred coverage on free television. If it does so, the Member

television involved a cultural change for viewers used to receive these services on a free-to-air basis.¹⁷ As a result, most games of the national football championship are nowadays available as a premium television channel or on a pay-per-view basis.

Competition between pay television operators has followed a similar pattern in the “terrestrial” Member States of the EU, such as those mentioned *supra*. Head-to-head rivalry in the markets for the acquisition and the exploitation of premium television content proved untenable in the long-run, with this leading to the consolidation of the pay television segment across the EU. Several mechanisms were put in place to tackle this tendency. Exclusive agreements between television operators and right holders became subject to permanent scrutiny under competition law.¹⁸ Similarly, regulation at the national and the European level introduced strict conditions regarding access to the physical “bottlenecks” (in particular, technical services for pay television).¹⁹

Even though these regulatory efforts proved plainly ineffective to stop or prevent what seemed an inevitable tendency towards consolidation, competition authorities initially proved reluctant to clear mergers—which in many cases created superdominant positions, if not quasi-monopolies—until it was eventually understood that a “regulated solution” to the issues raised by mergers was preferable than an outright prohibition.

This “regulated solution” to mergers in the pay television segment rested on two major assumptions. To begin with, decisions in the field, since *NewsCorp/Telepiù*,²⁰ convey the idea, explicitly or implicitly, that the acquisition and the exploitation of premium television content are two activities that bear some features of a natural monopoly, in that competition for the acquisition and the exploitation of premium content being difficult to sustain. The pay television segment indeed showed a clear tendency to tip in favour of the leading operator. Indirect network effects can be identified at two levels of the value chain. The operator with a lead in the markets for premium television content (i.e. the operator having more attractive premium rights) tends to attract more subscribers, which in turns results improves the likelihood that the operator will successfully bid for premium content in subsequent auctions. Moreover, since consumers must typically acquire or rent costly equipment, they may subscribe to the operator with a lead in the number of subscribers; alternatively, they may wait until the market tips in favour of one of the players.²¹ A second assumption underlying these decisions is that access to premium television content is indispensable for competition to be restored at the downstream level.²²

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State concerned shall draw up a list of designated events, national or non-national, which it considers to be of major importance for society. It shall do so in a clear and transparent manner in due time. In so doing the Member State concerned shall also determine whether these events should be available by whole or partial live coverage, or where necessary or appropriate for objective reasons in the public interest, whole or partial deferred coverage”.

¹⁷. An analysis of the question can be found in Stefan Szymanski, “Why have premium sports rights migrated to Pay-TV in Europe but not in the US?”, in Claud Jeanrenaud and Stefan Kesenne (eds.), *The economics of sport and media*, Edward Elgar, Cheltenham, 2006, pp. 148-159.

¹⁸. Besides the *Premier League* case, prominent cases include Commission Decision of 19 January 2005, *Bundesliga*, OJ (2005) L 134/46 and Commission Decision of 23 July 2003, *UEFA Champions League*, OJ (2003) L 291/25.

¹⁹. See, in particular, See Article 6 of Directive 2002/19/EC of the European Parliament and of the Council of 7 March 2002 on access to, and interconnection of, electronic communications networks and associated facilities (“Access Directive”), OJ (2002) L 108/7.

²⁰. Commission Decision of 4 April 2003, *NewsCorp/Telepiù*, OJ (2004) L 110/73 (hereinafter, “*NewsCorp/Telepiù*”).

²¹. This phenomenon is often put forward as an explanation for the fast collapse of competition in the pay television market in the UK. See Mark Williams, “Sky Wars: The OFT Review of Pay-TV”, *European Competition Law Review* (1997), vol. 18, n.4, pp. 214-229.

²². Several decisions of the European Commission suggest that premium television content is “essential” or indispensable for a pay television operator to compete. In *NewsCorp/Telepiù*, for instance, the European Commission considered that “[t]hese specific contents [premium television services] are essential for the survival of any pay-TV operator” and that, in

On the basis of these assumptions, remedies in horizontal merger cases sought to restore downstream competition in such a way that upstream cut-throat competition between pay television operators could be avoided. This was achieved in three alternative ways. A first “regulated solution”, seldom explored and limited to exceptional circumstances, involves the ban of exclusive agreements in dealings between pay television operators and right holders. In *NewsCorp/Telepiù*, the scope of exclusivity was limited to transmission via satellite, so that a new entrant relying on an alternative delivery technology was able to negotiate directly with the right holder.²³

Alternatively, the vertically-integrated pay television operator can be required to sub-license its premium television channels in two ways. In *NewsCorp/Telepiù*, the merged entity accepted to sub-license its premium television channels at the wholesale level on a retail minus basis.²⁴ Instead of a sub-licensing obligation, a competition authority may accept that premium television channels are made available to competing pay television operators on a “self-distribution” basis. In this setting, the downstream competitor acts as an agent of the vertically-integrated operator and the latter entertains a direct relation with customers. In the merger between the French satellite pay television operators CanalSat and TPS, the Conseil de la Concurrence accepted that the new entity makes available its flagship premium television bundle Canal+ Le Bouquet on a “self-distribution” basis. The authority justified this choice by the need to strike a balance between the investments made by Canal+ in the acquisition of content and the development of downstream competition.²⁵

Against this background, the regulatory regime to which BSkyB is subject is a very particular one, and this is explained by the particular fate of competition in the pay television segment in the UK. Satellite pay television services were launched as far back as 1989, but “head-to-head” competition between Sky and BSB collapsed in 1990, i.e. much earlier than in the rest of Member States. As a result, the remedies explored by the European Commission in horizontal mergers such as *NewsCorp/Telepiù* do not apply in the UK. BSkyB supplies its premium television services to cable operators at the wholesale level.²⁶ In its dealings with Tiscali, however, BSkyB preferred to supply its content on a self-distribution basis.²⁷ Agreements with other pay television operators, and in particular BT, have failed so far to come to fruition.²⁸

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the post-merger scenario they would “not be available in the market”.

²³. *NewsCorp/Telepiù*, paras. 233 et seq.

²⁴. *Ibid.*, paras. 246 et seq.

²⁵. Conseil de la Concurrence, Opinion n. 06-A-13 of 13 July 2006, *Vivendi/Canal+/TPS*: “Pour des raisons de cohérence et de clarté juridique, d’une part, et de respect du modèle économique de GCP, d’autre part, il est proposé de ne pas remettre en cause l’exclusivité de distribution de GCP sur ses propres chaînes et de n’imposer à la nouvelle entité la mise à disposition sur le marché de gros que des chaînes acquises à l’occasion de la concentration dans les thématiques sensibles: premium, cinéma, sport, information et jeunesse (remède nécessaire n° 10 – Annexe I). Le privilège de la distribution exclusive devrait donc se limiter aux chaînes dont la nouvelle entité assume le risque et le coût d’édition [...]”.

²⁶. Ofcom’s consultation document, pp. 125-127.

²⁷. *Ibid.*

²⁸. *Ibid.*

Interestingly, a chance was presented to the OFT to promote a regulated solution in 2005, when BSkyB acquired the broadband operator Easynet in 2005.²⁹ However, the competition authority considered that remedies were not justified in that case. Drawing on the “single monopoly profit” theory, the authority considered that the vertical merger did not have an impact on BSkyB’s incentives to supply its premium television channels to downstream pay television operators.³⁰

The submission made by BT, Setanta, TopUp TV and Virgin Media requesting Ofcom to proceed with a market reference to the Competition Commission attempted to exploit the regulatory divergence between the UK and other countries in which vertically-integrated pay television operators are subject to some sort of intervention via competition law. Market references to the Competition Commission are rarely based on the anticompetitive behaviour of a single firm and focus far more often on the features in a market taken as a whole.³¹ In accordance with the logic behind market references, the joint submission had to explain the ways in which the features in the pay television market that distort competition to the detriment of consumers.

BSkyB’s competitors advanced the theory whereby there would be a “vicious circle” that prevents the emergence of competition at the levels of the acquisition and the exploitation of premium television content. In this sense, the vicious circle offered an explanation of the long-lasting dominance enjoyed of BSkyB in these markets. In essence, the logic of the theory relies on the assumption that premium television channels are something akin to a natural or a network monopoly, in line with what has been pointed out *supra*. Put shortly, the joint submission explained that BSkyB’s downstream position as the leading pay television operator increases the chances that the company will successfully bid for premium television content, which in turn reinforces its downstream position as the leading pay television operator.³² In line with the assumptions made *supra* by competition authorities, the parties considered that the only way in which competition could flourish at the downstream level is by imposing an obligation on BSkyB to supply access to its premium television channels on a fair, reasonable and non-discriminatory (“FRAND”) basis. From this perspective, competition law remedies to tackle alleged anti-competitive practices from BSkyB would contribute little to the development of a competitive market structure.

The joint submission proposed extensive regulatory intervention. A first line of remedies dealt with the ability of pay television competitors to thrive in the market, which was to be achieved in two ways. One of them, by imposing FRAND obligations on BSkyB for the sub-licensing of its premium television channels to its downstream competitors.³³ The other one is achieved by prohibiting the so-

²⁹. OFT, Decision of 30 December 2005, Anticipated acquisition by BSkyB Broadband Services Limited of Easynet group plc.

³⁰. *Ibid.*, para. 20: “Third parties initially assumed that Sky would be motivated to foreclose premium content by the extra revenue that could result. However, Sky’s incentives are not changed by the merger as there is only one monopoly profit to be made from its position in premium channels and the incentive for it to maximise revenue is not enhanced through acquiring Easynet. Pre-merger, Sky extracted a monopoly profit from its premium channels through a strategy of widespread distribution. DSL will increase those to whom it can sell premium channels. The monopoly profit would not increase if Sky chose to limit distribution”.

³¹. OFT, *Market Investigation References – Guidance about the making of references under Part 4 of the Enterprise Act*, March 2006, p. 8: “The problems referred to in the previous three paragraphs involve industry-wide market features or multi-firm conduct. It is likely that the great majority of references the OFT makes will be of that type. Generally speaking single-firm conduct will, where necessary and possible, be dealt with under CA98 or appropriate sectoral legislation or rules. It is not the present intention of the OFT to make market references based on the conduct of a single firm, whether dominant or not, where there are no other features of a market that adversely affect competition”.

³². See the Joint Submission, pp. 23 et seq.

³³. *Ibid.*, p. 33: “An express obligation on the market leader in the provision of premium sports and movies channels to provide FRND access to third party retailers has already been imposed in a number of instances; for example, on Canal+ and Sky Italia. Whilst these access obligations were imposed on Canal+ and Sky Italia as remedies in merger cases, it

called enforced “buy through” of these channels, i.e. the obligation to subscribe to a bundle of basic television services before subscribing to a premium television service.³⁴ The second line of remedies was intended to tackle the alleged incentives on the part of BSkyB to discriminate against its downstream competitors and proposed as the major solution a form of functional separation of BSkyB’s upstream and downstream activities,³⁵ in a proposal that mirrors the functional separation of BT following the Strategic Review of telecommunications undertaken by Ofcom.³⁶

Ofcom's Assessment and Remedies

Remedies were finally proposed by Ofcom in its second consultation document. The approach of the regulator to the issues raised by BSkyB’s competitors is somewhat more pragmatic than the approach found in the consultation document. This is probably explained by Ofcom’s preference to deal with the question through its powers under the Communications Act, as already said. This choice indeed relieved it from the need to establish that the conditions for the submission of a market reference to the Competition Commission were established.

Ofcom’s assessment in the consultation document was structured around three principles: (i) the importance of premium content; (ii) BSkyB’s dominance in the markets for premium content and (iii) BSkyB’s incentives to give access to its premium channels to its downstream competitors.

On the assumption that, indeed, BSkyB lacked an incentive to sub-license its premium channels,³⁷ Ofcom examined the negative effects on consumers of the alleged lack of competition in the pay television sector. In the regulators’ view, BSkyB’s practices are likely to harm consumers in various ways. From a static perspective, this harm is to be expected from: (i) a reduction in the number of retailers (and platforms) from which the premium television channels are available and (ii) a limitation in the number and type of content bundles.³⁸ From a dynamic perspective, Ofcom expected reduced innovation in the growth of new services, such as video-on-demand, new hardware and in the development of new bundles.³⁹

By way of contrast, the consultation document does not establish clearly that pay television services are not priced “competitively and efficiently” in spite of BSkyB’s position in the markets for the wholesale supply of premium television channels. This is so because of the inherent difficulties in determining what constitutes a “competitive and efficient” price in the audiovisual industry, characterised by very high fixed costs and close to zero marginal costs.⁴⁰ Moreover, it was difficult to establish a clear case on the basis of the international comparisons used. Conversely, Ofcom was

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should be noted that the underlying rationale for the imposition of remedies in both merger cases and market investigations is broadly the same [...].

³⁴. Ibid., p. 35.

³⁵. Ibid., pp. 37-39.

³⁶. See e.g. Cave, “Six Degrees of Separation – Operational Separation as a Remedy in European Telecommunications Regulation”, *Communications & Strategies* (2006), n. 64, 4th Quarter, pp. 89-103.

³⁷. In its consultation document, Ofcom undertook a cost-benefit analysis of a decision by BSkyB to withdraw its premium television channels from its competitors’ platforms, concluding that any such decision could be a rational strategy if a dynamic perspective is introduced. On this issue see also Helen Weeds, “TV Wars: Exclusive Content and Platform Competition in Television Broadcasting”, mimeo, March 2007, available at <http://privatewww.essex.ac.uk/~hfweeds/>.

³⁸. See in particular Ofcom’s consultation document, p. 167: “Having a reduced number of retailers with access to Core Premium content reduces the range of price points on premium and reduces the range of bundles of premium products with other products. More simply, decreased competition in the provision of premium content reduces pressure on retail costs relative to the counterfactual”.

³⁹. Ibid., pp. 156-159.

⁴⁰. Ibid., pp. 159 et seq.

reluctant to draw any definitive conclusions from some studies showing that subscribers to pay television services appeared satisfied with the current services.⁴¹

Among the different remedies explored in the consultation document, the regulator expressed a preference for the imposition of a “wholesale must-offer” obligation on BSkyB, in an attempt to tackle the ability of the operator to foreclose the supply of its premium television channels to its competitors.⁴² While this remedy would increase the number of retailers for the product, it would do little, as such, to ensure that alternative operators would be able to offer alternative bundling offerings that would prove sufficiently attractive. In relation with this second concern, Ofcom was particularly interested in requiring BSkyB to offer stand-alone bundles of premium television channels, which are currently unavailable as a consequence of the BSkyB’s “buy through” requirement, referred to *supra*. Therefore, Ofcom proposed to complement the wholesale “must-offer” obligation with a proposal whereby BSkyB would be obliged to supply its premium services as a stand-alone package.⁴³

As mentioned in the introduction, Ofcom expressed a preference for an intervention through its powers to promote “fair and effective competition” under Section 316 of the 2003 Communications Act (“Section 316”), which applies to broadcasting licensees.⁴⁴ On the one hand, because the remedies proposed did not go as far as to plead for the “functional separation” of BSkyB, a market reference to the Competition Commission was not deemed justified.⁴⁵ On the other hand, Ofcom considered that its powers under competition law could prove ineffective, from a formal and a substantive perspective, to tackle the problems identified.⁴⁶

An Analysis of Ofcom’s Proposal

Methodology and Analysis in the Consultation Document

Ofcom can make use of several tools to promote competition in the sectors falling under its jurisdiction. As already said, the 2003 Communications Act empowered the authority to apply competition law provisions, and Ofcom has made use of these powers, for instance in margin squeeze cases against BT.⁴⁷ Moreover, Ofcom is in charge of the implementation of the principles stemming from the Regulatory Framework, one objective of which is the promotion of effective competition in the provision of electronic communications markets and services.⁴⁸ Even though the coincidence

⁴¹. Ibid., pp. 163 et seq.

⁴². Ibid. pp. 176 et seq.

⁴³. Ibid.: “In order to address our concern about the lack of stand-alone premium packages, it should be sufficient to make a stand-alone premium package available at the wholesale level; particularly as we see different platforms as being in the same retail market, this should tackle the retail-level concern”.

⁴⁴. In accordance with Section 316(1) of the 2003 Communications Act: “The regulatory regime for every licensed service includes the conditions (if any) that OFCOM consider appropriate for ensuring fair and effective competition in the provision of licensed services or of connected services”.

⁴⁵. Ibid., pp. 183-184.

⁴⁶. This is so for two reasons. First of all, evidence of anticompetitive behaviour is necessary both under Article 82 EC and its equivalent in the CA 1998. Moreover, the remedies available under competition law may not suffice to tackle the concerns identified by Ofcom. See the consultation document, pp. 179 et seq.

⁴⁷. Ofcom, Decision of 12 July 2004, Case CW/00760/03/04, Investigation against BT about potential anti-competitive exclusionary behaviour.

⁴⁸. See Framework Directive, Article 8(2): “The national regulatory authorities shall promote competition in the provision of electronic communications networks, electronic communications services and associated facilities and services by inter alia: [...] (b) ensuring that there is no distortion or restriction of competition in the electronic communications sector [...]”.

between the two is not exact,⁴⁹ it is generally agreed that competition law and the Regulatory Framework share a common ground regarding principles and methodology.⁵⁰

The remedies proposed in the consultation document, which in essence amount to a compulsory licensing mechanism, stand at odds with these bodies of law, and this for several reasons. On methodological grounds, the theory of harm developed by Ofcom is incomplete if analysed from the perspective of competition law. Suffice it to recall that the consultation document merely established BSkyB's (super-)dominance in the two markets for the wholesale supply of television content and the lack of incentive on the part of the operator to sub-license its channels to its downstream competitors. In other words, Ofcom derived the existence of harm for consumers directly from the absence of an incentive to supply.

This theory of harm contradicts the common principles underlying competition law and the Regulatory Framework. Regardless of the specific provision applied, in vertical settings such as the one examined in the consultation document, a competition or a regulatory authority will complement an assessment of the ability and the incentive of an undertaking to foreclose access to an input with an additional—and indispensable—step, which is the assessment of the effects of the behaviour in question—or vertical merger, for that matter—on a downstream market. In merger cases, the relevant question is whether foreclosing access to an input results in higher prices for consumers in the downstream market.⁵¹ The substantive standard is somewhat higher under Article 82 EC, in that such a strategy requires, at the very least, that the behaviour leads to the elimination of downstream competition.⁵² The standard set in Article 12 in the Access Directive is not as strict, given that the relevant question is whether a refusal to supply access to an input at the wholesale level hinders “the emergence of a sustainable competitive market at the *retail level*” (emphasis added).⁵³

The main implication of these principles is that a refusal to supply/raising rivals' costs strategy put in place by a vertically integrated company, such as BSkyB, may have neutral or positive effects on consumer welfare in the downstream market. For instance, the refusal to supply an input may spur competition in the downstream market, if the downstream rivals enjoy a larger market share than the vertically integrated company. Similarly, a foreclosure strategy may not entail a negative impact on competition where downstream competitors are able to deploy counterstrategies.

Surprising as it may be, Ofcom's consultation document expressly excludes the need to define the relevant downstream market,⁵⁴ and, *a fortiori*, does not assess whether Ofcom's alleged strategy would

⁴⁹. The coincidence between the two is not exact because the objectives of the Regulatory Framework go beyond the promotion of effective competition and include other social and consumer protection objectives (of which universal service is probably the most prominent example). This is so, moreover, because there are several instances in which the Regulatory Framework sets a lower standard for intervention, in particular the conditions under which shared access to infrastructure is mandated. See, in this sense, Article 12(1) of the Access Directive.

⁵⁰. On these issues, see e.g. Alexandre de Stree, “The Integration of Competition Law Principles in the New European Regulatory Framework for Electronic Communications”, *World Competition* (2003), Vol. 26, No. 3, pp. 489-514.

⁵¹. Guidelines on the assessment of non-horizontal mergers under the Council Regulation on the control of concentrations between undertakings, OJ (2007) C 265/6, para. 31 (the “Non-horizontal merger Guidelines”).

⁵². See, in particular, Case C-7/97, *Oscar Bronner GmbH & Co. KG v Mediaprint Zeitungs- und Zeitschriftenverlag GmbH & Co. KG and Others*, [1998] ECR I-7797; Joined Cases C-241/91 P and C-242/91 P, *Radio Telefis Eireann e Independent Television Publications Ltd. v. Commission*, [1995] ECR I-743 and Case C-418/01, *IMS Health GmbH & Co. OHG v. NDC Health GmbH & Co. KG*, [2004] ECR I-5039.

⁵³. In accordance with Article 12 of the Access Directive access remedies may be granted under the Regulatory Framework where “the national regulatory authority considers that denial of access or unreasonable terms and conditions having a similar effect would hinder the emergence of a sustainable competitive market at the retail level, or would not be in the end-user's interest”.

⁵⁴. Ofcom's consultation document, p. 57: “Our focus is on wholesale markets. It is not necessary formally to define the downstream markets. However, when defining wholesale markets we take account of the indirect constraint that final

lead to anticompetitive foreclosure in the downstream market. Because Ofcom examines the effects of a refusal to supply/raising rivals's costs strategy directly on consumers, its reasoning is problematic for an additional reason. Suggesting, as Ofcom does, that the lack of incentive on the part of BSkyB to supply its premium television channels to downstream competitors harms consumers because it limits the number of retailers for the product—and the number of platforms from which these channels would be available—would not withstand competition law scrutiny, and this from two perspectives.

First, such an approach provides little or no guidance to authorities, since it could call for intervention to promote competition in virtually every arrangement between firms. Take the example of vertical restraints. Selective or exclusive distribution systems limit the number of retailers of a product in the way described by Ofcom, and in spite of that they are regarded leniently by competition authorities.⁵⁵ Similarly, it has been often pointed out that if one ignores the *ex ante* investments made by a vertically-integrated company to achieve dominance in the upstream market (e.g. through the exploitation of a technology or an infrastructure) a compulsory licence will necessarily have positive effects on competition, at the very least in the sense that such a measure will increase rivalry in the downstream market.⁵⁶ However, it is clearly established under competition law that a compulsory licence is not imposed merely because a company enjoys a competitive advantage or exploits a superior product (or, conversely, because the compulsory licence would be pro-competitive). In reality, compulsory licences under competition law are only imposed under very strict circumstances, precisely because the investments made *ex ante* by the dominant company—and the need to preserve the incentives to invest—are valued.⁵⁷ To the extent that it takes into account the importance of preserving the incentives to invest in infrastructure, the Regulatory Framework is not fundamentally different in this regard.⁵⁸

From the opposite perspective, Ofcom's argument can be said to be incomplete, insofar as compulsory access to an input controlled by an upstream dominant company may not, as such, benefit consumers—at the very least if by benefit one means an improvement in the welfare of consumers. Interestingly, an argument in this sense was advanced in the context of past investigations into the pay television market in the UK, when some authors (and cable companies) argued that the wholesale rates applied by the satellite operator, based on the “retail minus” principle, left unaffected BSkyB's ability to charge monopoly prices in the downstream market.⁵⁹ In other words, for a compulsory licensing

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consumers place on channel wholesalers as a result of their relationship with retailers”.

⁵⁵. In this regard, see the Guidelines on vertical restraints, OJ (2000) C 291/1. For instance, purely qualitative selective distribution systems fall outside the scope of Article 81(1) EC, regardless of the market share enjoyed by the supplier provided that certain conditions are met. Similarly, exclusive distribution agreements are deemed to fall outside the scope of Article 81(1) EC where the market share of the supplier does not exceed 30 percent.

⁵⁶. This point was elegantly made in Einer Elhauge, “Defining Better Monopolization Standards”, *Stanford Law Review* (2003), vol. 56, n. 3, pp. 253-344: “[Referring to the US Supreme Court's opinion in the *Aspen* case] The more fundamental problem is that, from an *ex post* perspective, excluding rivals from any property rights valuable and unique enough to enjoy monopoly power will generally constrain consumer choice, lower output, and raise prices, thus producing allocative inefficiency. This is certainly true with intellectual property, where sharing is normally costless, and thus any dissemination of the knowledge protected by the property right will produce more efficient competition in using that knowledge. But it is also true with any other kind of physical property that gives the owner monopoly power, assuming sharing is not more costly than the efficiency gains from competitive use of the property”.

⁵⁷. See in this regard the Opinion of Advocate General Jacobs in Case C-7/97, *Oscar Bronner GmbH & Co. KG v Mediaprint Zeitungs- und Zeitschriftenverlag GmbH & Co. KG and Others*, [1998] ECR I-7797.

⁵⁸. See Framework Directive, Article 8(2): “The national regulatory authorities shall promote competition in the provision of electronic communications networks, electronic communications services and associated facilities and services by inter alia: [...] c) encouraging efficient investment in infrastructure, and promoting innovation”.

⁵⁹. Where wholesale rates are set on a “retail minus” basis, any increase in the retail prices is indeed reflected on wholesale rate, thereby limiting the ability of one of the downstream competitors to react to a price increase by the vertically-integrated incumbent. On this issue see, in particular, David Harbord and Marco Ottaviani, “Contracts and Competition in

strategy to yield benefits for consumers it may have to be complemented with direct or indirect price regulation (FRAND charges, cost-based pricing, unbundled access...). Far from being an exception, the consultation document acknowledged this fact, and Ofcom even sketched the alternative mechanisms that could be used, both to estimate costs and to ensure the downstream viability of BSkyB's competitors.

Summing up, Ofcom's assessment departed from standard competition law analysis and methodology, and this in turn explains why the consultation document lays down less stringent standards for the imposition of a compulsory licence on BSkyB. This conceptual divergence raises a more fundamental question. While there is certainly no obstacle in theory to Section 316 departing from competition law, the idea that a regulatory authority could endorse simultaneously two different standards when promoting competition in electronic communications markets should be seen with suspicion.

Choice of Section 316 as a Legal Basis: Implications

Ofcom's choice to intervene on the basis of Section 316 of the Communications Act (instead of submitting a market reference or relying on its powers to enforce competition law provisions) can indeed be objected as such. To be sure, it is not the first time that Ofcom uses its powers under this provision. In particular, Ofcom has adopted two codes of practice dealing with access to electronic programme guides⁶⁰ and cross-promotion of programmes⁶¹ relying on the same legal basis. However, these precedents cannot be easily compared with the form of large scale intervention proposed in the consultation document. The limited use of this provision in past proceedings by Ofcom gives the impression that Ofcom's boundaries of action under Section 316 are not yet properly defined and that, more importantly, there are no clear objectives underlying Ofcom's intervention to promote "fair and effective competition" in broadcasting markets. By way of contrast, there is growing consensus whereby competition policy should ultimately be guided by efficiency and consumer welfare.⁶²

A regulatory environment that, in the absence of a solid rationale clearly defined *ex ante*, allows for the coexistence of two opposing competition law standards is likely to undermine legal certainty, insofar as the regulator would be given the chance of choosing between the rules better serving its purposes depending on the circumstances at stake in any given case. This risk became clear in the consultation document. After much controversy in the past few years, the most recent policy documents of the European Commission have insisted on the fact that the primary objective of Article 82 EC should be the protection of consumers, and not of the competitors of the dominant firm.⁶³ In contrast, the consultation document does not hesitate to take the welfare of competitors into account when delineating the guiding principles of the wholesale "must-offer" remedy.

For instance, when evaluating whether to rely on Article 82 EC (and its national equivalent), Ofcom considered that, even if BSkyB's behaviour were to be found abusive, competition law would not allow to take into consideration the viability of less efficient competitors when imposing remedies.⁶⁴

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the Pay-TV Market", mimeo, July 2001.

⁶⁰. Ofcom, Code on Electronic Programme Guides, July 2004.

⁶¹. Ofcom, Cross-Promotion Code, July 2006.

⁶². For a recent example in the UK in this sense, see OFT Prioritisation Principles – Consultation, September 2007.

⁶³. See e.g. the European Commission Guidance on the Commission's Enforcement Priorities in Applying Article 82 EC Treaty to Abusive Exclusionary Conduct by Dominant Undertakings, December 2008, para. 6.

⁶⁴. Ofcom's consultation document, p. 180: "[...] if we saw fit to determine a wholesale price designed to facilitate entry, that price would be based on different cost data from a test of whether Sky was applying a CA98 margin squeeze. Specifically, a remedy intended to promote competition might seek to reflect the lack of scale economies of a new entrant. The CA98 margin squeeze test is more focused on an equally efficient operator. It might therefore generate a different result and in this case be less effective at promoting the dynamic benefits of competition".

Ofcom conceded in its assessment that BSkyB might be more efficient than its competitors and that, to the extent that it is so, intervention would not be afforded under competition law—suffice it to recall in this regard that Ofcom found no clear evidence that BSkyB was charging excessive prices.⁶⁵ On the other hand, Ofcom saw no obstacle in promoting the entry of less efficient competitors under Section 316.

Ofcom's inclination in the consultation document to equate "effective competition" in pay television with increased rivalry in the marketplace for the provision of these services (even at the price of promoting inefficient entry) should also be put in perspective. The gradual shift in the enforcement of competition law towards efficiency and consumer welfare (at the expense of the protection of rivalry in the marketplace as such) is explained by an effort on the part of competition authorities to avoid contradictions in policy-making that had become apparent and that were in part explained by a concern with rivalry in the marketplace.⁶⁶ In this sense, authorities have in general conceded that, where rivalry is protected over efficiency, the incentives of companies to compete will tend to be harmed, without this resulting in any tangible benefits for consumers (if not the opposite). The ways in which Ofcom's proposed remedies can be said to lead to anticompetitive results will be examined *infra*.

It is submitted that the wealth of precedents in the field competition law and the gradual evolution in policy-making by specialised authorities should not be ignored by Ofcom when using its powers under Section 316. Thus, if Ofcom chooses to depart from current competition law standards for intervention so as to give more prominence to rivalry in the marketplace, the rationale and the objectives behind this choice should be clearly identified *ex ante*, as already pointed out. This is all the more so if one takes account of Ofcom's self-declared bias against intervention. For instance, the substantive conditions under which access may be granted in accordance with the Regulatory Framework are less stringent than those applying under competition law. In addition, these conditions appear to reflect a concern with developing rivalry at the downstream level. However, the reasons why this is so are adequately identified, and this is not true in the case of Section 316.

Setting lower standards for promoting rivalry under the Regulatory Framework may be justified if one considers that incumbent telecommunications operators enjoyed exclusive rights for a long period of time and that some elements of their infrastructure bear natural monopoly features. In any event, access remedies under the Regulatory Framework are only justified where a given market satisfies the so-called "three criteria test".⁶⁷ In particular, this test requires evidence of the existence of "high and

⁶⁵. Ibid.: "One of the potential reasons we identified for Sky's lack of incentive to supply was possible differences in efficiency between Sky and other retailers. If that were the case, an abuse might well not have taken place, but the negative impact on competition and consumers that we have identified would still exist. If we were to rely on our powers under CA98, we would not be able to address this competition problem absent an actual finding of anticompetitive behaviour".

⁶⁶. For instance, the Guidelines on vertical restraints, referred to *supra*, following heavy criticism of a system that was perceived as rigid and formalistic (see in particular Barry Hawk, "System Failure: Vertical Restraints and EC Competition Law", *Common Market Law Review* (1995), vol. 32, n. 4, pp. 973-989. Likewise, the review of Article 82 EC which resulted in the adoption on a Guidance Paper, equally referred to *supra*, was launched by the European Commission after a series of controversial judgments (see, in particular, Denis Waelbroeck, "Michelin II: A Per Se Rule Against Rebates by Dominant Companies?", *Journal of Competition Law and Economics* (2005), vol. 1, n. 1, pp. 149-171).

⁶⁷. The requirements under the three-criteria test are the following: "(a) the presence of high and non-transitory barriers to entry. These may be of a structural, legal or regulatory nature;(b) a market structure which does not tend towards effective competition within the relevant time horizon. The application of this criterion involves examining the state of competition behind the barriers to entry; (c) the insufficiency of competition law alone to adequately address the market failure(s) concerned". See the Commission Recommendation on relevant product and service markets within the electronic communications sector susceptible to ex ante regulation in accordance with Directive 2002/21/EC of the European Parliament and of the Council on a common regulatory framework for electronic communications networks and services, OJ (2007) C 344/65 (the "2007 Recommendation").

non-transitory”, structural or legal, barriers to entry in the market under scrutiny. In this sense, the “three criteria” test can be said to reflect a presumption that anticompetitive foreclosure of the downstream market would result if access remedies were withdrawn.⁶⁸

As can be seen, before Ofcom chooses to extend to premium television content the access remedies applying to BT under the Regulatory Framework, two prerequisites should be satisfied. From a substantive perspective, Ofcom should define the policy objectives underlying Section 316, and the reasons why these objectives would be jeopardised if current competition law standards were applied. Whether or not Ofcom chooses to depart from current competition law standards, it would still be necessary to assess the effects of BSkyB’s behaviour on competition using the methodology shared by competition law and the Regulatory Framework. Some principles for the assessment of BSkyB’s behaviour on the basis of these two prerequisites are proposed *infra*.

Some Guiding Principles for the Assessment of Competition in Pay Television Markets

An evaluation of the impact of BSkyB’s refusal to license its premium television channels on competition requires assessing whether the ability and the incentive to compete of BSkyB’s rivals at the downstream level is affected by lack of access to premium television channels. An adequate definition of downstream markets and an analysis of the conditions under which operators compete therein is a necessary step in this assessment.

As far as the definition of downstream markets is concerned, two relevant levels can be identified in the broadcasting value chain. There is a wholesale level, in which television channels negotiate distribution with multichannel operators, and a retail level, in which multichannel operators bundle these channels and offer them to viewers.

Ofcom’s market definition at the wholesale level, which identifies a market for premium sports and another one for premium cinema, finds some support in the most recent practice of competition authorities.⁶⁹ Therefore, it is probably a sterile exercise to contest Ofcom’s finding that BSkyB holds a dominant position in the two wholesale markets for premium channels. Where the consultation document provides less guidance is in the definition of retail markets, even though it hints at the existence of a downstream pay TV market in some passages.⁷⁰

It is beyond the scope of this piece to define markets in detail. Suffice it to mention that an overview of the television sector in the UK gives some hints about the candidate downstream markets. There are three major multichannel distributors in the UK, the DTT subscription-free service Freeview, with more than 9 million “Freeview only” households, and the subscription-based services BSkyB—with a similar number of subscribers—and Virgin Media, with almost 3.5 million subscribers.⁷¹ The role of DSL providers, which is on the rise in other Member States of the EU, is still marginal.⁷²

The first relevant question should then be whether Freeview, on the one hand, and competing multichannel operators using other delivery technologies, on the other, are part of the same relevant market. It is submitted that there are probably little reasons to exclude Freeview from the broad candidate retail market for the multichannel distribution of television services. Freeview offers more than 30 channels, generalist and theme-based, including Setanta’s premium offer—and, if approved, a

⁶⁸. In this regard, see also Article 14(3) of the Framework Directive.

⁶⁹. See in particular the cases referred to *supra*, note 7.

⁷⁰. For instance, when stressing the “importance” of premium content, Ofcom stresses that premium content is the driver for subscriptions to “pay television”, see e.g. the summary of its arguments in p. 3 of the consultation document.

⁷¹. Ofcom, *The Communications Market: Digital Progress Report. Digital TV – 2008 Q3*, December 2008.

⁷². *Ibid.*

selection of BSkyB's premium channels—and is in this sense difficult to differentiate from the offers coming from operators exploiting competing delivery technologies.⁷³ Therefore, it is likely that Freeview exerts a competitive constraint on other, subscription-based, multichannel operators.⁷⁴ If one assumes that there is a single retail market for multichannel television, this market would boast three prominent players, none of which would be dominant.

Television services are increasingly provided together with other services in “triple play” and “quadruple play” bundles. This explains, for instance, the takeover of Easynet by BSkyB in 2005 and the launch of BT Vision. As a result, a market for “triple play” bundles, or for broadband Internet services, may need to be identified alongside the market for the multichannel distribution of television services. Besides BSkyB, operators in this second market for broadband Internet services would include Virgin, BT and other DSL operators, such as Tiscali. In bundling settings, the relevant market may be defined as encompassing not only the separate products but also the bundle; alternatively, the bundle may form a relevant market of its own alongside the markets for the separate products.⁷⁵ The question seems to depend in this regard on the differences between the price charged for the bundle and for each of the products.⁷⁶

It is in this environment that the harm for competition and consumers stemming from BSkyB's commercial strategies should be examined. As already pointed out, it is not because BSkyB does not have an incentive to supply its premium television channels to other downstream operators that competition and, by extension, the welfare of consumers, will necessarily be harmed. Two of the issues analysed in the consultation document could be reconsidered. Ofcom derives the harm to competition in the downstream market from the alleged “importance” of premium content. The harm for consumers, in turn, is assessed with regard to the lack of access to BSkyB's premium channels from some of the distributors.

It is submitted that the “importance” of premium television content is not an adequate starting point to examine the convenience of regulatory intervention, as it lacks precision. From a competition law perspective, an adequate benchmark would consist of examining whether premium television content is indispensable within the meaning of the *IMS Health* line of case law,⁷⁷ or, alternatively whether lack of access to premium content harms the ability to compete of downstream competitors to the extent that this results in higher prices for consumers.⁷⁸

⁷³. It must be noted that DSL providers such as BT have launched their pay television services with hybrid decoders from which Freeview is accessible via terrestrial delivery while on-demand content is delivered via DSL platforms.

⁷⁴. In the *NewsCorp/Telepiù* Decision, the European Commission excluded analogue terrestrial television from the “pay-TV” market in which the merging entities were found to be active. Interestingly, however, the authority acknowledged already in that case—decided in 2003—that the frontiers between the two markets were likely to dissipate in the future with the introduction of digital terrestrial television (see *NewsCorp/Telepiù*, para. 39). Likewise, in the Explanatory Note accompanying the 2007 Recommendation, for instance, the European Commission suggested that subscription-free services may exert a competitive constraint of subscription-based bundles of television services (See Accompanying Document to the 2007 Recommendation, Brussels 13 November 2007, p. 47).

⁷⁵. Report by Europe Economics for the European Commission, DG Competition, Market Definition in the Media Sector, November 2002, pp. 21 et seq.

⁷⁶. *Ibid.*

⁷⁷. Case C-418/01, *IMS Health GmbH & Co. OHG v. NDC Health GmbH & Co. KG*, [2004] ECR I-5039, para. 28: “[...] [I]n order to determine whether a product or service is indispensable for enabling an undertaking to carry on business in a particular market, it must be determined whether there are products or services which constitute alternative solutions, even if they are less advantageous, and whether there are technical, legal or economic obstacles capable of making it impossible or at least unreasonably difficult for any undertaking seeking to operate in the market [...]”.

⁷⁸. The Non-horizontal merger Guidelines refers (in para. 18) to the notion of “anticompetitive foreclosure” in the following terms “the term ‘foreclosure’ will be defined to describe any instance where actual or potential rivals’ access to supplies or markets is hampered or eliminated as a result of the merger, thereby reducing these companies’ ability and/or incentive

A comparative analysis of the structure of competition in other Member States casts some doubts on the assumption that premium content is indispensable for competition to take place in a downstream market. An interesting insight comes from the situation of competition in countries where cable is the default delivery technology and the take-up of multichannel television is near-universal, such as Germany or the US. In both cases, the take-up of premium television channels is significantly lower than the total number of subscriptions to cable television. In the US, about 43 percent of cable subscribers—of a total of around 65 million—subscribe to a premium television service.⁷⁹ The take-up of premium television in Germany is placed at around 3 million subscriptions,⁸⁰ while more than 50 percent of the 35 million households in the country subscribe to cable.⁸¹ Without ignoring the relevance of country differences, these figures suggest that the potential number of subscribers to a multichannel or a broadband “triple play” service may be significantly higher than the potential number of subscribers to a premium television services. In other words, there appears to be a large “contestable” share of television viewers that may be less willing to subscribe to a premium television service, and for which multichannel distributors may compete.

An interesting example has to do with the evolution of the television sector in France in recent years. Since the merger between CanalSat and TPS in 2006, the number of subscribers to the premium bundle Canal+ Le Bouquet has remained fairly stable at around 5 million.⁸² By way of contrast, the number of subscribers to television via DSL has exploded during the same period, being the platform of choice for more than 15 percent of households—with as many as 4.5 million subscribers—up from a mere 3 percent in 2006.⁸³ These figures suggest, again, that the potential for growth of basic multichannel services is very important in traditionally “terrestrial” countries such as France or the UK, as a result of the development of triple play bundles. Bundling of broadband and television services represents a shift from previous business models in which multichannel distributors relied exclusively on premium television content to attract subscribers.

This overview is an invitation to examine thoroughly whether lack of access to premium content truly harms the ability of multichannel distributors to compete with BSkyB at the downstream level. From a different perspective, this overview also suggests that consumers in the UK may be adequately served under the current market structure, with BSkyB and Virgin, on the one hand, and Freeview, on the other, providing attractive and complementary multichannel offers. In this regard, it is not clear whether, and why, the landscape that would emerge under the proposed intervention would represent a meaningful improvement for consumers.

One should also note that, as technology develops, BSkyB’s competitors will gain new tools. Pay-per-view and video-on-demand represent an evolution with regard to “first-window” film channels such as Sky Movies. BSkyB’s competitors acknowledged in their joint submission that rights for these film windows are generally sold on a non-exclusive basis by the major studios, meaning that access to this type of content would in principle not be an issue.⁸⁴ Interestingly, cable and DSL have a technological advantage when compared to satellite, in that the latter lacks a “return channel”.

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to compete. As a result of such foreclosure, the merging companies — and, possibly, some of its competitors as well — may be able to profitably increase the price charged to consumers. These instances give rise to a significant impediment to effective competition and are therefore referred to hereafter as ‘anticompetitive foreclosure’.

⁷⁹. See FCC, *12th Annual Video Competition Report to Congress*, March 2006, para. 40.

⁸⁰. In the 3rd quarter of 2008, Premiere reported having around 2.4 million direct subscribers and an additional 0.7 million indirect subscribers, see “Premiere Expects EBITDA Loss in 2008 and Releases Q3 – Subscriber Figures”, available at info.premiere.de.

⁸¹. See ALM, *Digitisation 2007 – Digitisation of the German Television Market*.

⁸². See *supra*, *Lettre de l’autorité*.

⁸³. *Ibid.*

⁸⁴. Joint Submission, p. 7.

In any event, a meaningful assessment of the overall effects of BSkyB's lack of incentive to supply its premium content cannot ignore the overall conditions of competition in the downstream market. Ofcom's consultation document seems to assume that "symmetric competition" in the downstream market—i.e. a downstream market in which all operators have access to premium content—delivers a superior outcome for consumers than the asymmetric *statu quo*, but this is not necessarily true. One should bear in mind that BSkyB and other "triple play" operators compete across the whole range of broadband products, not only television. In this context, lack of access to content by BSkyB may very well stimulate competition at the downstream level, and not the opposite. Suffice it to recall that BT and Virgin Media currently have about twice as many broadband subscribers as BSkyB.⁸⁵ If BSkyB's competitors react to the changing environment by reducing prices for broadband services or by developing counterstrategies, it is difficult to see why consumers would be harmed by the exclusive exploitation of premium television content by the satellite provider. By the same token, "symmetric competition" may in fact reduce the competitive pressure BSkyB exerted on broadband leaders, thereby contributing to making broadband markets more rigid. In this sense, it is submitted that any form of regulatory intervention that shields the position of the incumbents in any given market is not obviously desirable.

More generally, one of the major flaws of the consultation document is that Ofcom does not examine the potential anticompetitive effects of the remedies it proposes. These remedies have an impact both on the homogeneity of broadband offers⁸⁶ (all operators would in principle have access to the same range of products) and on transparency in the market (wholesale rates being regulated both for infrastructure and for content). The concern that regulatory intervention could pave the way for tacit collusion is probably important enough to be considered by the regulator.⁸⁷ It must moreover be noted that, after several years of rapid growth, broadband markets, while not declining, are entering maturity, making it difficult for operators to gain new subscribers as rapidly as in the past, which may prove a more favourable context for tacit collusion. Beyond the risk of tacit collusion, it is questionable whether Ofcom should favour a regulatory landscape in which all operators offer a homogeneous, commoditised, broadband product and have little scope for horizontal differentiation.

Conclusions

Ofcom's consultation document can be interpreted as a logical reaction to the absence of an adequate framework to deal with pay television. Technological convergence seems to be emerging in the way that had long been promised, with DSL providers being active in the provision of television services and with a growing take-up of triple play offerings. This trend will not do anything but accelerate as legacy infrastructures are upgraded. Because television content was excluded from the Regulatory Framework in 2002, several choices must now be made to deal with the interaction of television and telecommunications.

Players in the pay television segment, including upstream content providers and channel operators, prefer to deal on an exclusive basis in the majority of cases, and this explains, at least partly, the

⁸⁵. Ofcom, *The Communications Market 2008* (August), p. 323. According to the data in this report, BT had a 26.5 percent market share in August; Virgin Media's was of 23.7 percent and BSkyB's was at around 10 percent.

⁸⁶. Ofcom's proposal for remedies in the consultation document left open a number of issues, including the undertakings benefitting from the remedy. In particular, the authority left for further consideration the question of whether the remedies should only apply to multichannel distributors relying on a delivery technology other than those used by BSkyB.

⁸⁷. On this question, see Patrick Rey, "Collective Dominance and the Telecommunications Industry", in Pierre-André Buigues and Patrick Rey (eds.), *The Economics of Antitrust and Regulation in Telecommunications*, Edward Elgar, Cheltenham, 2004, pp. 91-113. Other factors mentioned by the author, which may be relevant for the present case include the existence of multi-market contacts, which ease collusion, as well as the absence of innovation in the market.

tendency towards monopoly shown in the sector. By way of contrast, the regulatory strategy to promote the emergence of a competitive market enshrined in telecommunications regulation is based on the idea of replication. In this regard, the Regulatory Framework requires that both the new entrant and the incumbent have access to the latter's infrastructure on a transparent and a non-discriminatory basis, with the functional separation of BT being the most accomplished regulatory effort to achieve replication. The choice that regulators like Ofcom now face boils down to opting between a model based on the ability to replicate premium content offerings (i.e. extending the telecommunications model) and another one based on competition law, in which the trigger for intervention would be anticompetitive foreclosure.

Ofcom favours the replication model. The proposal can be seen as a victory for "regulatory symmetry" in that BSkyB would no longer be able to rely on BT's infrastructure while being able to exploit at will its premium channels. Interestingly, the French legislator has recently been debating on whether to follow the replication model, but for the opposite reasons. The acquisition of television rights on an exclusive basis by France Télécom is perceived in France as a strategy on the part of the incumbent to re-monopolise broadband Internet markets.⁸⁸ In other markets, such as Belgium, the pure competition model has been preferred, and Belgacom acquired in 2008 the exclusive rights for the national football championship for the second time in a row, without it being obliged to share this content.⁸⁹

A close analysis of the consultation document invites for caution before making a choice in either direction. The main concern with Ofcom's proposal comes from the fact that the authority has not identified clear principles and objectives underlying the extension of the replication model to television on the basis of Section 316 of the Communications Act, and this is not without problems from the perspective of legal certainty.

From a substantive standpoint, the analysis *supra* shows that there are at least two fundamental ways in which premium television content and telecommunications infrastructures as the local loop differ from one another. The first one has to do with the alleged "indispensability" of premium content for downstream competition to emerge. The second one concerns the dynamic features of television markets, in which a number of developments ("triple play" bundling, growth of video-on-demand) may undermine BSkyB's position at the wholesale and the retail levels in the future.

Further stages in the market investigation will hopefully help define (and refine) Ofcom's position.

⁸⁸. At the time of writing, the issue of exclusivity over television content in electronic communications markets was being discussed in the French Parliament.

⁸⁹. "Belgacom obtient les droits TV", *Le Soir*, 3 June 2008.