

Determination

Vodafone Europe B.V. and Sky Network Television Limited [2017] NZCC 1

Sky Network Television Limited and Vodafone New Zealand Limited [2017] NZCC 2

The Commission:	Dr Mark Berry Dr Stephen Gale Dr Jill Walker Anna Rawlings
Summary of applications:	An application from Vodafone Europe B.V. seeking clearance to acquire up to 51% of the shares in Sky Network Television Limited and an application from Sky Network Television Limited to acquire up to 100% of the assets and/or shares of Vodafone New Zealand Limited.
Determination:	Under section 66(3)(b) of the Commerce Act 1986, the Commerce Commission declines to give clearance for the proposed acquisitions.
Date of determination:	22 February 2017

Confidential material in this report has been removed. Its location in the document is denoted by [].

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Acronyms and abbreviations

2degrees	Two Degrees Mobile Limited
5G	5 th generation mobile networks
ADSL	Asymmetric digital subscriber line
Applicants	Vodafone and Sky
Applications	The two applications for clearance of the proposed merger received by the Commission under s 66(1) of the Commerce Act 1986 from Vodafone Europe B.V. and Sky
ARPU	Average revenue per user
AFL	Australian Football League
Axiom	Axiom Economics
Blue Reach	Blue Reach Wireless Limited
Broadband	For the purposes of this Determination, includes data services giving high speed access to the internet, and fixed voice services
CAPEX	Capital expenditure
Castalia	Castalia Limited
Chorus	Chorus Limited
Commission	Commerce Commission
Covec	Covec Limited
EBIT	Earnings before interest and taxes
EBITDA	Earnings before interest, taxes, depreciation and amortisation
EPL	English Premier League
Freeview	Freeview Limited
FTA	Free-to-air
FWA	Fixed wireless access
HFC	Hybrid fibre-coaxial
IDC	IDC Research Inc.
IPTV	Internet protocol TV
ISP	Internet service provider
LFCs	Local fibre companies
MBIE	Ministry of Business Innovation and Employment
Mediaworks	Mediaworks TV Limited
MNO	Mobile Network Operator
MVNO	Mobile virtual network operator
NERA	NERA Economic Consulting
NPBT	Net profit before tax
NRL	National Rugby League

NZRU	New Zealand Rugby Union
NZX	New Zealand stock exchange
OECD	Organisation for Economic and Co-operation Development
OTT	Over the top
Pay TV	Generic term for all forms of TV services that consumers pay for, including linear, PPV, VOD and OTT services delivered across all types of platforms (eg, satellite, cable, UHF and internet)
Plum	Plum Consulting
PPV	Pay-per-view
Proposed merger	Proposed merger of Vodafone and Sky
Quad play	Bundle of mobile, fixed-line voice, fixed-line broadband and pay TV services
s	Section
RFP	Request for proposal
Sky	Sky Network Television Limited
Sky TV	Sky pay TV packages that include Sky Basic
Spark	Spark New Zealand Limited
STB	Set top box
SVOD	Subscription VOD
Triple play	Bundle of fixed-line voice, fixed-line broadband and pay TV services
Trustpower	Trustpower Limited
TSP	Telecommunications service provider
TUANZ	Telecommunications Users Association of New Zealand Inc.
TV	Television
TVNZ	Television New Zealand Limited
TVOD	Transactional VOD
UBA	Unbundled bitstream access
UCLL	Unbundled copper local loop
UFB	Ultra-fast broadband
UHF	Ultra-high frequency
VDSL	Very high bitrate digital subscriber line
Vocus	Vocus Communications Limited
VOD	Video on demand
Vodafone	Vodafone New Zealand Limited
Vodafone Europe	Vodafone Europe B.V.
Vodafone Group	Vodafone Group plc and its wholly owned subsidiaries including Vodafone Europe B.V. and Vodafone New Zealand Limited
VoIP	Voice over internet protocol

Executive summary

- X1. The Commission declines to give clearance to the Applications because it is not satisfied that the proposed merger will not have, or would not be likely to have, the effect of substantially lessening competition in the relevant broadband and mobile services markets in New Zealand.
- X2. Specifically, the Commission cannot exclude a real chance that the merged entity would leverage its market power over premium live sports content, foreclosing competition in the relevant broadband and mobile services markets over the medium to long term.
- X3. The proposed merger would combine Sky's pay television (TV) business with Vodafone's broadband and mobile services businesses. The merged entity would be majority owned and controlled by Vodafone Group.
- X4. In order to grant clearance to the proposed merger, the Commission must be satisfied that the proposed merger will not be likely to substantially lessen competition in any market. If the Commission is not satisfied, including if it is left in doubt, then it must decline to give clearance. The onus is on the Applicants to satisfy the Commission, but the Commission must also undertake its own inquiries and analysis and apply its own knowledge and expertise before reaching any conclusion.
- X5. The proposed merger would be a vertical/conglomerate merger between a major telecommunications provider and the major pay TV provider in New Zealand that, in particular, has the exclusive rights to broadcast a significant amount of New Zealand premium live sports content.
- X6. The context in which the proposed merger would be taking place made this a particularly challenging assessment. It is occurring at a time of rapid change in telecommunications (including broadband and mobile) and pay TV services. Technologies are evolving quickly and converging, ultra-fast broadband (UFB) is being rolled out and 5G mobile networks are expected to be deployed in the next five years. Consumer behaviour is also changing and, in particular, consumers are viewing more content over broadband and mobile networks.
- X7. After considering all the evidence in the round, and applying our expertise and analysis, the Commission was unable to exclude a real chance that the merger would result in a substantial lessening of competition in the relevant broadband and mobile services markets.
- X8. Sky TV, and specifically Sky Sport, has a substantial customer base – approximately []% of broadband customers subscribe to Sky Sport and approximately []% of mobile customers are in households with a Sky Sport subscription. The vast majority of Sky subscribers watch Sky's premium live sports content on Sky Sport. The evidence suggests that for Sky Sport subscribers there is no close substitute for this content.

- X9. We have been unable to exclude the real chance that the merged entity would use its market power over premium live sports rights to effectively foreclose a substantial share of telecommunications customers from rival telecommunications services providers (TSPs), resulting in a substantial lessening of competition in broadband and mobile services markets.
- X10. The merged entity's incentives would be to maximise the combined profits across Sky's pay TV business and Vodafone's broadband and mobile services businesses. The merged entity would have the ability – and we cannot exclude a real chance that it would have the incentive – to use its market power over premium live sports rights to supply bundles of pay TV, broadband and mobile services with which rival TSPs would be unable to effectively compete.
- X11. By contrast, without the merger, Vodafone and Sky would be independent and, separately, seek to maximise their own profits. Sky may choose to develop its products in a number of ways, but in our view it would be likely to shift to supplying more content over broadband and mobile networks. Importantly, Sky would have no reason to favour Vodafone over any other TSP. We do not, however, consider that Vodafone would be likely to expand its own pay TV offering (which is currently very limited) independently from Sky.
- X12. Both the broadband and, particularly, mobile services, markets are characterised by a relatively small number of TSPs that are likely to be the significant drivers of price competition. These TSPs are likely to be those that make the investments in their networks that will drive competition in the future. If any one of them was foreclosed from competing for a significant number of customers, this would have the potential to undermine future investment and substantially lessen competition in one or both telecommunications markets.
- X13. We cannot rule out a real chance that the merged entity would have both the ability and incentive to offer Sky Sport subscribers (and those thinking of subscribing to Sky Sport) bundles of pay TV, broadband and mobile services that are more attractive than they would otherwise be able to acquire. The proposed merger would facilitate the development of integrated bundles, with new and additional features. Such features could include exclusive content and 'zero rated' Sky Sport viewing over mobile.
- X14. The merged entity would be able to structure the relative price of its bundles such that consumers would not be able to match the offer by subscribing, separately, to Sky Sport, and broadband and/or mobile services from a rival TSP. This might include discounts for taking a bundle of services and/or increasing the relative price of the standalone Sky Sport. Since the merged entity would also set the terms on which rival TSPs could re-sell Sky Sport, it would also be able to prevent rival TSPs from creating bundles using Sky Sport that could effectively compete with the merged entity's bundles.
- X15. These bundles are likely to be attractive to a large proportion of Sky Sport subscribers who are not already Vodafone telecommunications customers, and we

cannot exclude a real chance that a significant number would switch their broadband and/or mobile accounts to the merged entity. Furthermore, there is evidence that the customers that would switch would be higher ARPU customers than non-Sky subscribers.

- X16. There are developments in the broadband and mobile services markets that are likely to further drive switching to the merged entity. In the broadband services market, the roll-out of UFB presents a significant opportunity for Vodafone (and other TSPs) to attract new customers. During this period, an increased number of consumers are likely to be 'in play' and looking at alternative offers, increasing the ability of the merged entity to attract these customers with exclusive bundles that rival TSPs cannot match.
- X17. In the mobile services market, the evidence suggests that consumer preferences are changing. Mobile data consumption has been increasing rapidly, and more content is being viewed over mobile networks. This convergence between content and mobile services is likely to increase the attraction of the merged entity's bundles, particularly as mobile data prices continue to fall.
- X18. By offering bundles that include mobile, as well as broadband, services and pay TV, Sky Sport customers are more likely to move both their broadband and mobile services to the merged entity, even if they are not currently viewing a lot of content over mobile.
- X19. Competition may increase in the short term as rivals try to retain customers by developing alternative offers (eg, bundling other types of products, increasing data allowances and/or reducing prices). However, they will be unable to match the merged entity's offers if they do not have access to equivalent premium live sports content. Since the merged entity would be likely to continue to control all New Zealand premium live sports rights, for which there is no close substitute, a significant number of customers would be foreclosed to rival TSPs.
- X20. Therefore we could not rule out the real chance that rival TSPs would lose a significant number of their customers in both the broadband and mobile services markets.
- X21. Once customers have switched to one of the merged entity's bundles, they are likely to become 'stickier' and harder for rival TSPs to win back, requiring even better promotional or other deals to compensate for the fact that they do not offer a close substitute for the merged entity's premium live sports offering. The likely return on promotional investments would also be reduced, undermining the incentive to make them.
- X22. Over time, the inability of rival TSPs to compete with the merged entity's bundles would be likely to result in a smaller pool of potential customers and loss of scale as a consequence. Further, given that there is evidence suggesting that these customers are more likely to be low ARPU customers (compared with Sky TV

subscribers), we cannot rule out a real chance that this pool of customers would generate lower returns.

- X23. We attempted to assess the potential impact of a significant loss of customers and scale on each of the rival TSPs that we identified as significant drivers of price competition. This was a difficult assessment and required a number of assumptions to be made. In the context of the significant changes occurring in the relevant broadband and mobile services markets, and the inherent uncertainty that they bring, it was difficult to assess the reasonableness of those assumptions.
- X24. On the basis of the evidence before us, we could not rule out a real chance that one or more of the significant TSPs in the broadband and mobile services markets would suffer a significant loss of scale. This would squeeze margins and reduce their ability and incentive to invest and innovate in the future, materially lessening the competitive constraint that they impose in the market. This, in turn, would allow the merged entity to raise or maintain prices at levels higher than would prevail absent the merger.
- X25. We also considered whether rival TSPs would be likely to enter or expand if prices later rose. It was difficult to assess the likelihood and effectiveness of such entry over the relevant timeframe, given the level of uncertainty regarding how the relevant markets are likely to evolve. However, we considered that rival TSPs would face a number of potential barriers to entry and expansion, especially in the mobile services market.
- X26. Importantly, it is also likely that consumer switching behaviour will be asymmetric once the UFB rollout 'event' is over and given the unbundling costs faced by consumers – the evidence suggests that customer churn is significantly reduced for customers on bundles. This would increase customer acquisition costs and likely put a significant number of customers 'out of reach' of rival TSPs.
- X27. On the basis of the evidence before us, we have therefore been unable to exclude the real chance that the proposed merger would be likely to substantially lessen competition in, separately, the markets for broadband and mobile services.
- X28. For these reasons, we decline to give clearance to the proposed merger.

The proposed merger

Summary of the proposed merger

1. On 29 June 2016, the Commerce Commission (the Commission) registered applications for two interdependent transactions under s 66(1) of the Commerce Act 1986 (the Applications):
 - 1.1 the proposed acquisition by Sky Network Television Limited (Sky) of 100% of the shares in Vodafone New Zealand Limited (Vodafone); and
 - 1.2 the proposed acquisition by Vodafone Europe B.V. (Vodafone Europe, a wholly-owned subsidiary of Vodafone Group plc (Vodafone Group)) of 51% of the shares in Sky.
2. Together, the transactions (referred to in this Determination as ‘the proposed merger’) would have the combined effect of Sky and Vodafone (the Applicants) coming under the common control of Vodafone Group. Given the interconnected nature of the transactions, we considered the Applications together.

Applicants’ rationale for the proposed merger

3. The Applicants submitted, in summary, that:¹

The proposed transaction will combine Vodafone’s and SKY’s complementary businesses to create an entity that combines Vodafone’s mobile and fixed telecommunications networks with SKY’s TV offering. This will assist the Combined Group to provide a better customer experience and to enhance cross-marketing opportunities, and lead to faster innovation to meet changing customer needs.
4. Acknowledging a successful and complementary existing strategic relationship, they submitted that “... the Combined Group will build on this foundation to meet customers’ converging communications and viewing preferences.”²
5. The Applicants consider that a benefit of the proposed merger would be “innovating and creating new engaging digital products”³ and aligning incentives to enable them to “design more attractive packages”.⁴
6. In describing their separate rationales for the merger, the Applicants also elaborated upon the perceived benefits of combining their businesses within the context of converging telecommunications and pay television (TV) services markets.
7. Vodafone elaborated that the merger would:⁵

¹ The Applications at 2.

² Ibid.

³ Ibid.

⁴ Ibid at [11.14].

⁵ Ibid at [4.2].

- 7.1 allow faster innovation to create new digital products and thus meet converging communications and viewing preferences to provide a better customer experience;
 - 7.2 allow enhanced cross-marketing opportunities (given the complementary strengths of the two businesses); and
 - 7.3 deliver an enhanced customer experience, thus accelerating the take-up of high speed broadband.
8. Sky advised that the proposed merger would help it to adapt to the increasing delivery and consumption of video content over broadband and mobile networks.⁶ Sky considers this is being driven by: the increasing prevalence of high-speed internet; the increasing speed of mobile networks; the low cost of delivering content over the internet; and the changing preferences of consumers to consume video on demand (VOD).⁷

Our decision

- 9. The Commission declines to give clearance to the Applications because it is not satisfied that the proposed merger will not have, or would not be likely to have, the effect of substantially lessening competition in a market or markets in New Zealand.
- 10. Specifically, the Commission cannot exclude a real chance that the merged entity would leverage its market power over premium live sports content, foreclosing competition in the relevant broadband and mobile services markets over the medium to long term.

Our framework

- 11. Our approach to analysing the competition effects of the proposed merger is based on the principles set out in our Mergers and Acquisitions Guidelines.⁸

The substantial lessening of competition test

- 12. As required by the Commerce Act 1986, we assess mergers using the substantial lessening of competition test.⁹
- 13. We determine whether a merger is likely to substantially lessen competition in a market by comparing the likely state of competition if the merger proceeds (the scenario with the merger, often referred to as the ‘factual’), with the likely state of competition if the merger does not proceed (the scenario without the merger, often referred to as the ‘counterfactual’).¹⁰

⁶ Ibid at [4.3-4.4].

⁷ Ibid at [4.4].

⁸ Commerce Commission, *Mergers and Acquisitions Guidelines* (July 2013).

⁹ A substantial lessening of competition includes the “hindering or preventing of competition”: Commerce Act 1986, s 3(2).

¹⁰ *Commerce Commission v Woolworths Limited* (2008) 12 TCLR 194 (CA) at [63].

14. The present state of competition in a market (often referred to as the 'status quo') may not be the counterfactual that we use for our competition assessment. Where we regard it as likely that the future without the merger would be different from the status quo (because of technological developments or some other reason), we may identify a likely counterfactual that is different from the status quo.
15. We make a pragmatic and expert assessment of what is likely to occur in the future with and without the merger based on the information we obtain through our investigation and taking into account factors including market growth and technological changes.
16. A lessening of competition is generally the same as an increase in market power. Market power is the ability to raise price above the price that would exist in a competitive market (the 'competitive price'), or reduce non-price factors such as quality or service below competitive levels.
17. Determining the scope of the relevant market or markets can be a useful tool in determining whether a substantial lessening of competition is likely.
18. We define markets in the way that we consider best isolates the key competition issues that arise from the merger. In many cases this approach may not require us to precisely define the boundaries of a market. A relevant market is ultimately determined, in the words of the Commerce Act 1986, as a matter of fact and commercial common sense.¹¹

When a lessening of competition is substantial

19. Only a lessening of competition that is substantial is prohibited. A lessening of competition will be substantial if it is real, of substance, or more than nominal.¹² Some courts have used the word 'material' to describe a lessening of competition that is substantial.¹³
20. Consequently, there is no bright line that separates a lessening of competition that is substantial from one that is not. What is substantial is a matter of judgement and depends on the facts of each case.¹⁴ Ultimately, we assess whether competition will be substantially lessened by asking whether consumers in the relevant market(s) are likely to be adversely affected in a material way.
21. A lessening of competition need not be felt across an entire market to be substantial. A substantial lessening of competition in a significant section of a market, may, according to the circumstances, be a substantial lessening of competition in a

¹¹ Section 3(1A). See also *Brambles v Commerce Commission* (2003) 10 TCLR 868 at [81].

¹² *Woolworths & Ors v Commerce Commission* (2008) 8 NZBLC 102,128 (HC) at [127].

¹³ *Ibid* at [129].

¹⁴ For example, while a merger that allows the merged entity to raise prices by 5-10% would substantially lessen competition, a lower increase may also be 'substantial' in some markets. See *ibid* at [138].

market.¹⁵ While we commonly assess competition effects over the short term (up to two years), the relevant timeframe for assessment depends on the circumstances. A longer timeframe will be appropriate if, on the evidence, competition effects are likely to arise in later years.¹⁶ Indeed, some transactions which arguably produce competitive benefits in the immediate or short term, can give rise to a substantial lessening of competition over a more extended timeframe.

When a substantial lessening of competition is likely

22. A substantial lessening of competition is ‘likely’ if there is a real and substantial risk, or a real chance, that it will occur.¹⁷ This requires that a substantial lessening of competition is more than a possibility, but does not mean that the effect needs to be more likely than not to occur.¹⁸

The clearance test

23. In *Commerce Commission v Woolworths*, the Court of Appeal found:¹⁹

... [W]hat constitutes a substantial lessening of competition must in the end be a matter of judgment, although we accept, of course, that such a judgment must be informed by as much practical evidence as possible.

24. Not all evidence of past or present conduct or events provides a reliable predictor of future likely impact.²⁰ In addition, there may be insufficient evidence to justify a conclusion that there is no likelihood of a substantial lessening of competition in any particular case.²¹ We will sometimes have before us conflicting evidence from different market participants and must determine what weight to give to the evidence of each party.²²
25. The Commission must make a reasonable enquiry into a clearance application.²³ However, the burden of proof ultimately lies with the Applicants to satisfy us on the balance of probabilities that the proposed merger is not likely to have the effect of substantially lessening competition.²⁴

¹⁵ *Dandy Power Equipment Pty Ltd & Anor v Mercury Marine Pty Ltd* (1982) 64 FLR 238, 260; 44 ALR 173, 192; ATPR 40-315, 43,888, cited with approval by McGechan J in *Commerce Commission v Port Nelson Ltd* (1995) 6 TCLR 406 at [435].

¹⁶ *Woolworths & Ors v Commerce Commission* (HC) above n12 at [131].

¹⁷ *Ibid* at [63].

¹⁸ *Ibid* at [111].

¹⁹ *Commerce Commission v Woolworths Ltd* (CA) above n10 at [101].

²⁰ See, for example, the discussion of evidence in *Commerce Commission v Woolworths Ltd* (CA) above n10 at [192].

²¹ See, for example, *ibid* at [197].

²² *Brambles New Zealand Ltd v Commerce Commission* above n11 at [64].

²³ *Commerce Commission v Woolworths Ltd* (CA) above n10 at [101].

²⁴ *Commerce Commission v Southern Cross Medical Care Society* (2001) 10 TCLR 269 (CA) at [7] and *ibid* at [97].

The meaning of ‘in doubt’

26. We must clear a merger if we are satisfied that the merger would not be likely to substantially lessen competition in any market.²⁵ If we are not satisfied – including if we are left in doubt – we must decline to clear the merger.²⁶
27. In *Commerce Commission v Woolworths*, the Court of Appeal considered what it means to be left ‘in doubt’ as to whether a merger is likely to substantially lessen competition. It held that:²⁷
- the existence of ‘doubt’ corresponds to a failure to exclude a real chance of a substantial lessening of competition.
28. If, after considering all the evidence, we are left in doubt – that is, we have been unable to exclude a real chance of a substantial lessening of competition – we must decline to clear the merger.
29. The source of doubt is irrelevant. There is no significant difference between uncertainty associated with deficiencies in the evidence and uncertainty associated with the impracticality of predicting future events – in either case, the Commission must decline the clearance application.²⁸

Applying the clearance test in this case

30. Applying the clearance test always involves some degree of uncertainty. Comparisons of what may happen with or without the merger (the factual and counterfactual) both involve making predictions about the future and are therefore “necessarily incapable of accurate assessment”.²⁹
31. However, the information considered during our assessment of the merger demonstrated that the nature of the changing and converging services at issue renders the level of uncertainty in this case higher than in others. We summarise some of these below but discuss them further in the detailed reasons that follow.
32. The proposed merger is taking place at a time of significant change in each of pay TV, broadband and mobile services, and further significant changes are expected in the future. We discuss this in detail in later sections relating to industry trends and the context of the proposed merger.
- 32.1 There have been consistent improvements in the quality and availability of broadband and mobile networks. The continued roll-out of the new high speed ultra-fast broadband (UFB) network means that approximately 1.1 million premises will be able to switch to UFB in the next two years.

²⁵ Section 66(1) of the Commerce Act 1986.

²⁶ *Commerce Commission v Woolworths Limited (CA)*, above n10 at [98].

²⁷ *Ibid.*

²⁸ *Ibid* at [93].

²⁹ *Ibid* at [75].

- 32.2 Similarly, 5G technology, when it arrives, is likely to result in further improved mobile services.
- 32.3 Over the top (OTT) players have entered the market and have attracted viewers, contributing to an increase in the amount of content that is viewed over the internet, and the corresponding surge in data consumption.
- 32.4 Telecommunications and broadcasting markets are ‘converging’, or becoming more closely linked, and the technologies used to deliver broadband and mobile are also converging, with the infrastructure used to deliver these services becoming more common to both.
- 32.5 There has been an increase in the uptake of bundles of telecommunications services and content.³⁰
33. The proposed merger would result in a single, vertically integrated pay TV, broadband (including voice)³¹ and mobile provider with the exclusive rights to broadcast premium live sports content. As discussed at [259-263], below, there are no close substitutes for Sky’s premium live sports content and we consider that it is a source of market power for Sky, and would similarly be a source of market power for the merged entity.
34. The merged entity’s incentives will be different from the incentives of Vodafone and Sky in the counterfactual, most importantly because it will own both broadband and mobile capabilities and premium live sports content for which there is no close substitute. It will therefore have the ability and potentially the incentive to leverage its market power over this content by bundling it with broadband and mobile services.
35. What these bundles look like will be a function of the merged entity’s assessment of what will be attractive to consumers, and the terms on which they will be available (including price) will depend on its assessment of the short and long run costs and benefits to the merged entity.
36. Consumers may well be better off in the short term, as the merged entity introduces more attractive bundles to consumers. However, our focus is on whether competition is likely to be impacted in the medium to long term.³² The degree of uncertainty associated with predicting future events is higher in this instance given the evolving nature of the relevant products and services.
37. The expected changes in consumer behaviour and technology, together with the changed incentives of the merged entity, will all affect consumer demand,

³⁰ See Figure 11, below.

³¹ In this Determination, we define broadband services to include voice services because both are typically purchased from the same broadband supplier in a bundle. See, for example, Vodafone New Zealand Limited and TelstraClear Limited [2012] NZCC 33 at [79-83].

³² We consider the medium to long term to be, approximately, the 2-5 years post-merger, however we do not rule out the real chance of effects occurring before or after this period.

competitive behaviour, and the services and bundles that the merged entity would have the ability and incentive to offer in the future.

38. We collected and reviewed some useful evidence from which to construct the factual and counterfactual and our competition analysis. However, we also note that a number of parties provided some submissions on the merger that did not seem, to us, to accord entirely with statements made by the submitters elsewhere, including in internal records. We did not consider that all evidence of past or present conduct or events provided a reliable predictor of future likely impact.
39. Ultimately, the uncertain nature of the matters relevant to our assessment of the merger made it challenging for us to be positively satisfied, one way or the other, about how the proposed merger would impact each of the relevant broadband and mobile services markets, and the timeframe over which these effects would take place.
40. We therefore applied the decision framework set out by the Court of Appeal in *Woolworths* when assessing the position of doubt. We asked: are we able to exclude a real chance of a substantial lessening of competition? We concluded that we could not.

Key parties

Vodafone

41. Vodafone Europe is a wholly owned subsidiary of Vodafone Group (a company listed on the UK stock exchange). Vodafone Europe is the current owner of Vodafone.
42. Vodafone is a telecommunications service provider (TSP) in New Zealand offering fixed and mobile services, including fixed and mobile broadband internet to residential and business customers. As at October 2016, Vodafone had [] mobile customer connections and [] fixed-line customer connections.³³ Vodafone states that its mobile network covers 98.5% of the population.³⁴ Vodafone also offers wholesale services using its national fibre backhaul and mobile networks.³⁵
43. Vodafone offers customers the opportunity to acquire TV content in packages bundled with its telecommunications services. To enable this, Vodafone is a reseller of Sky services, where customers are invoiced by Vodafone for the provision of a Sky decoder and Sky TV. It also retransmits Sky TV and free-to-air (FTA) services to customers using a Vodafone set top box (STB). Its contract with Sky is non-exclusive – while Sky can enter into similar reselling arrangements with other TSPs if it chooses,

³³ E-mail from Bell Gully (on behalf of Vodafone) to the Commerce Commission (5 December 2016).

³⁴ <http://www.vodafone.co.nz/network/coverage/>.

³⁵ For a description of backhaul services see [81-85], below.

there are restrictions on the pay TV services that Vodafone can offer to its telecommunications customers.³⁶

44. As at August 2016, Vodafone was reselling³⁷ Sky TV to [] customers and retransmitting³⁸ Sky TV to [] customers (a combined total of [] customers).^{39 40}

Sky

45. Sky is listed on both the New Zealand and Australian stock exchanges.
46. Sky's principal business is supplying pay TV services to its subscriber base. Sky offers a range of news, sport, movies and general entertainment channels. Sky's 'Basic' package offers subscribers access to 50 channels of general entertainment. All Sky TV subscriptions must include a 'Basic' subscription. Subscribers can also choose to subscribe to more content for an additional charge (eg, 'Sky Movies', 'Sky Sport' and the 'SOHO' channel).
47. Sky holds the exclusive rights for live broadcast of many of the most popular sports in New Zealand including rugby, rugby league (NRL), cricket and netball.⁴¹
48. Sky's primary distribution method is via satellite. It also has online services including:
- 48.1 SkyGo: a service that enables Sky TV satellite subscribers to view programming over the internet;
- 48.2 FanPass: an OTT service, available to those with and without a Sky TV subscription, providing access to certain events on a pay-per-view (PPV) basis and Sky Sport Channels 1-4 on a short term subscription basis (a day, a week or a month); and
- 48.3 NEON: an OTT subscription video on demand (SVOD) service available to Sky TV and non-Sky TV subscribers.
49. In addition, Sky owns 100% of Igloo, an ultra-high frequency (UHF)-based pay TV service.⁴² It also owns the FTA TV channel, Prime.

³⁶ As noted in our Sky *Contracts* investigation,

[]. Commerce Commission Investigation Report on Sky TV contracts (8 October 2013) at [100-101].

³⁷ That is, selling Sky TV to customers, who are invoiced by Vodafone for the provision of a Sky decoder and Sky TV.

³⁸ That is, selling Sky TV to consumers, who watch Sky TV (and Freeview) on a Vodafone STB.

³⁹ E-mail from Bell Gully (on behalf of Vodafone) to the Commerce Commission (3 October 2016).

⁴⁰ Vodafone also has a very limited movie offering, where customers with Vodafone STBs can purchase movies (sourced directly by Vodafone) on a pay-per-view (PPV) basis. At the time of filing of the Applications, around [] customers used this service per month. See the Applications at footnote 2.

⁴¹ Sky's ownership of these rights, which are described as 'premium live sports' rights in this Determination, is central to our consideration of whether the proposed merger is likely to substantially lessen competition, and is described in detail further below.

50. As at October 2016, Sky had []⁴³ satellite subscribers, [] or []% of which also subscribed to Sky Sport for an additional charge. Sky also had other subscribers accessing content over the internet ([] NEON subscribers and [] FanPass subscribers) and around [], UHF-based, Igloo subscribers.⁴⁴
51. Sky's subscriber base has been declining and in February 2017 it presented its 2016 interim results, showing a 32% year on year decrease in net profit after tax.⁴⁵ Sky TV's net subscriber numbers reduced between 30 June 2013 and 31 May 2016 by approximately []⁴⁶ ([]⁴⁷).
52. In addition to its pay TV services, Sky's wholly-owned subsidiary, Outside Broadcasting Limited, owns and operates specialist equipment to film and produce live sports and other events for Sky (and others).
53. Sky does not provide telecommunications services. Sky's participation in telecommunications markets is limited to referring Sky customers to Vodafone to acquire residential fixed-line broadband services. Referred Sky customers that sign up for Vodafone services receive a discount on their Sky bill.⁴⁸ From [], when the referral agreement was signed, to 30 June 2016, [] customers had been referred to Vodafone by Sky and signed up for Vodafone broadband services.⁴⁹

Other TSPs

54. Vodafone is one of New Zealand's major retail TSPs. The other major TSPs are Spark New Zealand Limited (Spark), Two Degrees Mobile Limited (2degrees), Vocus Communications Limited (Vocus) and Trustpower Limited (Trustpower).

Spark

55. Spark offers broadband and mobile services to residential and business customers and, as at October 2016, had [] mobile customer connections and [] broadband connections.⁵⁰ Spark's retail brands include Spark (mobile and broadband), Skinny (mobile and fixed wireless broadband) and Bigpipe (broadband).

⁴² Igloo is available to those with and without a Sky TV subscription. Sky has announced that its Igloo service will cease in 2017 and is offering Igloo customers a deal on Sky basic services. See <https://www.sky.co.nz/igloo-closed>.

⁴³ This includes customers contracting directly with Sky and that subscribed to Sky via a third party (eg, Vodafone).

⁴⁴ Letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (11 November 2016) at 6-7 and Commerce Commission interview with Sky (14 July 2016).

⁴⁵ <https://www.nzx.com/companies/SKT/announcements/297166>.

⁴⁶

[]

⁴⁷ Sky Application at Annexure D.

⁴⁸ The Applications at [10.13]. Details of Sky's broadband offer (including the \$10 discount) can be found at <https://www.sky.co.nz/broadband>.

⁴⁹ E-mail from Bell Gully (on behalf of Vodafone) to the Commerce Commission (5 December 2016).

⁵⁰ E-mail from Spark to the Commerce Commission (12 December 2016).

Spark states that its mobile network covers 97% of New Zealanders.⁵¹ Spark also offers wholesale services using its national fibre backhaul and mobile network.⁵²

56. Spark launched Lightbox in August 2014. Lightbox is an SVOD service offering TV series content. Lightbox is available free with Spark's telecommunications services and for a monthly charge on a standalone basis to non-Spark customers. As at 2 August 2016, Lightbox had [] subscribers.⁵³
57. Spark has agreements with other content owners to include products as part of its telecommunication bundles. Namely, it offers Spotify's 'Premium' music service at no additional cost to mobile services customers on qualifying plans⁵⁴ and in late 2016 reached an agreement with Netflix to provide Spark customers free Netflix for 12 months on certain broadband plans.⁵⁵

2degrees

58. 2degrees commenced operations as New Zealand's third mobile network operator (MNO) in 2009. It initially focused on retail pre-pay mobile services for residential customers but it has since expanded into on-account mobile services for residential and business customers. 2degrees' website states that it covers "97.5% of places New Zealanders live and work".⁵⁶ 2degrees reaches 95% of the population through its own network and 2.5% through roaming arrangements with Vodafone.⁵⁷ 2degrees also offers broadband and voice services following its acquisition of internet service provider Snap in March 2015. As at October 2016, 2degrees had [] mobile customer connections and [] broadband connections.⁵⁸

Vocus

59. Vocus is a provider of telecommunications services in both New Zealand and Australia. Vocus provides broadband services to residential and business customers. Vocus also provides mobile services on a mobile virtual network operator (MVNO) basis using Spark's network. Vocus' brands include Flip, Slingshot and Orcon (all of which are targeted at residential customers), and Callplus (targeted at business customers). As at October 2016, Vocus had [] residential broadband connections.⁵⁹ Vocus also offers wholesale services using its national fibre backhaul network.⁶⁰

⁵¹ <http://www.spark.co.nz/coverage>.

⁵² <https://www.sparkwholesale.co.nz/s/Home>.

⁵³ Appendix 1 to submission from Spark to the Commerce Commission (12 August 2016) at [16].

⁵⁴ <https://www.spark.co.nz/shop/mobile/whyultramobile/activatespotifypremium/>.

⁵⁵ E-mail from Spark to the Commerce Commission (12 December 2016). Spark publicly announced this agreement on 27 February 2017: at <https://www.sparknz.co.nz/news/spark-partners-netflix/>.

⁵⁶ <https://www.2degreesmobile.co.nz/coverage/>.

⁵⁷ Submission from 2degrees to the Commerce Commission (12 August 2016) at [1.2].

⁵⁸ E-mail from 2degrees to the Commerce Commission (1 December 2016).

⁵⁹ E-mail from Vocus to the Commerce Commission (5 December 2016).

⁶⁰ Commerce Commission interview with Vocus (29 July 2016).

60. On 1 December 2016 Vocus completed the purchase of Switch, an energy provider.⁶¹ Vocus has announced that it will offer bundles of energy and broadband services to customers.⁶²

Trustpower

61. Trustpower is a wholesale and retail energy company that operates in the New Zealand and Australian electricity markets. In 2004 Trustpower started offering telecommunications services⁶³ and now offers bundles of electricity, gas and telecommunications services. As at October 2016, Trustpower had [] broadband connections.⁶⁴
62. Trustpower submitted that it would like to expand into offering mobile services on an MVNO basis,⁶⁵ []^{66 67}

Other providers of TV content

63. As acknowledged by the Applicants, Sky is New Zealand's leading pay TV provider, with a portfolio of premium content.⁶⁸
64. There are several other providers of online pay TV services:
- 64.1 Quickflix launched SVOD services in New Zealand in 2012 and as at 3 August 2016 had [] subscribers in New Zealand;⁶⁹
- 64.2 Lightbox (as noted above) was launched by Spark in 2014 and as at 2 August 2016 had [] subscribers in New Zealand;⁷⁰
- 64.3 Netflix launched SVOD services in New Zealand in 2015 and as at June 2016 had an estimated 264,000 subscribers in New Zealand;⁷¹

⁶¹ http://www.nzherald.co.nz/business/news/article.cfm?c_id=3&objectid=11758435.

⁶² http://m.nzherald.co.nz/telecommunications/news/article.cfm?c_id=93&objectid=11810765.

⁶³ Submission from Trustpower to the Commerce Commission (14 August 2016) at 3.

⁶⁴ E-mail from Trustpower to the Commerce Commission (1 December 2016).

⁶⁵ Submission from Trustpower to the Commerce Commission (14 August 2016) at v.

⁶⁶ Trustpower

[

]. Submission from Trustpower to the Commerce

Commission (14 August 2016) at 24.

⁶⁷ Vodafone advised that

[

]. Submission from Vodafone to the Commerce Commission (11

September 2016) at [10.4].

⁶⁸ Vodafone and Sky NZX announcement of the proposed merger (9 June 2016) at 2.

⁶⁹ Commerce Commission interview with Quickflix (3 August 2016).

⁷⁰ Submission from Spark to the Commerce Commission (12 August 2016) at [16]. Spark offers Lightbox free to customers on certain broadband and mobile contracts: <https://www.spark.co.nz/getmore/lightbox/>.

[] Commerce Commission interview with Spark (3 August 2016).

⁷¹ http://www.nzherald.co.nz/entertainment/news/article.cfm?c_id=1501119&objectid=11651395.

- 64.4 beIN launched a live streaming service in October 2016 for English Premier League games;⁷² and
- 64.5 Amazon Prime launched SVOD services in December 2016.⁷³
- 65. None of these providers offer live sports content other than beIN.
- 66. Other providers and platforms of FTA TV services in New Zealand include:
 - 66.1 Television New Zealand Limited (TVNZ), which broadcasts TVNZ1 and TVNZ2;
 - 66.2 Mediaworks TV Limited (Mediaworks), which broadcasts Three and Bravo;
 - 66.3 Maori Television, New Zealand’s indigenous broadcaster; and
 - 66.4 Freeview Limited (Freeview), a joint venture between TVNZ, MediaWorks, Maori Television and Radio New Zealand, that provides a platform for accessing FTA TV and radio content.⁷⁴

Relationship between Sky and other TSPs

- 67. As noted at [43], above, Vodafone resells and retransmits Sky TV on a non-exclusive basis. It offers bundles of Sky and broadband to its customers.
- 68. Sky has had commercial relationships with TSPs other than Vodafone in the past, as well as with other commercial partners []. Sky’s relationships with TSPs are detailed below.

68.1 []⁷⁵

68.2 []⁷⁶
[]

⁷² <https://www.nbr.co.nz/article/promises-promises-bein-says-launch-announcement-coming-later-today-ck-p-coys-195869>. Sky also hosts beIN’s coverage on its platform, and Sky subscribers can view this footage through their Sky box. []

⁷³ http://www.nzherald.co.nz/entertainment/news/article.cfm?c_id=1501119&objectid=11767287.
⁷⁴ Freeview is used in 75% of New Zealand households. It has 35 TV and radio services and, since 2015, can be viewed over broadband as well as satellite: submission from Freeview to the Commerce Commission (12 August 2016) at [1.2], [2.2] and [2.4].

⁷⁵ []
⁷⁶ [] provided under cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (2 September 2016).

] ⁷⁷

68.3 []

] ⁷⁸
] ⁷⁹

69. Sky has also negotiated with these and other TSPs about reselling its services at various other times in recent years, including during the time of our assessment of the Applications.

Industry background

Introduction

70. Broadband, mobile and pay TV services are currently undergoing a period of significant change, and this is expected to continue in the future. In this section we set out the key concepts and players, before moving on to explain the trends and changes in the following section.

Broadband⁸⁰

Market participants

71. Broadband is a generic term for a data service giving high speed access to the internet; it is typically any data service faster than a dial-up modem. New Zealand has a large number of TSPs that sell broadband services on a retail basis. This is largely due to the Telecommunications Act 2001, which provides TSPs with regulated access to the local network infrastructure needed to provide broadband.⁸¹ Although there are many TSPs, the majority of residential and business broadband customers are supplied by the three largest TSPs (Spark, Vodafone and Vocus).

⁷⁷ []

⁷⁸ [] provided under cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (2 September 2016).

⁷⁹ []

⁸⁰ Unless otherwise specified, in this Determination 'broadband' refers to 'fixed line broadband' only. This includes Vodafone's HFC network, but does not include satellite and FWA.

⁸¹ This does not include most backhaul, which needs to be obtained (owned or acquired) separately.

Table 1: Share of broadband connections (October 2016)

Firm	Residential	Share	Business	Share
Spark	[]	[]%	[]	[]%
Vodafone	[]	[]%	[]	[]%
Vocus	[]	[]%	[]	[]%
Trustpower	[]	[]%	[]	[]%
2degrees	[]	[]%	[]	[]%
Others	[]	[]%	[]	[]%
Total	[]	100%	[]	100%

Notes: Includes fixed line connections only.

Source: TSPs, [

]. Total figure for residential

customers is from IDC for Q4 financial year 2016, provided by Spark in an e-mail to the Commerce Commission (12 December 2016). Total figure for business customers is the sum of the business customer numbers of each of the named TSPs.

Types of broadband and the shift to UFB

72. Most broadband in New Zealand (ADSL and VDSL) is currently delivered over the copper network of Chorus Limited (Chorus). However, with the roll-out of UFB, an increasing number of premises are connecting to higher speed fibre networks, and this trend is expected to continue.
73. In 2010, the Government launched the UFB Initiative in order to improve New Zealand's broadband services.⁸² The UFB Initiative provides funding to accelerate the roll-out of fibre optic cables throughout New Zealand. The aim is to provide fibre to 75% of premises by 2019,⁸³ and to 85% by 2024.⁸⁴ The Government has contracted with four companies, including Chorus, to deliver UFB. These are known as "UFB service providers" or "local fibre companies" (LFCs).⁸⁵
74. UFB provides significantly faster download speeds than are available over a copper network.⁸⁶ ADSL download speeds in urban areas are up to 30Mbps on basic broadband plans. A basic UFB plan delivers download speeds of up to 100Mbps.⁸⁷

⁸² For more information on the UFB programme see <http://www.mbie.govt.nz/info-services/sectors-industries/technology-communications/fast-broadband>.

⁸³ MBIE "Broadband deployment update" (December 2016).

⁸⁴ <https://www.beehive.govt.nz/release/ultra-fast-broadband-extended-151-towns>.

⁸⁵ The LFCs are Northpower Limited (Whangarei), WEL Networks (Waikato) and Enable Networks (Christchurch). Chorus (all other areas) is not strictly speaking an LFC, since it operates under a different commercial model.

⁸⁶ The UFB Initiative Policy is to offer services of at least 100Mbps download and 50Mbps upload speeds, which compares to an average speed of 7Mbps in 2014. <http://www.crownfibre.govt.nz/ufb-initiative/frequently-asked-questions/>.

⁸⁷ ADSL is the most commonly used broadband technology using the copper network. VDSL is faster, at speeds up to 70Mbps. UFB speeds can reach up to 1Gbps.

75. In addition, the technology being rolled out under the UFB Initiative requires LFCs to offer a “multicast” service. The multicast service allows a TSP to broadcast a media stream (such as TV content) to multiple consumers simultaneously. As the multicast service uses a different allocation of bandwidth to that allocated for broadband services, the use of multicast does not affect the performance of broadband (and vice versa). This means that pay TV providers can broadcast to multiple households simultaneously without compromising the quality (ie, responsiveness) of broadband services. Both the availability of UFB infrastructure and multicast service eases the way for consumers to increase their viewing of media over broadband.
76. For access to both copper and UFB networks, TSPs need to contract with a network service provider for access to the network.
77. Chorus owns the copper network that links homes and businesses to local exchanges, and TSPs can gain access under regulated prices. TSPs can choose between two services, which differ based on the extent to which the TSP uses its own equipment (UCLL⁸⁸) or Chorus’ (UBA⁸⁹) to manage traffic. Unbundling has afforded TSPs more control over the quality of their services and the ability to differentiate their services from their competitors.
78. For UFB, at present LFCs handle the broadband traffic on a local network on behalf of the TSP that operates on that network. From 2020, TSPs will be able to “unbundle” UFB, and install their own equipment at the exchange to handle their own traffic, similar to the UCLL service for copper.
79. As with copper, unbundling of fibre is likely to afford TSPs enhanced control over, and quality of, the services they provide to customers. The ability for TSPs to “unbundle” the UFB network may influence their investment decisions from 2020, as unbundling could require investments in equipment to install at exchanges.⁹⁰ In its submission on the Commission’s current Study of telecommunications backhaul services, Vodafone stated:⁹¹

We also expect increased competition and innovation in backhaul services in the future, especially from 2020 when we expect fibre unbundling will unleash investment in delivering high-speed broadband services and enable new and innovative ways for network operators and broadband service providers to move data up and down New Zealand.

80. Other ways to provide broadband are Vodafone’s hybrid fibre-coaxial (HFC) cable in Wellington, Christchurch and the Kapiti coast ([] subscriptions); fixed wireless

⁸⁸ Unbundled copper local loop. A TSP uses this service if it wishes to install its own equipment in the exchange. Doing so requires greater investment by the TSP but gives it more control over the quality of service. This is often referred to as “unbundling”.

⁸⁹ Unbundled bitstream access. Under this service Chorus uses its equipment in the exchange to manage the broadband traffic on its network on behalf of the TSP. This provides a relatively low-cost means for TSPs to provide retail broadband.

⁹⁰ We sought evidence from the Applicants and TSPs on the likely investments required, however they were not able to provide reliable estimates about the likely costs.

⁹¹ Vodafone “Section 9A Backhaul Study – Submission on Commerce Commission Paper” (23 September 2016) at 2.

access (FWA), which uses radio signals rather than cables to provide telecommunication services to consumers ([] subscriptions); and satellite broadband, which operates in a similar way to FWA and is generally used in remote areas ([] subscriptions).⁹²

Backhaul services

81. To provide a retail broadband service, a TSP must also have access to backhaul data transport services. Backhaul is a generic term used to describe the transport of data between regional and national data aggregation points. Backhaul generally involves carriage of signals by fibre optic cables rather than by copper cables; although it can also be provided by microwave radio.
82. Chorus, Vodafone, Spark and Vocus are among those that own network equipment enabling them to provide backhaul capability.⁹³ These TSPs use their backhaul networks to support their own retail requirements or to supply backhaul capacity on a wholesale basis. Other TSPs must pay one of the owners of the backhaul networks for access.
83. The TSP owners of backhaul networks (Spark, Vodafone and Vocus) are likely to have an advantage over those that do not own such infrastructure. Owning backhaul infrastructure allows TSPs greater control over the quality of the service that they provide to their customers.
84. []⁹⁴
[]⁹⁵
85. As UFB is rolled out, the volume of traffic on backhaul networks is likely to increase.⁹⁶ As this happens, even TSPs with a significant ‘footprint’ may need to make additional investments or purchase backhaul from another provider, and there is likely to be an increase in demand in areas currently supplied by one backhaul service provider.⁹⁷

⁹² Figures correct as at 30 June 2016, collected by the Commission from industry participants and rounded to the nearest 1,000.

⁹³ Commerce Commission “A Section 9A Backhaul Study – Preliminary questions in understanding domestic backhaul services” (12 August 2016) at [34-37].

⁹⁴ []

⁹⁵ Ibid at 5.

⁹⁶ Commerce Commission “A Section 9A Backhaul Study – Preliminary questions in understanding domestic backhaul services” (12 August 2016) at [40.1]. In its submission on the Study, Vodafone stated that it expects that monthly bandwidth requirements in 2019 will be 13 times greater than those in 2015: Vodafone “Section 9A Backhaul Study – Submission on Commerce Commission Paper” (23 September 2016) at 3.

⁹⁷ Commerce Commission “A Section 9A Backhaul Study – Preliminary questions in understanding domestic backhaul services” (12 August 2016) at [40.2] and [41.2]. In its submission on the Study, Vodafone submitted at 4 that: “The change to UFB also makes it a difficult time to assess the backhaul market. There are approximately 600 exchanges on the copper network. The UFB network will have considerably fewer, meaning some backhaul services will become redundant, and others will require a higher capacity. How this market will function in a few years’ time is decidedly unclear”.

Owning backhaul infrastructure is likely to confer more of an advantage as UFB is rolled-out.

Regulatory environment

86. The Ministry of Business Innovation and Employment (MBIE) is conducting a review of the Telecommunications Act 2001 to assess “whether the current regulatory framework for telecommunications in New Zealand is the optimal one for competition, investment and innovation after 2020”.⁹⁸
87. In December 2016, the Government agreed plans to introduce price-quality regulation for Chorus’ UFB services from 2020.⁹⁹ Under price-quality regulation an annual ‘maximum allowable revenue’ cap will be set for Chorus. In addition to the cap, Chorus will also be required to provide two regulated products with price and quality terms set by the Commission.¹⁰⁰
88. The existing obligation on Chorus and the LFCs to provide a layer 1 unbundled service on the UFB network from 2020 will be retained. The Commission will be able to classify a layer 1 unbundled service on Chorus’s UFB network as an ‘anchor’ product from 2024 following an investigation (subject to certain conditions being met).
89. The Government is currently considering how the Commission will be empowered to price-regulate fibre unbundling after 2020.¹⁰¹ LFCs will only be subject to information disclosure regulation from 2020 with monitoring and oversight by the Commission.¹⁰² They will not be subject to regulated price and quality terms, unless certain conditions are met.¹⁰³
90. Unlike in a number of other jurisdictions, New Zealand does not have any specific laws requiring TSPs to treat all internet traffic equally (known as ‘net neutrality’).¹⁰⁴ This means that TSPs can discriminate between different types of traffic,¹⁰⁵ either by:
 - 90.1 not carrying certain types of content; or
 - 90.2 limiting the speed at which certain content is carried (known as ‘throttling’), which impacts the quality of the content.

⁹⁸ MBIE “Telecommunications Act review: Public Questions and Answers” at 1.

⁹⁹ Cabinet Economic Growth and Infrastructure Committee “Review of the Telecommunications Act 2001: Final Policy Decisions for Fixed Line Communications Services” Minute of Decision (14 December 2016) at [12].

¹⁰⁰ The Government also proposes deregulating Chorus’ copper network inside areas where fibre is or becomes available, allowing Chorus to continue operating it or close it down (subject to some consumer safeguards): *ibid* at [64-65].

¹⁰¹ MBIE “Telecommunications Act Review: Cabinet Minute” (14 December 2016).

¹⁰² *Ibid* at [13].

¹⁰³ *Ibid* at [16-17].

¹⁰⁴ See, for example, the US Federal Communications Commission’s Open Internet Rules, adopted on 26 February 2015, and European Union Regulation 2015/2120 of 25 November 2015.

¹⁰⁵ Subject to Part 2 of the Commerce Act 1986.

Mobile services

Market participants

91. New Zealand has three MNOs: Spark, Vodafone, and 2degrees. Vodafone's and Spark's networks each cover approximately 97% of the population. 2degrees' network reaches approximately 95% of the population and it has a roaming agreement with Vodafone for areas its network does not reach (but Vodafone's does).
92. The three MNOs are the only significant suppliers of mobile services in New Zealand. There are some parties (such as Vocus and The Warehouse) that resell services purchased from the MNOs, but none have a significant number of customers.¹⁰⁶
93. The share of supply for pre-pay, consumer on-account and business on-account for each TSP is set out below. Spark has [], whereas 2degrees' customer base is heavily weighted towards pre-pay, and it has the smallest number of on-account customers. More recently, however, 2degrees has been increasing its on-account subscriber base.¹⁰⁷

Table 2: Share of mobile connections (October 2016)

Firm	Pre-pay	Share	Consumer on-account	Share	Business on-account	Share
Spark	[]	[]%	[]	[]%	[]	[]%
Vodafone	[]	[]%	[]	[]%	[]	[]%
2degrees	[]	[]%	[]	[]%	[]	[]%
Total	[]	100%	[]	100%	[]	100%

Notes: [].

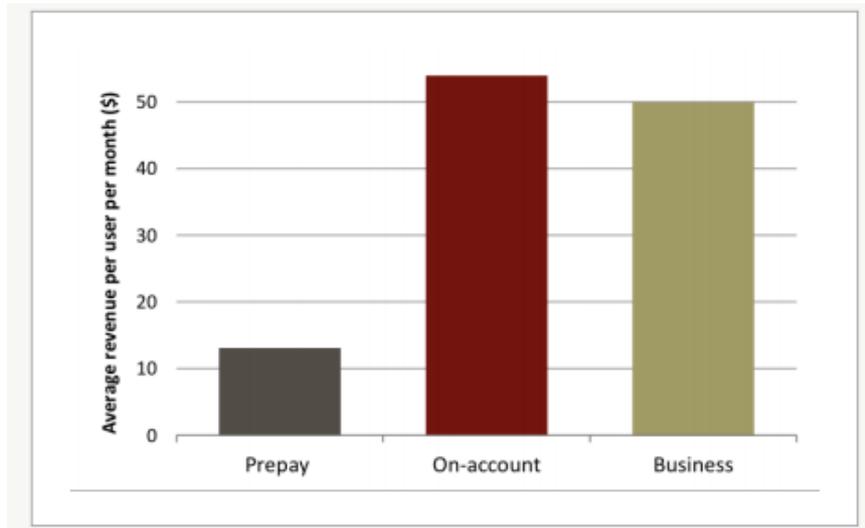
Source: Vodafone, Spark and 2degrees.

94. There is a significant difference between the value to TSPs of pre-pay and on-account customers. Consumer on-account and business on-account customers generate the highest average revenue per user (ARPU) for TSPs. As can be seen in Figure 1 below, a consumer on-account customer generates, on average, over four times as much revenue as a pre-pay customer.

¹⁰⁶ Parties that resell mobile services from MNOs are known as a Mobile Virtual Network Operators or MVNOs. The total number of MVNO subscribers was under 20,000 as at 30 June 2015: Commerce Commission "Annual Telecommunications Monitoring Report 2015" (26 May 2016) at 28.

¹⁰⁷ Commerce Commission "Annual Telecommunications Monitoring Report 2015" (26 May 2016) at 29. See also <https://www.2degreesmobile.co.nz/company/news-and-media-releases/2degrees-fy15-results-strong-growth-continues-revenue-lifts-43-1-ebitda-up-43-9-mobile-network-reaches-95-population-coverage/>.

Figure 1: ARPU by mobile segment

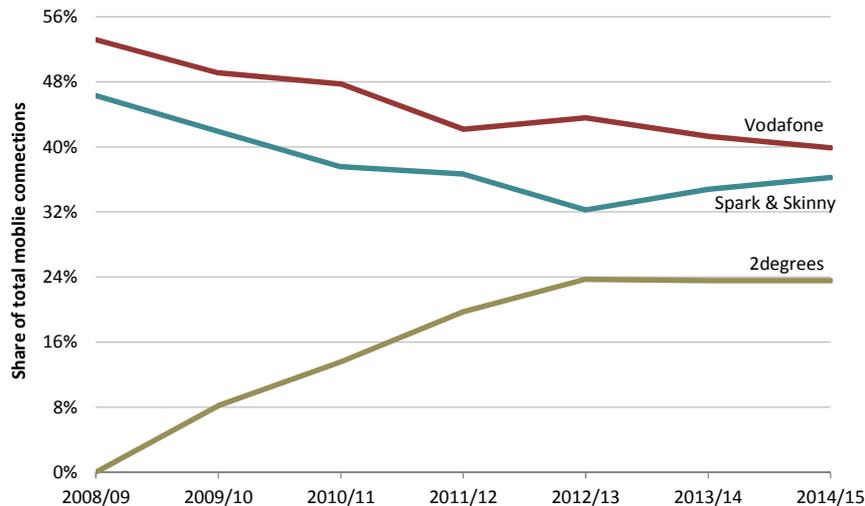


Source: Commerce Commission “Annual Telecommunications Monitoring Report 2015” (26 May 2016) at 35.

The impact of 2degrees on competition

- 95. Since its entry into the mobile services market in 2009, 2degrees has had a significant impact on competition in that market. Prior to its entry, Telecom (now Spark) and Vodafone were the only MNOs in New Zealand. As at the end of June 2009, Vodafone’s share of subscribers was estimated to be 53% and Telecom’s share 47%.¹⁰⁸
- 96. The relative market shares in the mobile services market since 2degrees’ entry are set out in Figure 2, below.

Figure 2: Mobile services market share trends



Notes: Based on total number of subscribers (including pre-pay, on-account and business).
 Source: Commerce Commission “Annual Telecommunications Monitoring Report 2015” (26 May 2016) at 29.

¹⁰⁸ Commerce Commission, “Final report on whether the mobile termination access services should become designated or specified services” (22 February 2010) at [189].

97. The Commission found that the lack of competitive pressure prior to 2degrees' entry had resulted in prices in New Zealand being high relative to other OECD countries.¹⁰⁹ In a 2008 report the Commission stated:¹¹⁰

In the downstream retail [mobile] market, the Commission considers that New Zealand's relatively high prices indicate lower competitive pressures than in other OECD countries, where there are typically at least three mobile network operators.

98. In the Commission's first annual telecommunications monitoring report published in 2010 after the entry of 2degrees, it stated:¹¹¹

In the mobile market the entry of a new network operator, 2degrees, has had an immediate impact in terms of consumer choice and competitive offerings. Although there is evidence that competition in the mobile market is increasing following the launch of 2degrees, mobile voice usage remains low by international standards.

99. In subsequent years, the Commission has observed further decreases in mobile prices, increases in mobile phone usage and an improvement in New Zealand's OECD benchmark ranking.¹¹² MBIE, in its 2015 review of the Telecommunications Act 2001 acknowledged the impact of 2degrees' entry and stated that it is important to "maintain and build on the competition gains achieved over the last decade".¹¹³

Pay TV and FTA content

100. Pay TV and FTA content is delivered to consumers using various technologies, including satellite, terrestrial broadcast, the internet and cable.
- 100.1 *Satellite.* Sky uses satellite as its main means of delivering pay TV services. Sky also retransmits some FTA channels over satellite. Sky's satellite services are encoded at source, requiring a STB to decode them as well as a satellite dish to receive them.
- 100.2 *Terrestrial broadcast over radio waves.* Terrestrial broadcasts have been digitally encoded since 2012. This form of broadcasting is used mainly by FTA broadcasters such as TVNZ, Mediaworks and Sky's Prime.
- 100.3 *Internet.* The main means of distributing TV content over the internet is OTT. OTT providers are so-called because they deliver content over the open internet¹¹⁴ without the need for a STB or involvement of any intermediary transmission (eg, satellite).

¹⁰⁹ Commerce Commission, "Draft report on whether the mobile termination access services should become designated or specified services" (30 June 2009) at [220].

¹¹⁰ Commerce Commission, "Final report of schedule 3 investigation into amending the roaming service" (10 March 2008) at [114].

¹¹¹ Commerce Commission "Annual Telecommunications Monitoring Report 2009" (23 April 2010) at 7.

¹¹² Commerce Commission "Annual Telecommunications Monitoring Report 2015" (26 May 2016) at 39.

¹¹³ MBIE discussion paper "Regulating communications for the future" (September 2015) at 44.

¹¹⁴ As opposed to delivery over closed internet network systems, such as Internet Protocol Television (IPTV), that can only be accessed via an appropriate STB. Vodafone is the only IPTV provider in New Zealand, but it has only a very small number of subscribers (approximately []).

100.4 *Cable*. Cable services are provided only by Vodafone in Christchurch, Wellington and the Kapiti Coast. Vodafone uses the cable network to retransmit Sky and also offers some limited IPTV PPV services of its own.¹¹⁵

101. Content is delivered either as a linear broadcast or on demand.

101.1 A linear broadcast is where programming is scheduled at a particular time on a particular channel. This is the traditional means to deliver programming and continues to be used by FTA broadcasters and Sky.

101.2 Traditional linear broadcasting has evolved and can now be combined with a recording capability. This technology enables viewers to 'catch up' with missed content at a later time or to effectively 'pause' a broadcast and continue watching at a later time. Sky's 'MySky' STB has this functionality.

101.3 On-demand services provide a catalogue of content made available for viewing at any time, although a number of these services offer availability for limited periods of time. Netflix, Apple TV and Lightbox are examples of on-demand services.

The relationship between different types of broadcasting

102. FTA, Sky and OTTs are all broadcasters of content, and there are overlaps in the type of content that they carry, in particular entertainment content. However, there are significant differences between them and the evidence suggests that they are more complements than substitutes. This is because of:

102.1 the nature of the broadcast (scheduled linear broadcast versus on demand);

102.2 the type of content (eg, live sport, movies, news, general entertainment);

102.3 the amount of content available (catch up service versus full back catalogues of series); and

102.4 pricing (ranging from 'free', \$10-20 per month for OTTs to over \$49 per month for Sky TV, and over \$70 per month for Sky TV including Sky Sport).

103. Netflix advised that [].¹¹⁶

FTA

104. FTA providers generate revenues principally by selling advertising. They purchase, commission or produce content programming.

105. Content is delivered via a scheduled, linear broadcast. Although they offer a limited number of 'catch-up' channels, unlike the catalogues of content that OTTs make

¹¹⁵ Given the very small size of its customer base, for the purpose of this Determination we treat Vodafone as not having a pay TV business.

¹¹⁶ Commerce Commission interview with Netflix (23 September 2016).

available on demand (discussed below), these catch-up services only offer a small number of recent episodes and are only available for a limited period.¹¹⁷

106. The main types of content that FTA providers offer are set out below.
- 106.1 News and current affairs programming. For example, TVNZ produces programming including One News and Seven Sharp, which it broadcasts on TVNZ1.¹¹⁸ MediaWorks produces NewsHub.¹¹⁹
- 106.2 General entertainment programming that the FTA broadcaster has purchased or commissioned from production companies. For example, TVNZ offers dramas, general entertainment and documentaries.¹²⁰
- 106.3 Sports content. Although in the past premium live sports content has been shown live on FTA channels, this is generally no longer the case. Although FTA providers have the rights to broadcast some events, these are sports that do not attract a sufficient audience to make them attractive to a pay TV operator.¹²¹ For example, AFL and Bundesliga games are shown on TVNZ's FTA channel, Duke.¹²²

Sky

107. As noted above, Sky's main method of broadcasting is via satellite, although it now also offers its content through various online platforms.
108. Sky produces news programming which is broadcast over a dedicated 24 hour news channel (Sky News New Zealand).¹²³ The channel also includes international programming from international affiliates Sky News Australia and America's CBS and ABC networks.
109. Sky produces and broadcasts coverage of sporting events. Sky has the rights to premium live sports content including rugby, NRL, cricket and netball. We discuss this in detail further below.
110. Sky also offers a range of other types of programming including: entertainment, leisure and lifestyle, documentaries, children's channels and movies.¹²⁴ Sky has

¹¹⁷ These 'catch-up' channels commonly show content an hour later than when it was first broadcast. Some FTA providers also offer on-demand content (eg, TVNZ OnDemand).

¹¹⁸ <http://tvnz.co.nz/tvz-corporate-comms/tvz-4880728>.

¹¹⁹ <http://www.mediaworks.co.nz/ourbrands.aspx>.

¹²⁰ <http://tvnz.co.nz/tvz-corporate-comms/our-channels-4902645>.

¹²¹ Submission from TVNZ to the Commerce Commission (12 August 2016) at [5.7].

¹²² Sommet Sports previously had the rights to broadcast live AFL and Bundesliga games and MotoGP events. It launched in early 2013 but ceased broadcasting in December 2014.

¹²³ <https://www.skyadvertising.tv/sky-news>.

¹²⁴ Grant Samuel "Independent Adviser's Report and Appraisal Report in relation to the Proposed Acquisition of Vodafone New Zealand Limited" (June 2016) at 29.

contracts with various content owners to broadcast their content in New Zealand, for example, other news channels such as CNN and BBC.¹²⁵

OTTs

111. OTT providers are relatively new to the New Zealand market, and differ from traditional forms of pay TV in a number of ways. Most OTT providers (such as Netflix, Lightbox and Sky's NEON) charge a monthly subscription for unlimited access to a library of content. This is known as SVOD. Some OTTs (such as Apple TV and, in part, Quickflix) charge one-off fees to access particular content. This is known as transactional video on demand (TVOD) or PPV.

111.1 OTT services require an internet connection, but do not require the installation of specialist equipment such as satellite dish. This allows OTTs to avoid a major cost that traditional forms of pay TV have faced. It also makes it easier for customers to subscribe and unsubscribe.¹²⁶

111.2 Rather than scheduled programming, OTTs typically offer access to a large library of on-demand content, such as movies, documentaries and TV series.

111.3 OTT content is, by comparison with satellite content, relatively inexpensive for consumers to acquire. For example, Netflix currently charges between \$11.49 and \$18.49 per month and Lightbox charges \$12.99 per month (or free with some Spark plans). This compares to \$49.91 per month for Sky Basic.

112. OTTs primarily offer entertainment content. Examples of OTTs are set out below.

112.1 Netflix has sought to build a library of exclusive content including original series (that it produces in-house), documentaries and feature films.¹²⁷ Netflix series include drama (such as House of Cards), real life crime (such as Making a Murderer) and thrillers (such as Bloodline).

112.2 Lightbox offers TV shows which it describes as including "globally trending shows, cult classics, New Zealand favourites, and a huge range of kids' shows".¹²⁸

112.3 Quickflix focuses on providing movies and TV shows on a PPV basis.¹²⁹

112.4 Amazon Prime offers TV shows, movies and original series.¹³⁰

¹²⁵ Ibid at 30-31.

¹²⁶ Although, as discussed at [182-185], below, customers that acquire to services in bundles are 'stickier' (ie, they exhibit lower rates of switching).

¹²⁷ <https://ir.netflix.com/faq.cfm>.

¹²⁸ <https://www.lightbox.co.nz/about-lightbox>.

¹²⁹ <https://www.quickflix.co.nz/About>.

¹³⁰ <https://www.primevideo.com/>.

113. [

] ¹³¹

114. There are few examples of OTTs that offer (or have offered) live sport in New Zealand.

114.1 beIN currently offers English Premier League and some European football directly to subscribers.

114.2 Spark previously had a sport offering (in conjunction with Coliseum Sports) called “Lightbox Sport”. Lightbox Sport offered English Premier League, international golf and some European Rugby. Spark advised that the service was closed in 2016 because it did not achieve sufficient subscription levels to be sustainable.¹³²

The importance of premium live sports content

115. Live sports content in New Zealand can be divided into two broad categories: ‘premium’ and ‘non-premium’. Premium live sports content includes rugby (including Super Rugby and All Blacks games), NRL, cricket and netball, and events such as the Olympic Games and the Cricket and Rugby World Cups.

116. As noted above, Sky holds the rights to broadcast this content. Its premium live sports broadcasts run on Sky Sport 1-4 (that subscribers access by paying an additional fee on top of their Sky Basic package) and on FanPass.¹³³

117. In the past, Sky has also shown live sport on additional, short term ‘pop up’ channels (eg, during the Rio Summer Olympic Games). These pop up channels were not available on FanPass, however, and so were only available to those Sky subscribers willing to commit to longer term subscriptions.

118. The importance of ‘premium’ sport has been identified by the Applicants. For example: Grant Samuel’s independent Adviser’s Report to Sky stated that:¹³⁴

The availability of exclusive premium content is likely to be a further driver of differences in the impact of OTT services across markets. In particular, the availability of exclusive sports programming may be a powerful defensive opportunity for pay television operators. In some markets (such as Australia) government mandated access to sports programming via free-to-air television (“anti-siphoning legislation”) limits the ability of pay television operators to secure exclusive rights over the most attractive programming. However, in other markets, such as the United Kingdom for soccer and New Zealand for rugby, exclusive sporting rights fundamentally underpin the content offerings of the incumbent pay television operators and are a driver of subscriber loyalty.

¹³¹ We discuss the likelihood of the merged entity retaining these rights, including barriers to rivals winning them, at [273-282], below.

¹³² Submission from Spark to the Commerce Commission (12 August 2016) at [33-34].

¹³³ It also shows live overseas rugby on the Rugby Channel.

¹³⁴ Grant Samuel “Independent Adviser’s Report and Appraisal Report in relation to the Proposed Acquisition of Vodafone New Zealand Limited” (June 2016) at 27.

119. The same report later stated:¹³⁵

there are no anti siphoning laws in New Zealand and Sky TV has a strong lock on the key sporting rights that are significant drivers of customer attraction and retention.

120. The importance of ‘premium’ sport is also recognised in internal documents of the Applicants. For example:

120.1 []¹³⁶

120.2 []¹³⁷ and];

120.3 []¹³⁸.

121. Similarly, third party submissions that we received in relation to this transaction highlighted the premium nature of these broadcast rights. For example, TUANZ listed the sports important to New Zealanders as rugby, rugby league, netball and cricket.¹³⁹

122. When analysing the merger, we did not need to reach a firm conclusion about which sports rights are premium and which are not. It was sufficient for our purposes to recognise that Sky holds the rights to the majority of popular live sports content in New Zealand, for which there is no close substitute. It broadcasts this content on Sky Sport and FanPass,¹⁴⁰ and would be likely to retain those rights in the future.

123. In this regard, Sky holds the exclusive New Zealand broadcast rights for the above mentioned sports until at least 2020^{141 142} and we consider it likely that it will

¹³⁵ Ibid at 56.

¹³⁶ [] provided under the cover of a letter from Bell Gully (on behalf of Vodafone) to the Commerce Commission (29 July 2016) at 31.

¹³⁷ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (5 August 2016) at 72.

¹³⁸ [] provided under the cover of a letter from Bell Gully (on behalf of Vodafone) to the Commerce Commission (5 August 2016) at 43.

¹³⁹ Submission from TUANZ to the Commerce Commission (12 August 2016) at [29].

¹⁴⁰ Pop up sport channels have not in the past been available to FanPass subscribers. See [117], above.

¹⁴¹ Sky has the exclusive New Zealand rights to broadcast cricket until 2020 (New Zealand Cricket), rugby and netball until 2021 (NZRU and Netball New Zealand, respectively), and rugby league until 2022 (NRL).:Grant Samuel “Independent Adviser’s Report and Appraisal Report in relation to the Proposed Acquisition of Vodafone New Zealand Limited” (June 2016) at 56.

¹⁴² [] provided under the cover of an e-mail from Buddle Findlay (on behalf of Sky) to the Commerce Commission (13 July 2016).

continue to hold these rights past the date on which the current rights contracts end. We discuss this in further detail in the ‘competition analysis’ section, below.

Regulatory environment

124. New Zealand has no laws or regulations mandating access to content, with the Commerce Act 1986 acting as the “main economic regulatory backstop in the broadcasting sector”.¹⁴³
125. For example, unlike in some other jurisdictions, there are no specific regulations ensuring that FTA broadcasters have an opportunity to bid for the rights to broadcast important or culturally significant events such as premium live sports (so-called ‘anti-siphoning’ rules). Nor does New Zealand have laws that mandate that certain sports content be broadcast live on a FTA channel.¹⁴⁴
126. Similarly, there are no regulations requiring broadcasting companies to provide other broadcasters access to their content on minimum terms.¹⁴⁵ In other jurisdictions, such as the UK, there have been requirements that premium content such as live sport be made available subject to ‘fair access’ rules.¹⁴⁶

Industry trends/context of the transaction

127. The proposed merger is taking place at a time of significant change in the telecommunications and broadcasting sectors, and further changes are expected in the medium to long term.
- 127.1 There have been consistent improvements in the quality and availability of broadband and mobile networks. The continued roll-out of the new high speed UFB network means that approximately 1.1 million premises will be able to switch to UFB in the next two years. This roll-out is expected to create increased opportunities for TSPs to entice customers to switch TSPs.
- 127.2 Similarly, the quality of the mobile network has improved with each new generation of technology. 5G technology, when it arrives, is likely to result in further improved mobile services.

¹⁴³ MBIE discussion paper “Regulating communications for the future” (September 2015) at 10.

¹⁴⁴ See, for example, Australia’s anti-siphoning scheme which prevents pay television broadcasters from acquiring the rights listed in the Broadcasting Services (Events) Notice (No. 1) 2010 before FTA broadcasters have had the opportunity to bid for them. In the UK, certain specified events such as the Olympic Games must be shown on FTA channels. See Ofcom “Code on Sports and Other Listed and Designated Events” (30 April 2010).

¹⁴⁵ Although an outright or constructive refusal to provide access to certain content may breach s 36 of the Commerce Act 1986 in some circumstances.

¹⁴⁶ Ofcom’s ‘wholesale must-offer’ (WMO) obligation required Sky UK to offer its Sky Sports channels 1 and 2 to other pay TV providers on a wholesale basis. Ofcom lifted this obligation in 2015 because Sky UK was supplying access to these channels on commercial terms: Ofcom “Ofcom removes ‘wholesale must-offer’ for Sky Sports 1 and 2” (November 2015). BT has successfully won the rights to broadcast some English Premier League games. See, for example: <https://www.theguardian.com/football/2015/feb/10/premier-league-tv-rights-sky-bt>.

- 127.3 OTTs have entered the market and have attracted viewers, although they have not competed strongly to show premium live sports content, and it is unclear how successful some of them will be over the long term.
- 127.4 The entry of OTTs has contributed to an increase in the amount of content that is viewed over the internet, and the corresponding surge in data consumption. For example, new OTT entrants, such as Netflix, have entered and offer a range of entertainment content (eg movies, TV series and documentaries). They do not compete against Sky's premium live sports content, however.
- 127.5 Telecommunications and broadcasting markets are 'converging', or becoming more closely linked. In particular, TV is becoming more closely associated with the broadband and mobile services markets, as consumers increasingly view video content over broadband and mobile networks. The technologies used to deliver broadband and mobile are also converging, with the infrastructure used to deliver these services becoming more common to both.¹⁴⁷
- 127.6 There has been an increase in the uptake of bundles offered by a single supplier containing both telecommunications and content products.

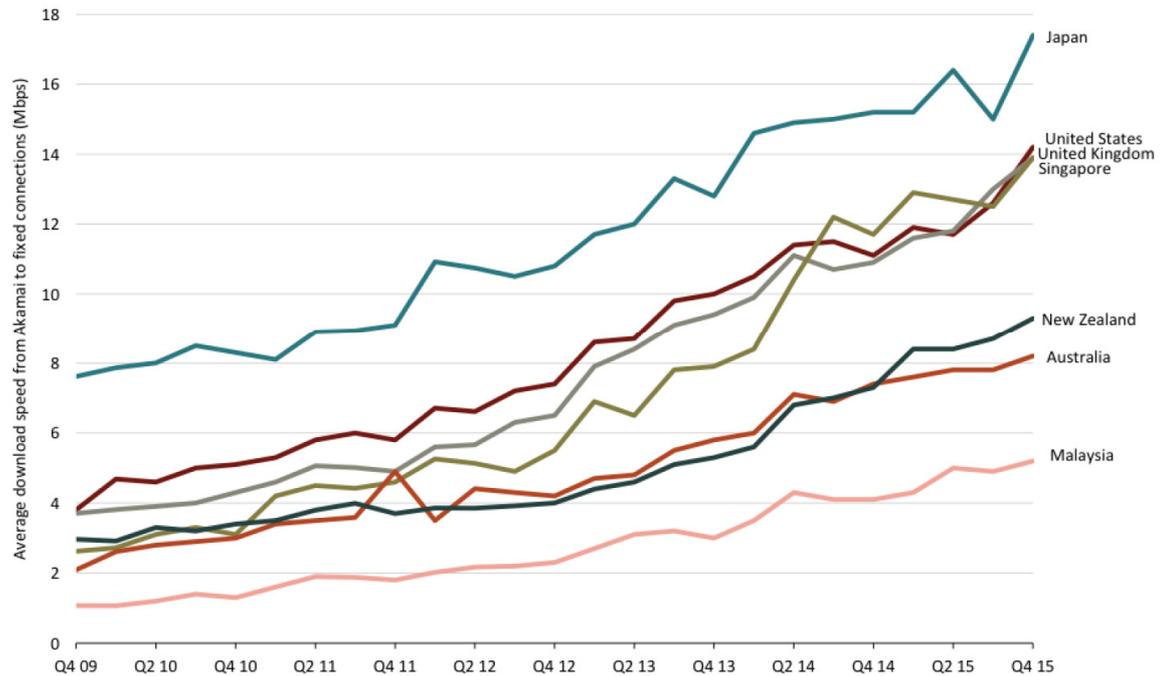
128. We explain these changes in more detail below.

Improvements in broadband quality and availability

129. There have been consistent improvements in the quality and availability of broadband, globally and in New Zealand. Figure 3, below, shows the average broadband speed in different countries between 2009 and 2015. Speed is a key indicator of broadband quality.

¹⁴⁷ For example, the Evolved Packet Cores – or 'intelligent' parts – of broadband and mobile networks are increasingly using the same software and technology.

Figure 3: Average download speeds by country



Commerce Commission "Annual Telecommunications Monitoring Report 2015" (26 May 2016) at 26 (based on Akamai data).

130. This trend is expected to accelerate, as an increasing number of consumers take-up UFB. As discussed above, the Government's UFB Initiative is rolling out faster broadband to New Zealanders, and it is expected that 75% of New Zealanders will have access to peak download speeds of at least 100/50Mbps by 2019 (UFB phase 1) (compared to peak ADSL download speeds of 30Mbps today)¹⁴⁸ and 85% will have access by 2024 (UFB phase 2).
131. The roll-out of UFB will further improve the quality and reliability of streaming content. For example, content can be streamed over multiple devices without affecting internet performance. This is likely to lead to increased convergence between broadband and pay TV, and we discuss this, and its significance for consumer preferences, in more detail below.
132. This switching from copper to UFB provides an opportunity for TSPs to entice customers to switch not only broadband delivery platforms, but also providers. By 2019, UFB will be available to an additional 400,000 premises, meaning that over 1.1 million end users are or will be 'in play' and more receptive to switching broadband providers as they switch to the new UFB platform, by this time.¹⁴⁹

¹⁴⁸ <http://www.crownfibre.govt.nz/getting-ufb/rollout-timetable/>.

¹⁴⁹ Source of figures: MBIE "Broadband deployment update" (December 2016). It is possible that consumers will be forced to switch if Chorus chooses to cease operating the copper network in their area. See n100, above. This could further hasten the switch from copper to fibre.

133. Switching from copper to fibre involves the installation of a fibre connection by LFCs (such as Chorus), as well as the purchase (or lease) of a fibre-compatible modem/router. It also involves the customer entering into a new contract with a TSP. Therefore, switching providers at the same time as switching platforms is likely to incur limited additional time and effort compared to remaining with the same provider and simply switching platforms.
134. There is therefore the possibility of significant churn of customers between TSPs in the next few years.¹⁵⁰ Indeed, a Vodafone []¹⁵¹
135. Market share data we obtained indicated that there are differences between the market shares for total broadband connections and for initial fibre connections, which is consistent with consumers switching TSPs as they switch to fibre. It also indicates that historic market shares may not be a good indicator of how competition is likely to play out in the future as UFB continues to be rolled out.

Table 3: Share of broadband and UFB connections

TSP	Broadband connections	Broadband share	UFB connections	UFB share
Spark	[]	[]%	[]	[]%
Vodafone	[]	[]%	[]	[]%
Vocus	[]	[]%	[]	[]%
Trustpower	[]	[]%	[]	[]%
2degrees	[]	[]%	[]	[]%
Others	[]	[]%	[]	[]%
Total	[]	100%	[]	100%

Source: Broadband connections totals from Table 1. Total fibre connections from submission from Vodafone to the Commerce Commission (11 November 2016) at 24.

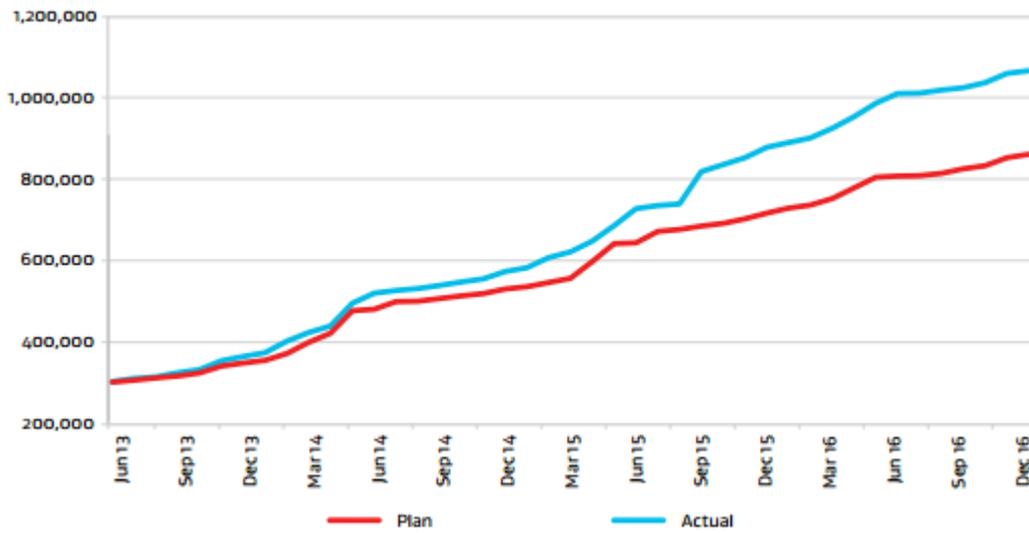
136. As at September 2016, 1,062,433 premises had access to UFB, and 327,864 users had connected.¹⁵² Figure 4, below, shows that the roll-out of UFB is proceeding more quickly than first planned.

¹⁵⁰ []

¹⁵¹ [] provided under the cover of a letter from Bell Gully (on behalf of Vodafone) to the Commerce Commission (19 August 2016) at 3 and 7.

¹⁵² MBIE “Broadband deployment update” (December 2016).

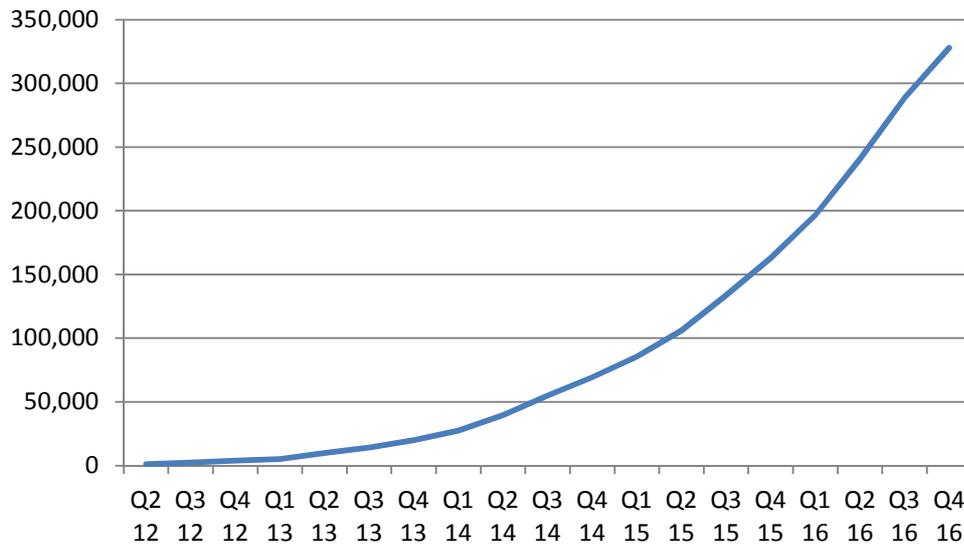
Figure 4: Households and businesses able to connect to fibre (June 2013 – December 2016)



Source: MBIE “Broadband deployment update” (December 2016).

137. Figure 5, below, shows the number of connected customers since the UFB Initiative commenced in 2012.¹⁵³

Figure 5: Total premises connected to UFB (July 2012 – December 2016)



Data source: MBIE, Broadband Deployment Quarterly Updates.

Notes: Q212 connection figures are the total number of connections between July 2011 and June 2012.

Improved quality of the mobile network

138. The quality of the mobile network has also improved with each new generation of technology.

¹⁵³ The source data for Figure 5 is accessible at <http://www.mbie.govt.nz/info-services/sectors-industries/technology-communications/fast-broadband/deployment-progress>.

139. The roll-out of 4G technology was a significant improvement on 3G, allowing much higher download speeds and facilitating increased content consumption over mobile networks, although consumption is still likely to be limited by data pricing.
140. The introduction of 5G technology is expected to significantly improve the speed at which data is transferred across mobile networks.¹⁵⁴ While 5G standards have not yet been formalised, the criteria for 5G includes the ability to provide connection speeds of 1-10Gbps.¹⁵⁵
141. 5G is likely to make it more attractive for users to stream or download video content over the mobile network, as well as over a FWA network.
142. The exact date of 5G deployment is uncertain; however we consider that there is good evidence suggesting that it will be rolled-out in the next five years in New Zealand.¹⁵⁶
- 142.1 The standards setters for 5G – the International Telecommunications Union and 3GPP – have a target date for 5G release of 2020.¹⁵⁷
- 142.2 Mobile phone manufacturers Huawei and Nokia have publicly stated that they expect 5G technology to be rolled out before 2020.¹⁵⁸
- 142.3 Vodafone and Nokia conducted live public tests of 5G technology in Australia in October 2016.¹⁵⁹
- 142.4 Vodafone CEO Russell Stanners has previously stated that he expects to see 5G “around 2020”.¹⁶⁰
143. Data costs present one barrier for consumers streaming or downloading content using the mobile network. However, according to Commission data, the costs of mobile plans with high data caps have been trending downward.

¹⁵⁴ <http://www.newshub.co.nz/technology/5g-technology-10-times-faster-than-current-fibre-2015030716>.

¹⁵⁵ <https://www.gsmaintelligence.com/research/?file=141208-5g.pdf&download>.

¹⁵⁶ See, for example: http://www.nzherald.co.nz/business/news/article.cfm?c_id=3&objectid=11743299.

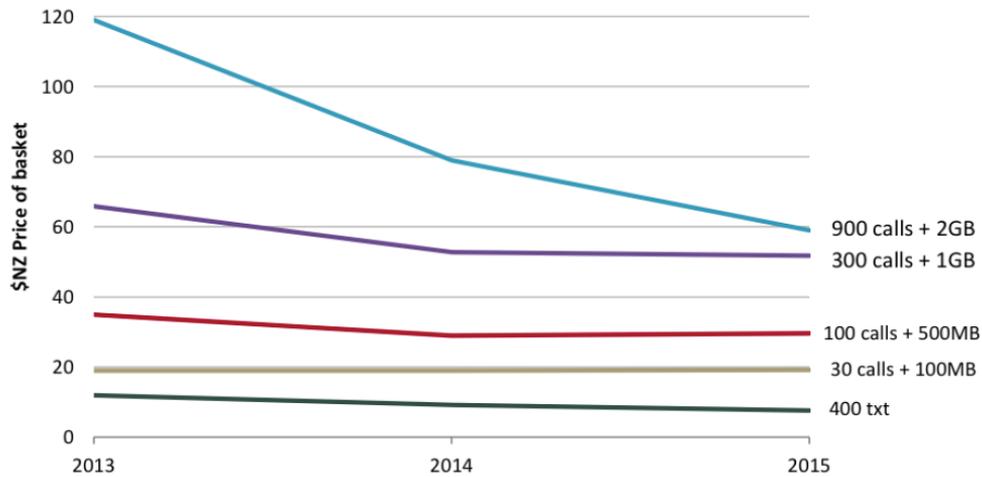
¹⁵⁷ <http://www.itu.int/en/ITU-R/study-groups/rsg5/rwp5d/imt-2020/Pages/default.aspx> and http://www.3gpp.org/news-events/3gpp-news/1674-timeline_5g.

¹⁵⁸ <http://www.stuff.co.nz/technology/digital-living/77125276/5g-could-begin-as-early-as-2017> and <http://www.zdnet.com/article/huawei-plans-5g-network-launch-by-2020-100-times-faster-than-4g/>.

¹⁵⁹ <http://www.vodafone.com.au/media/vodafone-nokia-conduct-australias-first-live-public-5g-trial/>.

¹⁶⁰ http://www.reseller.co.nz/article/548074/expect_5g_nz_by_2020_vodafone/.

Figure 6: Trend in \$NZ price of mobile basket including data (2013 – 2015)



Note: 900 calls + 2GB is used as a proxy for unlimited calls.

Source: Commerce Commission "Annual Telecommunications Monitoring Report 2015" (26 May 2016) at 39 (based on Teligen data).

144. As mobile technology improves and costs continue to fall, consumers are likely to view more content over mobile. As with broadband, it is likely that these improvements will increase convergence with pay TV, and we discuss this in more detail below.

Growth of internet-based broadcasting (OTT)

145. Improvements in broadband quality and speed have led to the growth of internet-based video and the rise of OTT providers. As discussed at [111-114], above, these providers largely screen entertainment content.
146. The OTTs have grown rapidly.
- 146.1 Netflix is the largest OTT provider. It launched its OTT business in 2007, and it now has over 93 million subscribers in over 190 countries.¹⁶¹ Netflix entered New Zealand in 2015 and had gained 264,000 subscribers by 2016.¹⁶²
- 146.2 Sky launched NEON in 2015 and had gained [] subscribers by October 2016.¹⁶³
- 146.3 Lightbox (Spark) launched in 2014 and had gained [] subscribers as at August 2016,¹⁶⁴ although [].¹⁶⁵

¹⁶¹ <https://ir.netflix.com/>.

¹⁶² http://www.nzherald.co.nz/entertainment/news/article.cfm?c_id=1501119&objectid=11651395.

¹⁶³ Letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (11 November 2016) at 7.

¹⁶⁴ Submission from Spark to the Commerce Commission (12 August 2016), Appendix 1 at [34].

¹⁶⁵ Commerce Commission interview with Spark (3 August 2016).

- 146.4 Amazon Prime, Quickflix, YouTube Red and beIN launched in New Zealand over the last few years.
147. The growth of OTTs appears to have been a disruptive force for the traditional forms of broadcasting. FTA broadcasters and Sky have lost audience share, with some Sky TV subscribers cancelling their subscriptions. For example, Sky [].¹⁶⁶ At the same time, OTTs have increased competition for content which has pushed up the cost of acquiring this content.¹⁶⁷
148. Satellite and FTA broadcasters have responded to the demand for content over the internet by developing their own platforms. As noted earlier, Sky has developed SkyGo, FanPass and NEON. FTA channels offer VOD for viewers to catch up on episodes that have already screened on terrestrial channels.
149. As the business models of traditional broadcasters and OTTs continue to change, they could potentially be both substitutes and complements to one another in that demand for one increases demand for the other. For example, Netflix told us that [].¹⁶⁸ As OTTs are relatively cheap and have different shows from Sky and other OTTs (and do not have premium live sports rights), customers may choose to purchase both Sky TV and OTT content.
150. As noted above, although some OTTs have been successful at winning some live sports rights (eg, beIN winning the EPL), many of these forays into live sports broadcasting have not been successful and it is unclear whether OTTs will broadcast premium live sport in the future.
151. Indeed, Netflix considers that [],¹⁶⁹ [].
152. Finally, there are indications that many OTT service providers are not profitable when operated on a standalone basis. It is possible that some of the OTT services available today will not survive in the longer term.

¹⁶⁶

[

]: Sky Application at Annexure D and letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (11 November 2016) at 7. It is also possible that some of these subscribers moved onto a less expensive Sky TV package. See n46, above.

¹⁶⁷ Grant Samuel "Independent Adviser's Report and Appraisal Report in relation to the Proposed Acquisition of Vodafone New Zealand Limited" (June 2016) at 27.

¹⁶⁸ Commerce Commission interview with Netflix (23 September 2016).

¹⁶⁹ Ibid.

152.1 [170]

152.2 Quickflix went into administration before being rescued in 2016.¹⁷¹

152.3 EzyFlix ceased operating in August 2015 in New Zealand less than two years after it commenced operations.¹⁷²

152.4 A number of OTT service providers in Australia have faced challenges building market share. EzyFlix exited the Australian market in 2015¹⁷³ and Presto announced in October 2016 that it would cease operations in January 2017, after initially launching in 2014.¹⁷⁴

Increased consumption of broadband and mobile data

153. Commensurate with improvements to broadband and mobile networks and the entry of OTT providers offering a wider range of content readily accessible via those networks, the last five years has seen a sharp increase in the consumption of broadband and mobile data.¹⁷⁵
154. Figure 7, below, shows broadband data throughput per user since 2011. The figure shows strong growth, which Chorus has identified is due to the rise in SVOD services.¹⁷⁶ There is a noticeable jump in 2015 (indicated with an arrow) which coincides with the entry of Netflix into the market.

¹⁷⁰ []

¹⁷¹ <https://www.nbr.co.nz/article/quickflix-new-owner-has-turnaround-plan-ck-p-197782>.

¹⁷² <http://www.smh.com.au/digital-life/digital-life-news/ezyflix-switches-off-the-popcorn-popper-and-closes-the-curtains-20150827-gj8tsx.html>.

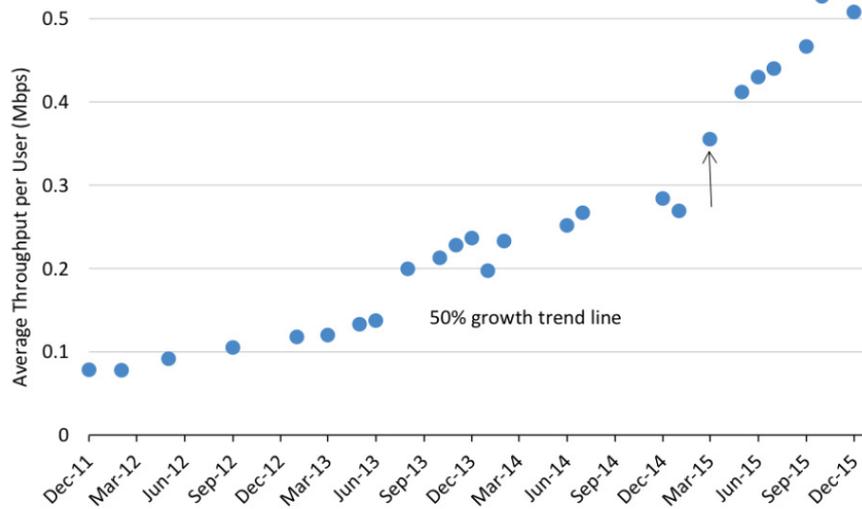
¹⁷³ Ibid.

¹⁷⁴ <http://www.smh.com.au/business/media-and-marketing/presto-to-shut-down-in-january-after-seven-sells-to-foxtel-20161003-gru8q3.html>. Presto was a joint venture between Foxtel and Seven West Media.

¹⁷⁵ Commerce Commission “Annual Telecommunications Monitoring Report 2015” (26 May 2016) at 22 and 33.

¹⁷⁶ <https://www.nbr.co.nz/article/netflix-effect-chorus-tracks-huge-increase-data-use-ck-186257>.

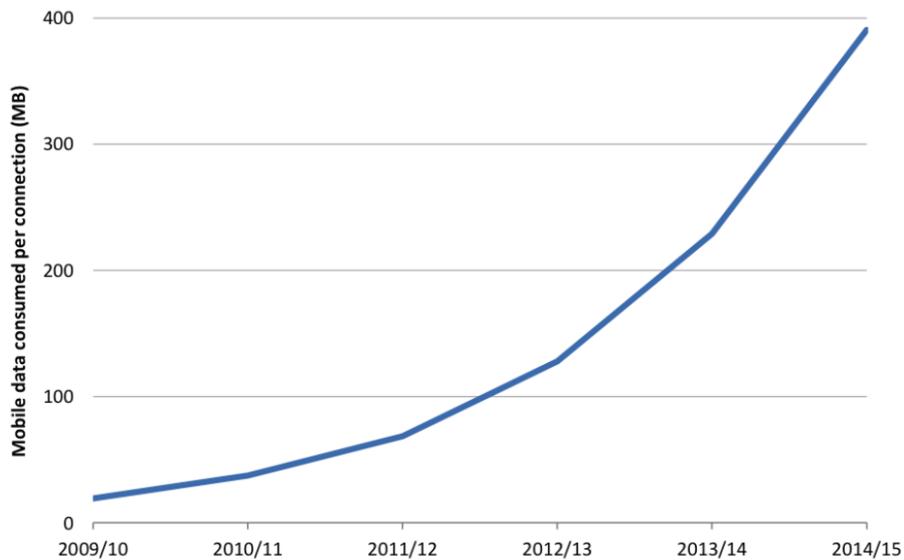
Figure 7: Broadband data throughput per user (2011-2015)



Source: Commerce Commission “Annual Telecommunications Monitoring Report 2015” (26 May 2016) at 23 (based on Chorus data).

155. Similarly, Figure 8, below, shows mobile data consumption per connection has grown exponentially since 2009.

Figure 8: Mobile data consumption per connection (2009-2015)



Source: Commerce Commission “Annual Telecommunications Monitoring Report 2015” (26 May 2016) at 33.

156. The Applicants were unable to provide a split between broadband and mobile data usage for entertainment and sport. The best data that we obtained showed

(separately) the combined OTT broadband traffic for SkyGo and NEON¹⁷⁷, and the combined mobile data traffic for SkyGo, NEON and FanPass.¹⁷⁸

157. []

158. We did, however, obtain subscriber numbers for FanPass. Figure 9, below, sets out the number of FanPass subscribers at the end of each month from soon after the service was introduced in January 2015, until October 2016.

Figure 9: FanPass subscriber numbers (February 2015 – October 2016)

[]

Source: Sky Application at Annexure D and letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (11 November 2016) at 7.

159. []

] ¹⁷⁹

160. The Applicants appeared to recognise the increasing trend of consumers watching content over broadband and mobile networks away from traditional means of broadcast.¹⁸⁰ As set out above, part of their rationales for the merger was as a response to this trend.

160.1 Vodafone advised us that UFB will make it easier to deliver content OTT and that [].¹⁸¹

160.2 Sky CEO, John Fellet, stated in February 2016 that:¹⁸²

Like most traditional pay-television companies, we are losing traditional satellite customers, but gaining in our online products like Neon and Fan Pass.

161. Third parties suggested that the rollout of UFB and the increased speed of mobile networks would lead to an increase in consumption of content over a greater range of devices.¹⁸³

¹⁷⁷ Between January 2016 and September 2016.

¹⁷⁸ Between December 2015 and October 2016.

¹⁷⁹ This data is based on subscriber numbers as at the end of each month, not the total number of active subscribers within each month. FanPass is purchased on a relatively short term basis; it is available on a 24 hour, weekly and monthly bases. The data may therefore underestimate subscriber activity. On the other hand, it may include customers that previously used SkyGo to watch Sky Sport, and so in this respect could over-state the trend towards watching live sport OTT.

¹⁸⁰ See, for example, the Applications at [4.4].

¹⁸¹ Commerce Commission interview with Vodafone (7 October 2016).

¹⁸² <https://www.nbr.co.nz/article/sky-tv-first-half-profit-falls-58-competition-drives-content-costs-b-185435>.

¹⁸³ Report from Plum (on behalf of 2degrees and TVNZ) to the Commerce Commission (12 August 2016) at 17 and submission from TUANZ to the Commerce Commission (12 August 2016) at [27].

162. Finally, there is evidence that watching sport, including live sport, over the internet is growing in popularity overseas.

162.1 Australian TSP Optus reportedly recorded its best sales figures in six years between July and December 2016, which has been attributed to its ownership of the rights to broadcast live EPL games.¹⁸⁴

162.2 A January 2016 OOYALA report found that in the UK and Ireland 45% of sports viewing occurs on smartphones and tablets.¹⁸⁵

162.3 A December 2016 OOYALA report found that viewing of sports-related content on mobile devices in Ireland had increased to 59%. It was over 54% in Europe, 52% in the United States and 49% worldwide. Year on year growth in Europe was over 38% in Europe and over 33% in the US.¹⁸⁶

162.4 Nielsen, in a 2015 report about marketing to New Zealand sports fans, noted that:¹⁸⁷

Options to ‘watch the game’ have never been greater and sports fans have higher incidence of usage and ownership of devices of the general population. Seven out of ten sports fans use a smartphone and one-in-three own a tablet.

As the creation and distribution of mobile-first sport video content grows, publishers are developing more convenient and streamlined options for mobile sport video viewing. Live streaming and short-form content designed for mobile consumption are all trends that are gaining momentum in the U.S. and are poised to emerge locally.

Convergence of telecommunications services and pay TV

163. The development of telecommunications and pay TV technologies over time has led to a convergence of those services, which is expected to continue in the future.

164. “Technological convergence” refers to the blurring of boundaries between once separate industries, due to the ability to provide a range of services over a single network, and the ability of different networks to carry similar kinds of services (see illustration below).¹⁸⁸

165. For example, in the past, telephones were used to make phone calls, computers were used to access the internet, and TVs were used to view content. All this can now be done using a smartphone, and content can be delivered using the same network as broadband. Even voice services can be offered using the broadband network (known as “voice over Internet Protocol” (VoIP)).

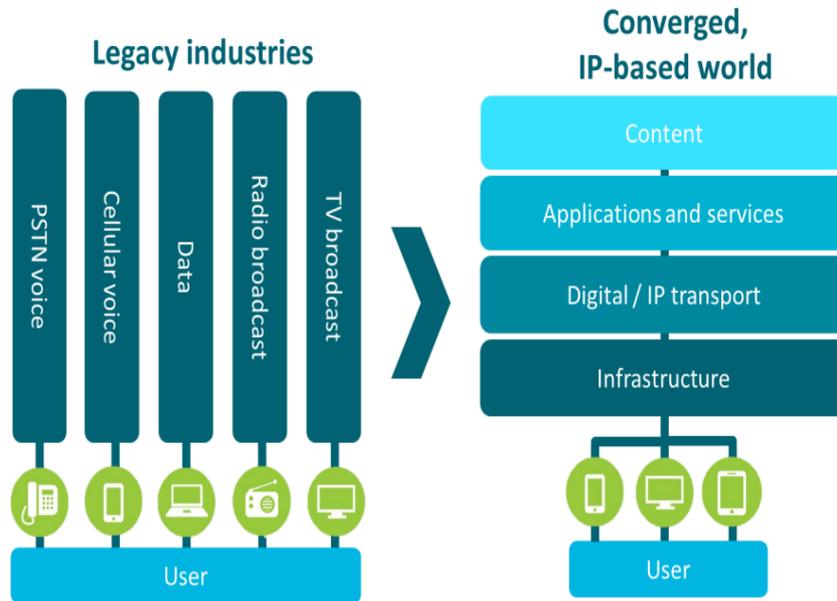
¹⁸⁴ <http://theworldgame.sbs.com.au/article/2017/02/20/optus-surge-back-premier-league-rights>. Optus has the broadcast rights for EPL in Australia, and shows all games live. FTA broadcaster SBS shows one game per week. Optus’ coverage is only available to Optus customers.

¹⁸⁵ OOYALA “State of the Broadcast Industry 2016 – OTT Moves to Centre Stage” (6 January 2016) at 8.

¹⁸⁶ OOYALA “Global Video Index Q3 2016” (6 December 2016) at 24.

¹⁸⁷ Nielsen “The Rules of Marketers Engaging with New Zealand Sports Fans” (5 April 2016).

¹⁸⁸ MBIE “Regulating communications for the future: Review of the Telecommunications Act 2001” (September 2015) at 12.

Figure 10: Changes resulting from convergence

Source: MBIE "Regulating communications for the future: Review of the Telecommunications Act 2001" (September 2015) at 12.

166. As technologies converge, TSPs will increasingly be able to provide broadband and mobile services using the same infrastructure. This is likely to drive further bundling of broadband and mobile services, and may also increase customer stickiness as broadband and mobile services become more interconnected and consumers associate them as part of the same purchasing decision, preferring to obtain them from a single supplier.
167. In addition, there has been a trend towards higher quality, but lower cost, devices on which to view content. For example:
- 167.1 'smart' TVs that connect to the internet (and mobile devices via wifi) to allow the viewing of content without the need for a STB; and
- 167.2 an increased range of mobile devices of different sizes with higher quality display screens.
168. This tends to promote the viewing of content over the internet and on mobile devices and tablets.
169. Nielsen's 2016 Multi-Screen Report¹⁸⁹ notes that 26% of viewers watch TV content on a device other than their TV in an average week. The most popular devices are desktops/laptops (39%), smartphones (27%) and tablets (18%). Nielsen reported that mobile phones and smart TVs had the biggest year-on-year growth.

¹⁸⁹ Available online at: <http://www.nielsen.com/nz/en/insights/reports/2016/viewers-choice-in-home-tv-tops-new-zealand-screen-habits.html>.

170. As services become more converged, consumers are likely to start associating them as part of the same purchasing decision – the content and the method of delivery become more closely linked in the minds of consumers. Converging technologies also mean that it is increasingly cost-efficient for firms to offer all those products to customers at the same time and to offer discounts on bundles of services compared with the price of those products on a standalone basis.
171. Although OTT services are already available to consumers, UFB (and in particular the multicast service) further enhances the delivery qualities and reliability of content over the internet. 5G may also lead to a strong increase in viewing content over mobile networks as TSPs are able to carry more data.
- 171.1 As discussed above, UFB has download speeds that are significantly faster than ADSL broadband, which greatly increases the quality of streamed content, and allows more content to be streamed simultaneously. The multicast service allows a TSP to broadcast a media stream to multiple consumers simultaneously.
- 171.2 The introduction of 5G could also result in a broader consumption of video content on mobile devices by allowing TSPs to offer higher data caps, giving customers greater flexibility to view content over mobile networks rather than over broadband.
172. The Applicants’ internal documents recognise that telecommunications markets are converging.
- 172.1 As noted above,
[]¹⁹⁰
- 172.2 []¹⁹¹
- 172.3 []¹⁹²

Competition between bundles containing telecommunications products

173. A feature of telecommunications markets in New Zealand and overseas has been the emergence of TSPs offering bundles of services (eg, broadband and voice) and bundles of telecommunications services with other products or services (eg, broadband and pay TV) where customers are offered an inducement to purchase

¹⁹⁰ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (29 July 2016) at 1.

¹⁹¹ [] provided under the cover of a letter from Bell Gully (on behalf of Vodafone) to the Commerce Commission (29 July 2016) at 5.

¹⁹² [] provided under the cover of a letter from Bell Gully (on behalf of Vodafone) to the Commerce Commission (29 July 2016) at 4.

two or more services at once (eg, a discount on the total price of purchasing broadband and pay TV).

174. Bundling is akin to a volume discount, but where volume is based on aggregate sales across products. Instead of offering a discount to buy two of the same product rather than one, the customer receives a better price to buy the product and another product together.¹⁹³
175. Even if consumers do not receive a discount for purchasing multiple services from one provider, they may still prefer to get multiple services from the same provider to avoid unbundling costs (eg, avoiding multiple bills and problems associated with dealing with two customer service centres), especially where products need to work together, as is increasingly the case with broadband and mobile services and pay TV.
176. Common strategies include offering a consumer or household a single bill, discount or added-value proposition for:
- 176.1 multiple communications services – such as a discount for acquiring broadband and mobile services together;
- 176.2 a bundle of one or more telecommunications services with, for example, a subscription to an audio or pay TV service; and
- 176.3 the offer of a complementary product when subscribing, such as a games console or a smart TV.
177. The bundle of three services (eg, landline, broadband and pay TV) is commonly referred to as ‘triple play’ and the bundling of four services (eg, landline, broadband, pay TV and mobile) is commonly referred to as ‘quad play’.
178. Figure 11, below, from
[
].

Figure 11: Triple/quad play take-up in selected countries, 2013 (actual) to 2017 (expected)

[]

Source: [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (29 July 2016) at 101.

179. [

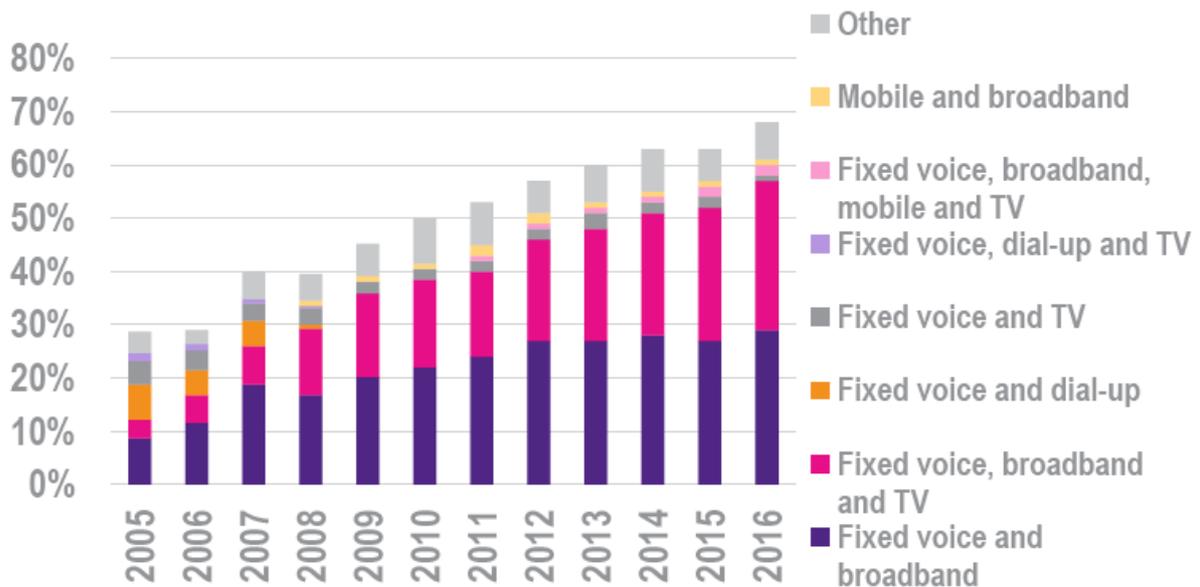
]¹⁹⁴

¹⁹³ Barry Nalebuff, “Bundling and tying” in Durlauf et al (eds) *The New Palgrave Dictionary of Economics*, Second Edition, (2008) at 602

¹⁹⁴ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (29 July 2016) at 101.

180. Figure 12, below, submitted by Plum, on behalf of 2degrees and TVNZ, shows that an increasing percentage of UK households are subscribing to telecommunications services in a bundle.

Figure 12: Telecommunications bundle take-up in the UK (2005-2016)



Source: Plum Consulting, Ofcom CMR, cited in report from Plum (on behalf of 2degrees and TVNZ) (12 August 2016) at 18.

181. Bundles that have been offered recently by TSPs in New Zealand are set out below.¹⁹⁵
- 181.1 Sky content – Vodafone has offered Sky Sport, NEON and SOHO free for between 6 and 12 months on some broadband plans. 2degrees has also offered free NEON on some of its mobile plans.
- 181.2 Other pay TV content – Spark offers Lightbox free with its broadband and mobile plans and in late 2016 signed a deal with Netflix to offer the service for free to broadband customers for 12 months when they subscribe to a 24 month unlimited UFB plan.¹⁹⁶
- 181.3 Music streaming – Spark offers free Spotify Premium on a number of its mobile plans,¹⁹⁷ and 2degrees offers music streaming service TIDAL on some plans.¹⁹⁸

¹⁹⁵ These bundles, and the period during which they ran, are set out in detail in **Attachment A**.

¹⁹⁶ Spark publicly launched this offer just after the date of this Determination, on 27 February 2017 – see <https://www.sparknz.co.nz/news/spark-customers-netflix/>.

¹⁹⁷ <https://www.spark.co.nz/discover/spotify/>.

- 181.4 Free offers – Vocus has targeted gamers with a free Xbox on some broadband plans,¹⁹⁹ while Trustpower has an offer of a free smart TV for customers taking up one of its UFB plans.²⁰⁰
182. Bundling has advantages for TSPs. Customers that take up bundles are less likely to switch away (or churn) than customers that purchase services on a standalone basis. These bundled customers are sometimes referred to as being ‘stickier’ than purchasers of a single service, and require greater inducements to switch away from a service acquired in a bundle than customers not purchasing services in a bundle.
183. The Applicants’ documents indicate that they recognise these advantages.
- 183.1 An independent report for Sky on the proposed merger noted that:²⁰¹
- The ability to package multiple services... into a single bundled offering has become increasingly important, with these bundled packages making price and value comparisons more difficult and providing disincentives for subscribers to churn.
- 183.2 The Explanatory Memorandum to Sky shareholders on the proposed merger stated that Vodafone’s New Zealand consumer business has:²⁰²
- ...converged services (packaged mobile and fixed line offerings) with a number of customers already taking mobile, fixed line and television services together resulting in higher per customer spend with Vodafone NZ and lower churn rates...
- 183.3 []²⁰³
- 183.4 []²⁰⁴
- 183.5 []²⁰⁵

¹⁹⁸ <https://www.2degreesmobile.co.nz/company/news-and-media-releases/2degrees-announce-exclusive-partnership-with-tidal/>.

¹⁹⁹ <https://netguide.co.nz/story/vocus-launches-gigabit-ufb-plans-aimed-gamers/>.

²⁰⁰ <http://www.trustpower.co.nz/landing-pages/nationwide/samsung?lcsp=EB>.

²⁰¹ Grant Samuel “Independent Adviser’s Report and Appraisal Report in relation to the Proposed Acquisition of Vodafone New Zealand Limited” (June 2016) at 26.

²⁰² Explanatory Memorandum to Sky Shareholders (14 June 2016) at 40.

²⁰³ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (29 July 2016) at 16.

²⁰⁴ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (5 August 2016) at 55.

²⁰⁵ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (5 August 2016) at 64.

184. Further, the Applicants’ documents indicate that they expect to benefit from reduced churn as a result of the proposed merger.

184.1 []²⁰⁶

184.2 The Explanatory Memorandum to Sky shareholders on the proposed merger stated that:²⁰⁷

The synergies are expected to include...a reduction in subscriber churn rates through the bundling of products. ...Subscribers for these bundled packages are typically much “stickier” than subscribers to a single product...

184.3 []²⁰⁸

185. Third parties also submitted that bundling reduces churn.

185.1 Spark submitted that the merged entity’s ability to offer triple play and quad play bundles will materially enhance customer stickiness.²⁰⁹

185.2 []²¹⁰]²¹¹

185.3 []²¹²

185.4 Axiom, on behalf of Fetch TV, submitted that both Virgin Media and BskyB in the UK have experienced lower churn rates due to bundling multiple services.²¹³ Figure 13, below, was submitted by Axiom and shows Virgin Media’s churn rates by number of services acquired.

²⁰⁶ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (29 July 2016) at 2.

²⁰⁷ Letter to Sky Directors “Summary of our Independent Adviser’s Report and Appraisal Report” (10 June 2016) at 5, included as Appendix 1 to Explanatory Memorandum to Sky Shareholders (14 June 2016).

²⁰⁸ [] provided under the cover of a letter from Bell Gully (on behalf of Vodafone) to the Commerce Commission (5 August 2016) at 12.

²⁰⁹ Submission from Spark to the Commerce Commission (12 August 2017) at [95(c)].

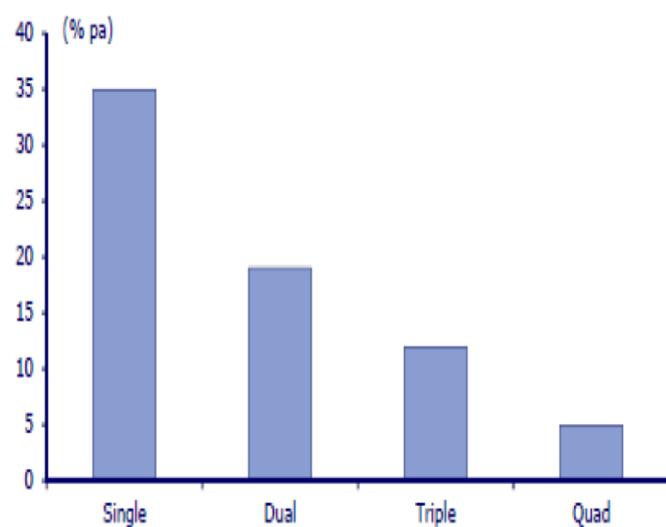
²¹⁰

[]

²¹¹ []

²¹² []

²¹³ Report from Axiom (on behalf of Fetch TV) to the Commerce Commission (26 August 2016) at 9.

Figure 13: Virgin Media UK churn rates by number of services per customer

Source: Axiom, citing CLSA, *Telecoms and media, sector outlook: Stream engines, From Broadcast to broadband*, 25 July 2016, Figure 41, at 17.

How the merger could substantially lessen competition

Introduction

186. The Applicants do not compete to supply products or services in competition with one another. Rather, the telecommunications services supplied by Vodafone complement the pay TV services offered by Sky. As our earlier discussion shows, this is increasingly the case as technology convergence facilitates the increased consumption of television content using broadband and mobile services.
187. A merger between suppliers who are not competitors, but who operate in related markets, is less likely to result in a substantial lessening of competition than a merger between existing competitors. This is because it does not lead to a direct loss of competition between the merging firms.²¹⁴
188. Nevertheless, such a merger can result in a substantial lessening of competition if it gives the merged entity a greater ability or incentive to engage in conduct that prevents or hinders rivals from competing effectively.²¹⁵ For example, if one of the merger parties has market power in a market and is able to leverage that market power into an otherwise competitive market as a result of a merger, this could lead to a substantial lessening of competition.²¹⁶

²¹⁴ Commerce Commission, *Mergers and Acquisitions Guidelines* (July 2013) at [5.1].

²¹⁵ *Ibid* at [5.2].

²¹⁶ A merger that forecloses potential competition could also raise concerns. We discuss this issue in relation to the proposed merger at [201-203], below.

189. Our assessment of the proposed merger focussed on whether the merged entity may be able to bundle Sky and Vodafone services in a way that substantially lessens competition.²¹⁷ We elaborate on this theory of potential harm below.
190. We also considered other potential competitive effects of the transaction, but we determined that they did not warrant further investigation. For completeness, we discuss these briefly below.

Bundling theory of harm

191. Bundling is a common business practice used by firms both with and without market power and it is often done for pro-competitive reasons. For example, suppliers can bundle products to reduce transaction costs by selling multiple products to customers at the same time. These cost savings can lead to lower retail prices.
192. However, where a firm has market power in relation to one product, bundling can result in competitive harm.
193. As an example, assume a firm has market power in a market where it sells product X. It also operates in another, competitive market, where it sells product Y. The firm decides to offer a bundle of products X and Y at a discount. If rivals are unable to match the firm's bundled offering, they could be foreclosed from supplying customers that wish to acquire product X. Concerns could arise if one or more rivals loses scale and exits the competitive market (where product Y is sold) or becomes a less effective competitor in that market. Potential entrants may also be deterred. This, in turn, may over time allow the price of product Y to rise above the level that would have prevailed if products X and Y had not been bundled together in this way.
194. Although customers may initially benefit from the bundle, as a result of its lower price and greater convenience, they may be worse off over the medium to long term as a result of the rise in prices when rivals are rendered less competitive, exit the market altogether or are deterred from entering. Bundling may be of concern if the merged entity has the ability and incentive to foreclose rivals, and the bundling would be likely to have the effect of substantially lessening competition in the way that we have described.²¹⁸
195. In the present case, third parties have raised concerns that reflect this theory of harm. They have said that the merged entity would be able to use Sky's premium live sports content to create bundles that rival TSPs are unable to compete with. They

²¹⁷ The theory of harm that we describe here could be viewed as having both conglomerate and vertical elements: a bundle with which rivals cannot compete, denying them access to sufficient demand and impacting their ability to achieve scale (a conglomerate effect) and rivals being unable to effectively compete with the merged entity's bundled offering, and therefore for a significant number of consumers, because they are unable to obtain premium live sports content on reasonable terms to form their own bundle (a vertical effect). For ease of reference, we refer to vertical effects in this Determination. See Commerce Commission, *Mergers and Acquisitions Guidelines* (July 2013) at [5.11-5.15] for further detail on how bundling can substantially lessen competition.

²¹⁸ See Vodafone New Zealand Limited and TelstraClear Limited [2012] NZCC 33 at [408-409].

say that this would result in a reduction in competition in each of the relevant broadband and mobile services markets.

196. This theory of harm, in both the broadband and mobile services markets, is summarised below.
- 196.1 The merged entity would control the broadcast rights for premium live sports content for which, for a significant number of consumers, there are no close substitutes. This control is a source of market power.²¹⁹ Post-merger, rival TSPs would be unable to compete effectively for these customers with other content, add-ons or strategies.
- 196.2 The merged entity would have the ability and incentive to offer this premium live sports content in a bundle on relatively more attractive terms than on a standalone basis.²²⁰ The merged entity also would not offer this content to rival TSPs at a sufficiently attractive wholesale price to enable them to offer bundles containing this content at prices competitive with the merged entity's offering.
- 196.3 A significant number of consumers would switch from rival TSPs to the merged entity. One or more rival TSPs would eventually lose sales to such an extent that they are unable or unwilling to invest and innovate, rendering them less competitively effective in the relevant market.
- 196.4 As a result, the merged entity is able to increase prices and/or decrease service quality (relative to the counterfactual²²¹). Rival TSPs would not be able to, or be incentivised to, expand and compete with the merged entity.
197. This scenario would play out against a backdrop of the UFB roll-out where more customers are in play. Subsequently they are less likely to switch back to rivals because once this 'event' is over, because these bundled customers have become 'stickier'.²²²

²¹⁹ The merged entity's control over exclusive broadcast rights for premium live sports content is a source of market power. In this Determination we use the terms 'control' and 'market power', in relation to Sky's premium live sports rights, interchangeably.

²²⁰ That is, it would set the price so that consumers could not 'build their own' bundle of the content and relevant telecommunications services for a price comparable to purchasing the merged entity's bundle.

²²¹ Our concern with the proposed merger, is that prices would be higher (or quality lower) than in the counterfactual. As such, we could observe falling prices (increasing quality) in the factual but still find a substantial lessening of competition, if those prices were higher (or quality was lower) than in the counterfactual.

²²² Axiom, on behalf of Fetch TV, submitted that the roll-out of UFB presents a rare 'consideration/re-contracting event' that changes the regular dynamic of broadband switching (which it submitted occurs when customers move house or switch for price/quality reasons) for the entire market analogous to, for example, Apple's original iPhone. Customers will have available to them a product not previously available and this presents a unique 'event' where they are more susceptible to churning. However, once this 'event' is over, they will be 'stickier'. Report from Axiom (on behalf of Fetch TV) to the Commerce Commission (26 August 2016) at 8.

198. As noted above, consumers may be better off in the short term as the merged entity offers better bundles (including better prices) and rivals react with their own bundles (and lower prices).
199. However, if the effect of the merged entity's bundling is to effectively foreclose a significant proportion of consumers from competition, such that rival TSPs become less competitively effective in the mobile or broadband services markets, the resulting price rises or decreases in the quality of service could mean that customers are worse off in the medium to long term, despite initially benefitting from more attractive offers. This may amount to a substantial lessening of competition.

Other issues raised

200. Third parties submitted that the transaction may give rise to other potentially negative competition effects. We considered these as part of our investigation, but determined that they did not warrant in-depth investigation. We discuss each of them briefly below.

Horizontal effects from the elimination of a potential competitor

201. Because Sky and Vodafone are not direct competitors, the transaction would not directly remove a competitor from a relevant market. However, we considered whether a potential competitor may be excluded. This would be the case if, without the merger, Sky and Vodafone would compete with one another in a relevant pay TV or telecommunications market. That is, if Sky would enter a telecommunications market or Vodafone would expand a pay TV service.
202. We did not consider it likely that Sky would set up its own TSP or acquire one.²²³ Rather, as set out in the counterfactual section, we consider that Sky could expand in telecommunications by reselling TSPs' products, most likely Vodafone's, where it already receives revenues through referring its customers.²²⁴
203. We also consider it unlikely that Vodafone would launch a more substantial pay TV service of its own by competing for content.
[
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²²³

[

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²²⁴ Sky has a referral arrangement with Vodafone

[

[

Commission interview with Sky (15 September 2016).

]. Sky submitted that
]. Commerce

Foreclosure of content rivals

204. We also considered whether the merged entity would disadvantage rival content providers, such as OTTs, by refusing to carry their content on its networks or by degrading the viewer experience (eg, by throttling) resulting in a lessening of competition in a relevant pay TV market.
205. We found no evidence that the merged entity would have both the ability and incentive to do so. First, throttling rivals' content would be technically challenging.²²⁵ Vodafone also submitted that it would face customer losses from degrading service quality,²²⁶ and [].²²⁷

Merged entity gaining market power for the acquisition of content

206. We assessed whether the merged entity would gain market power for the acquisition of content rights (including FTA content rights) over and above that already possessed by Sky and Vodafone independently. This could potentially further restrict rivals' chances of acquiring sufficient content to launch competing content-based offers,²²⁸ and potentially impact the competitive constraint imposed by FTA broadcasters.²²⁹
207. As discussed later in this Determination, Sky already controls the vast majority of premium live sports content rights in New Zealand.²³⁰ Both with and without the merger, Sky would be in a strong position to reacquire both the pay TV and FTA rights to this content, and would not be likely to offer it to rival TSPs on an 'unbundled' basis.²³¹
208. Regarding entertainment content, we note that there is a very large volume of rights available, as evidenced by the fact that OTTs have built large libraries of content.

²²⁵ For example, in some cases a third party, such as Akamai, acts as an intermediary between TSP networks and final consumers: Commerce Commission interview with [] (3 August 2016).

²²⁶ Submission from Vodafone to the Commerce Commission (11 September 2016) at [6.5-6.21].

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²²⁸ We consider that Vodafone would be unlikely to enter pay TV and compete with Sky directly, as explained above. However, we do not rule out that it may bid for more content in future.

²²⁹ Submission from TVNZ to the Commerce Commission (12 August 2016) at [7.1-7.11].

²³⁰ As noted earlier, Sky holds the exclusive rights to broadcast live coverage of the main sports of national significance in New Zealand: rugby, rugby league, netball and cricket. Third parties submitted that sports rights not currently licensed to Sky have proven to be less attractive to pay TV subscribers in New Zealand. For example, Spark and Coliseum Sports closed their Lightbox Sport joint-venture, which was formed to broadcast EPL and several other sports, citing insufficient subscriber interest. Submission from Spark to the Commerce Commission (12 August 2016) at [33-34].

²³¹ [] Commerce Commission meeting with Sky (19 September 2016).

[]
 209. []²³²
 []
]

The likely state of competition with and without the merger

210. As noted at the outset, we determine whether a merger is likely to substantially lessen competition in a market by comparing the likely state of competition if the merger proceeds (the factual), with the likely state of competition if the merger does not proceed (the counterfactual).²³³
211. In the context of this transaction we compare the factual and counterfactual for the purpose of determining whether the merged entity may be able to bundle Sky and Vodafone services in a way that substantially lessens competition when compared with what may occur under the counterfactual. Below, we describe the factual and the counterfactual that underpin our competition analysis, discussed in later sections.
212. In both the factual and the counterfactual, we consider that Sky (or the merged entity) is likely to retain control over the premium live sports rights held by Sky – and therefore have market power – for reasons discussed elsewhere.²³⁴

The factual – ‘with the merger’

213. The proposed merger would be a vertical/conglomerate merger between a major telecommunications provider and the major pay TV provider in New Zealand that has the exclusive rights to broadcast a significant amount of premium live sports content in New Zealand.
214. The merged entity’s incentives would be to maximise the combined profits across Sky’s pay TV business and Vodafone’s broadband and mobile services businesses. The merged entity would have the ability – and we cannot exclude a real chance that it would have the incentive – to use its market power over premium live sports rights to supply bundles of pay TV, broadband and mobile services with which rival TSPs would be unable to effectively compete.

Applicants’ submissions

215. As noted above, the Applicants advised that a rationale for the merger would be to benefit from cross-marketing opportunities and to enable firms to better respond to

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²³³ See [11-18], above.

²³⁴ See [273-282], below.

changing market conditions.²³⁵ The Applicants consider benefits from the merger would include “designing more attractive packages” and “innovating and creating new and engaging digital products”.²³⁶

216. However, the Applicants did not describe with any precision what products and/or bundles of products the merged entity would offer.

216.1 Vodafone advised that it had not thought about the post-merger bundles the merged entity would offer and had not had detailed discussions about this with Sky.²³⁷

216.2 Similarly, Sky advised that discussions with Vodafone about the services that the merged entity may offer had been at a high level only.²³⁸

Third party submissions

217. Third parties raised concerns that the merged entity would not offer Sky content on wholesale terms that would allow them to effectively compete with the merged entity.²³⁹ In particular, third parties argued that the Applicants each have a poor track record of wholesaling.²⁴⁰

218. Third parties claimed that Sky’s resale and retransmission wholesale offers have historically not been, and are not now, sufficiently attractive to allow rival TSPs to take up.²⁴¹

218.1 []^{242 243}

218.2 []²⁴⁴

218.3 Sky’s standard terms for its Sky TV offering require TSPs to purchase rights to resell or retransmit all Sky TV content. This prevents resellers from creating differentiated products and inhibits their ability to compete.²⁴⁵

²³⁵ The Applications at 2.

²³⁶ Ibid.

²³⁷ Commerce Commission interview with Vodafone (21 July 2016).

²³⁸ Commerce Commission interview with Sky (14 July 2016).

²³⁹ See, for example, submission from 2degrees to the Commerce Commission (12 August 2016) at [6.2].

²⁴⁰ See, for example, submission from 2degrees to the Commerce Commission (12 August 2016) at [6.1], submission from Trustpower to the Commerce Commission (14 August 2016) at 11 and submission from Spark to the Commerce Commission (12 August 2016) at 4.

²⁴¹ See, for example, submission from Spark to the Commerce Commission (12 August 2016) at 16, report from Covec (on behalf of 2degrees and TVNZ) to the Commerce Commission (12 August 2016) at 18 and submission from Trustpower to the Commerce Commission (14 August 2016) at 5-6.

²⁴² []

²⁴³ []

²⁴⁴ []

219. Third parties advised that Vodafone has been a reluctant wholesaler in other markets.²⁴⁶

219.1 2degrees submitted that

[
].²⁴⁷

219.2 Trustpower submitted that

[
].^{248 249}

Analysis of the evidence

220. After the merger, the merged entity would be incentivised to maximise the profits of the combined Sky and Vodafone business, as opposed to maximising the profits of each business separately, as Sky and Vodafone currently do, and would do without the merger.

221. Given the significant changes occurring in the relevant telecommunications markets discussed above, it is challenging to predict exactly where the merged entity's incentives would lie. Nevertheless, we cannot exclude a real chance that the merged entity would assess that its long-run profits would be maximised by making bundled offers combining Sky and Vodafone services (both new bundled products and discounts) that incentivise broadband and mobile services customers to switch TSP. The ability of the merged entity to do this would also be enhanced as the Applicants' incentives align and transaction costs reduce. This was indicated in the Applicants' explanation of their rationale for the merger (and Sky made express comment to this effect as described below).

222. Although the Applicants did not describe in detail the bundles of services that they would offer post-merger, their internal documents described a range of potential options. Based on these, we consider that bundles would be offered containing one or more of the features listed below.

222.1 []

222.1.1 []²⁵⁰

²⁴⁵ Submission from 2degrees to the Commerce Commission (12 August 2016) at 10 and submission from Trustpower to the Commerce Commission (14 August 2016) at 5.

²⁴⁶ Submission from 2degrees to the Commerce Commission (12 August 2016) at [6.1] and submission from Trustpower to the Commerce Commission (14 August 2016) at 11.

²⁴⁷ Submission from 2degrees to the Commerce Commission (12 August 2016) at Annexure 1.

²⁴⁸ []
Commerce Commission interview with Trustpower (11 August 2016) and submission from Trustpower to the Commerce Commission (14 August 2016) at Appendix A.

²⁴⁹ Vodafone advised that
[]

]. See n67, above.

[
]²⁵¹
 []²⁵²

222.1.2 Without the merger, Sky expects that

[
]²⁵³

222.1.3 The merged entity is likely to develop new products to deliver, as part of bundles, over broadband and mobile networks. Sky stated that, at present, bundling is challenging because each of the Applicants has different incentives. Following the merger, incentives will be aligned.²⁵⁴ The Applicants advised that a primary benefit from the merger is that the firms would be more easily able to innovate and design new products.²⁵⁵ This could include developing more attractive triple and quad play bundles and applications to deliver better experiences over mobile devices. For example, Sky advised us that the merged entity would be able to offer []²⁵⁶ and Sky CEO John Fellet stated that “[t]he faster we can get [the merger] going, the quicker we can start looking at the innovative steps we want to do – sending more content to mobile phones”.²⁵⁷

222.1.4 Vodafone also advised that it is keen to offer bundles of content and mobile services; something that it does not currently do.²⁵⁸

223. In addition to internet-based services, we consider that the merged entity would be likely to offer pay TV services that are available *only* via the internet. Mr Fellet has stated that “one of the advantages of the deal is that it gives us access to Vodafone’s

250 [] provided under the cover of an e-mail from Buddle Findlay (on behalf of Sky) to the Commerce Commission (22 September 2016).

251

[]

252

[]

253 Commerce Commission interview with Sky (15 September 2016).

254 Commerce Commission interview with Sky (21 July 2016).

255 The Applications at 2.

256 Commerce Commission interview with Sky (14 July 2016).

257 <https://www.nbr.co.nz/article/sky-tvs-fellet-tells-shareholders-submissions-against-merger-misleading-and-inaccurate-b>.

258 Commerce Commission interview with Vodafone (21 July 2016).

expertise in UFB and we certainly have plans to roll out internet-only packages to homeowners".²⁵⁹

224. Vodafone's documents also indicate that it has already considered offering content exclusively to the merged entity's customers. For example:

224.1 [

] ²⁶⁰

224.2 [

]

224.2.1 [

];²⁶¹

224.2.2 [

and

];^{262 263}

224.2.3 [

].²⁶⁴

225. Post-merger, Sky advised that the merged entity would

[

].²⁶⁵

226. Based on the evidence before us, we consider it is likely that the bundles offered by the merged entity would be lower priced and/or higher quality, with more additional

²⁵⁹ <http://stoppress.co.nz/news/sky-and-vodafone-executives-answer-questions-proposed-merger>.

²⁶⁰ [] provided under the cover of a letter from Bell Gully (on behalf of Vodafone) to the Commerce Commission (29 July 2016) at 12.

²⁶¹ [] provided under the cover of a letter from Bell Gully (on behalf of Vodafone) to the Commerce Commission (29 July 2016) at 36.

²⁶² Ibid at 36.

²⁶³

[

] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (29 July 2016) at 24.

²⁶⁴ [] provided under the cover of a letter from Bell Gully (on behalf of Vodafone) to the Commerce Commission (29 July 2016) at 34.

²⁶⁵ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (29 July 2016).

features than those available without the merger, or compared to those available on a standalone basis.

227. The roll-out of UFB and the stickiness of customers acquiring services in bundles suggests that the merged entity would be incentivised to make such offers to build sustainable market share. We discuss this in detail in a later section.
228. While we do not consider a ‘hard’ tie to be likely,²⁶⁶ we consider that there is a real chance that rival TSPs would be unable to access content from the merged entity on terms that would allow them to effectively compete with the merged entity’s bundles.
- 228.1 The Applicants have advised that the merger would allow them to develop new products and bundles. This implies that such products and bundles would be unlikely to be developed under the existing relationship between Vodafone and Sky and would be unlikely to be developed through an agreement between Sky and an independent TSP.
- 228.2 Sky has also not, to date, offered its content for resale on terms that rival TSPs consider allows them to compete on a differentiated basis. That is, TSPs are required to resell or retransmit Sky TV and cannot pick and choose content. We consider it unlikely that the merged entity would offer wholesale terms for its valuable premium live sports content (or packages containing this content) that would allow rival TSPs to construct bundles to effectively compete for these customers.
- 228.3 Similarly, while we consider it is likely that the merged entity would continue to make Sky TV available on a standalone basis, we cannot rule out the real chance that it would offer content on a standalone basis that would not allow consumers to ‘build their own’ bundles with this content and telecommunications bundles from other TSPs with the same features and at a comparable price.

The counterfactual – ‘without the merger’

229. Without the merger, Vodafone and Sky would be independent and, separately, seek to maximise their own profits. Sky may choose to develop its products in a number of ways, but in our view it would be likely to shift to supplying more content over broadband and mobile networks. Importantly, Sky would have no reason to favour Vodafone over any other TSP. We do not, however, consider that Vodafone would be likely to develop its own pay TV offering independently from Sky.

Applicants’ submissions

230. Sky submitted that without the merger it:

²⁶⁶ That is, forcing customers who wish to subscribe to Sky TV to also acquire broadband services from the merged entity.

230.1 [

],²⁶⁷

230.2 would continue to offer Sky services for resale/retransmission by third parties on the same terms as those currently offered to Vodafone (these terms are Sky's retail prices minus avoided costs and include restrictions on bundling Sky services with other pay TV services and restrictions on acquiring other content without the involvement of Sky);²⁶⁸

230.3 would consider [] (which the merged entity is also likely to do with the merger);²⁶⁹

230.4 may revisit making investments [];²⁷⁰

230.5 would likely wholesale Sky services to a greater number of parties, given recent interest that other parties have shown in reselling Sky;²⁷¹

230.6 would be unlikely to materially improve the wholesale terms on which it makes its content available to third parties for resale and retransmission.²⁷² This, it argues, would not be commercially rational because:

230.6.1 it would be sacrificing margin that it would otherwise make by selling directly to consumers;²⁷³ and

230.6.2 rival TSPs could use these revenues to develop alternative products and services in competition with Sky;²⁷⁴

230.7 would be unlikely to 'unbundle' and make content available on an individual basis (eg, offer only Sky Sport to a TSP). This is because, Sky submitted, allowing wholesale customers to pick and choose the individual rights that they purchase and combine those rights with other content in new pay TV packages (in competition with Sky) would devalue Sky's business;²⁷⁵ and

²⁶⁷ Sky Application at Annexure B.

²⁶⁸ Letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (9 September 2016) at [23].

²⁶⁹ Commerce Commission interview with Sky (15 September 2016).

²⁷⁰ Ibid.

²⁷¹ Commerce Commission interview with Sky (19 September 2016) and letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (10 October 2016) at [57].

²⁷² Letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (9 September 2016) at [23] and Commerce Commission interview with Sky (19 September 2016).

²⁷³ Letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (23 August 2016) at [14(b)].

²⁷⁴ Ibid.

²⁷⁵ Letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (23 August 2016) at [14(a)] and letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (9 September 2016) at 5.

230.8 []²⁷⁶

231. While Sky has previously considered entering telecommunications markets itself, it submitted that risk of return on investment and a lack of telecommunications expertise as reasons that it would be unlikely to pursue such a strategy.²⁷⁷ Sky considers that the resale of Vodafone services would be lower risk than expanding into telecommunications services in other ways, yet would still provide Sky with the benefits of bundling Sky and telecommunications services.²⁷⁸

[]
279

232. Vodafone advised us that it had not thought in detail about how its relationship with Sky would develop without the merger.²⁸⁰
- []²⁸¹ Vodafone indicated that it did not believe there would be any fundamental changes.²⁸²

233. Vodafone submitted that absent the merger it:²⁸³

233.1 []; and

233.2 [].

Third party submissions

234. A number of third parties submitted that without the merger Sky would become an 'enthusiastic' wholesaler of its content to a wide range of TSPs on improved terms from those that it currently offers.

234.1 2degrees, Spark, Trustpower and Blue Reach submitted that without the merger, Sky would likely become a more determined wholesale supplier of content to TSPs.²⁸⁴ Spark submitted that Sky would offer a wider range of

²⁷⁶ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (29 July 2016).

²⁷⁷ Letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (9 September 2016) at [31].

²⁷⁸ Commerce Commission interview with Sky (15 September 2016).

²⁷⁹ []

²⁸⁰ Commerce Commission interview with Vodafone (7 October 2016).

²⁸¹ See, for example, [] provided under the cover of a letter from Bell Gully (on behalf of Vodafone) to the Commerce Commission (29 July 2016) at 8.

²⁸² Commerce Commission interview with Vodafone (7 October 2016).

²⁸³ Vodafone Application at Annexure C.

²⁸⁴ Submission from 2degrees to the Commerce Commission (12 August 2016) at [4.1], submission from Spark to the Commerce Commission (12 August 2016) at [45] and [53], submission from Trustpower to the Commerce Commission (14 August 2016) at iii and submission from Blue Reach to the Commerce Commission (14 August 2016) at [1.21].

content options (including the resale of premium sport digital and mobile content rights) and at lower wholesale prices.²⁸⁵

- 234.2 Plum, on behalf of 2degrees and TVNZ, submitted that without the merger, Sky is likely to find it profit maximising to allow TSPs to repackage and rebrand its content, rather than to simply resell Sky services.²⁸⁶
- 234.3 Similarly, Covec, on behalf of 2degrees and TVNZ, submitted that wholesaling content to all or most TSPs would be a financially attractive strategy for Sky.²⁸⁷
235. Some third parties submitted that, without the merger, Sky would not enter telecommunications markets. For example, Trustpower submitted that Sky acquiring another TSP (other than Vodafone or Spark), or developing its own capability, would not provide it with sufficient scale quickly enough.²⁸⁸
236. On the other hand, other third parties submitted that Sky taking steps to become a provider of broadband is a “very likely” counterfactual scenario.²⁸⁹ Axiom, on behalf of Fetch TV, submitted that the international experience suggests that such entry is “highly probable, if not inevitable”.²⁹⁰
237. Axiom also submitted that, without the merger, Vodafone would create its own pay TV offering.²⁹¹ Trustpower similarly submitted that, without the merger, Vodafone would create its own pay TV offering in competition with Sky.²⁹²

Analysis of the evidence

238. In order to reconcile the submissions of all parties and assess the likely state of competition if the merger did not proceed, we considered the following two key questions.
- 238.1 Would Sky remain independent or seek a transaction with another entity?
- 238.2 Would Sky be likely to offer its content to other TSPs on substantially the same terms for resale and retransmission that it offers to Vodafone?
239. We also considered other changes that might occur in the market if the merger did not proceed and which are relevant to the consideration of the extent of the proposed merger’s likely effects.

²⁸⁵ Submission from Spark to the Commerce Commission (12 August 2016) at [53].

²⁸⁶ Report from Plum (on behalf of 2degrees and TVNZ) to the Commerce Commission (12 August 2016) at 30.

²⁸⁷ Report from Covec (on behalf of 2degrees and TVNZ) to the Commerce Commission (12 August 2016) at [49].

²⁸⁸ Submission from Trustpower to the Commerce Commission (14 August 2016) at 12.

²⁸⁹ Submission from Fetch TV to the Commerce Commission (9 November 2016) and report from Axiom (on behalf of Fetch TV) to the Commerce Commission (26 August 2016) at 19.

²⁹⁰ Report from Axiom (on behalf of Fetch TV) to the Commerce Commission (26 August 2016) at 19.

²⁹¹ Ibid at 19-21.

²⁹² Submission from Trustpower to the Commerce Commission (14 August 2016) at 13.

240. As discussed above at [201-203], we do not consider that Sky or Vodafone would be likely to enter the telecommunications or pay TV markets, respectively, and compete with one another in the counterfactual.

Would Sky remain independent?

241. As noted above,
[

] We
have therefore proceeded on the basis that Sky would remain independent if the merger did not proceed.

Would Sky offer the same wholesale terms to other TSPs that it offers to Vodafone?

242. We consider that, without the merger, Sky would be likely to wholesale content to more TSPs. We do not, however, consider that it would become the ‘enthusiastic’ wholesaler advocated by third parties; that is, offer its content on materially improved terms (eg, allowing TSPs to pick and choose the content that they acquire or allowing TSPs to re-brand Sky TV). We discuss each of these matters further below.

243. We consider that Sky would make its content available for resale and retransmission to other parties on largely the same terms that would be available to Vodafone.

243.1 Sky would still be an independent company seeking to maximise its own profits (rather than Sky’s and Vodafone’s joint profits as the merged entity would). There is no reason to expect that Sky would give preferential treatment to Vodafone. Sky would be willing to enter into agreements with other TSPs that enable it to increase its own profits.

[

] See [249], below.

243.2 We have seen no evidence to suggest that an exclusive arrangement between Sky and Vodafone is likely. Sky has indicated that this would be inconsistent with Sky’s incentives (eg, because it would be likely to restrict the pool of customers to which Sky TV can be sold).²⁹³

243.3 [

]²⁹⁴ []

²⁹³ Commerce Commission interview with Sky (19 September 2016) and letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (10 October 2016).

²⁹⁴ See for example, [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (5 August 2016) at 2.

243.4 Sky would also wish to avoid the risk that Vodafone gained market power in a telecommunications market, which would adversely affect Sky's ability to negotiate future reseller agreements with Vodafone.

244. Nevertheless, there is some evidence suggesting that Vodafone and Sky could deepen their relationship in the counterfactual.

[

] ²⁹⁵

244.1 [

] ²⁹⁶

244.2 Sky has identified opportunities to develop its commercial relationship with Vodafone without the merger,

[

] ²⁹⁷

245. While it is inherently difficult to predict the nature of the relationship between Sky and Vodafone in the future without the merger, we consider that this evidence indicates that, without the merger, Sky is likely to make its services available for resale and retransmission to other parties on largely the same terms that would be available to Vodafone.²⁹⁸ This differs from the factual, where we cannot exclude a real chance that the merged entity would have the incentive to offer its content to rival TSPs on terms that would not allow them to effectively compete.

²⁹⁵ For example, [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (5 August 2016) at 4, [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (12 August 2016) at 3, [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (5 August 2016) at 2, [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (12 August 2016) at 12-13, [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (12 August 2016) at 21 and Commerce Commission interview with Sky (15 September 2016).

²⁹⁶ See, for example, [] provided under the cover of a letter from Bell Gully (on behalf of Vodafone) to the Commerce Commission (5 August 2016) at 3 and [] provided under the cover of a letter from Bell Gully (on behalf of Vodafone) to the Commerce Commission (29 July 2016) at 2.

²⁹⁷ Commerce Commission interview with Sky (15 September 2016).

²⁹⁸ Notwithstanding this, it is possible that, absent the proposed merger, the Applicants could seek to enter into arrangements giving rise to similar competition issues as the proposed merger. These would be subject to Part 2 of the Commerce Act 1986.

Other market developments that may occur in the counterfactual

246. Our investigation has led us to identify other developments that might occur in the counterfactual that are relevant to the consideration of how competition may develop differently without the merger.

247. First, we considered whether any of the enhanced products available in the factual would be likely to be available in the counterfactual. We found evidence to suggest that they might, albeit with a delay.

247.1 []²⁹⁹

[]

247.2 []

247.3 []³⁰⁰

248. Second, Sky is likely to continue to make its content available to all TSPs, as well as on a standalone basis, on terms similar to those that it currently offers. In this scenario, Sky's content would be sold directly to customers and/or resold by all TSPs as part of bundles, in competition with one another.

249. Third, consistent with Sky's advice that it is likely that more TSPs would resell or retransmit Sky services in the future,³⁰¹ we consider that Sky may enter into more wholesale agreements with TSPs without the merger.

249.1 In the last 18 months, there has been an increase in interest from TSPs (including []) to enter into discussions with Sky, which

²⁹⁹ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (5 August 2016) at 4.

³⁰⁰ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (12 August 2016) at 4.

³⁰¹ Commerce Commission interview with Sky (19 September 2016) and letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (10 October 2016) at [57].

suggests an increased belief that a mutually beneficial agreement is possible.³⁰²

249.2 Sky accepts that there is a greater likelihood of it entering into agreements with TSPs in future, given recent interest that other parties have shown in doing so.³⁰³

249.3 [

] ³⁰⁴

250. As discussed already, we consider that the terms offered to other TSPs are likely to be the same as those offered to Vodafone. We do not consider that Sky would become an ‘enthusiastic’ wholesaler of the kind advocated by third parties because:

250.1 allowing wholesale customers to pick and choose the individual rights they purchase and combine those rights with other content in new pay TV packages (in competition with Sky) has the potential to devalue Sky’s business;³⁰⁵

250.2 becoming an ‘enthusiastic’ wholesaler (as discussed above) would be inconsistent with Sky’s past practice of carefully protecting its content (eg, by preventing TSPs from bundling Sky services with the content of other pay TV providers or offering other pay TV services); and

250.3 [

] ³⁰⁶

251. To the extent that the availability of attractive standalone products and greater reselling of Sky products by TSPs other than Vodafone in the counterfactual

³⁰² In the case of some parties (eg, []), there are some indications that the timing of this interest may have been driven, at least in part, by the timing of the Applications. This is not the case for all parties, however. For example, []].

³⁰³ Commerce Commission interview with Sky (19 September 2016) and a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (10 October 2016) at [57].

³⁰⁴ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (5 August 2016) at 69.

³⁰⁵ We have previously considered Sky’s restriction on TSPs bundling its content with non-Sky content in our *Sky Contracts* investigation, where we found that this conduct was legitimate to protect investments made in its products, and was unlikely to have breached the Commerce Act 1986. Commerce Commission Investigation Report on Sky TV contracts (8 October 2013) at [30-32].

³⁰⁶

[] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (12 August 2016).

increased competition in the broadband and/or mobile services markets, this is likely to exacerbate the detriment to competition arising from the foreclosure of rival TSPs in the factual.

Market definition

Our approach to market definition

252. Market definition is a tool that helps identify and assess the close competitive constraints that the merged entity would face. Determining the relevant market requires us to judge whether, for example, two products or services are sufficiently close substitutes as a matter of fact and commercial common sense to fall within the same market.
253. We define markets in the way that best isolates the key competition issues that arise from a merger.³⁰⁷ In many cases this may not require us to precisely define the boundaries of a market. What matters is that we consider all relevant competitive constraints, and the extent of those constraints. For that reason, we also consider products and services that fall outside the market but that still impose some degree of competitive constraint on the merged entity.

Applicants' submissions

254. The Applicants submitted that the key markets potentially affected by the merger would be:³⁰⁸
- 254.1 the national retail market for the provision of residential fixed-line broadband services; and
- 254.2 the national market for the retail provision of pay TV services.

Third party submissions

255. We received a number of submissions from third parties about the scope of the relevant markets.
- 255.1 Spark and 2degrees submitted that the retail market(s) for mobile services would be affected by the proposed merger.³⁰⁹
- 255.2 Fetch TV submitted that we should consider a market for the retail provision of pay TV services as part of a triple or quad play bundle.³¹⁰
- 255.3 Multiple parties submitted that wholesale markets for the acquisition of premium live sports, movies and/or first-run television series content were relevant to assessing the proposed merger.³¹¹

³⁰⁷ Commerce Commission, *Mergers and Acquisitions Guidelines* (July 2013) at [3.10-3.12].

³⁰⁸ The Applications at [6.1].

³⁰⁹ Submission from Spark to the Commerce Commission (12 August 2016) at [5] and submission from 2degrees to the Commerce Commission (12 August 2016) at [3.3].

³¹⁰ Submission from Fetch TV to the Commerce Commission (12 August 2016) at [3.2].

255.4 TVNZ submitted that it is necessary to examine the competitive effects of the proposed merger on the national market for the retail supply of FTA TV services (not just pay TV services) and on a broader national market for TV services (encompassing both FTA TV and pay TV services).³¹²

255.5 []³¹³

Analysis of the evidence

The relevant pay TV market

256. The Commission last considered pay TV markets in its *Sky Contracts* investigation in 2013, where we found a market for the supply of pay TV to consumers in New Zealand, including TV, SVOD and TVOD.³¹⁴ This was consistent with the Commission’s approach in the Investigation into the *Igloo* Joint Venture in 2012.³¹⁵
257. In this case, our primary concern is that the merged entity would be able to leverage its control of premium live sports content into one or more telecommunications markets. We therefore need to test whether there are sufficient substitutes for Sky’s premium live sports content that rival TSPs could use to create offers to allow them to effectively compete against the merged entity in broadband and mobile services markets.³¹⁶
258. The Commission has previously found that premium live sports content has characteristics that differentiate it from other content.³¹⁷ In this case, a significant number of Sky TV customers – over []% – pay an additional fee to subscribe to Sky Sport, the service on which Sky broadcasts its premium live sports content.

³¹¹ Submission from Spark to the Commerce Commission (12 August 2016) at [5], submission from 2degrees to the Commerce Commission (12 August 2016) at [3.3], submission from TVNZ to the Commerce Commission (12 August 2016) at [2.9] and submission from Fetch TV to the Commerce Commission (12 August 2016) at [3.2].

³¹² Submission from TVNZ to the Commerce Commission (12 August 2016) at [2.9]. As discussed below, given that we considered a market for premium live sports content, we did not need to come to a view about whether pay TV and FTA TV are in the same market.

³¹³ []

³¹⁴ Commerce Commission Investigation Report on Sky TV contracts (8 October 2013) at [139].

³¹⁵ In the *Igloo* investigation, we noted that there is a ‘spectrum’ of competition across content providers. For example, we found that SVOD services may compete more closely with FTA than with pay TV, although we did not need to conclude on the precise scope of the market. Commerce Commission, Investigation Report on the *Igloo* Joint Venture between TVNZ Ltd and Sky Network Television Ltd (16 May 2012) at [108-133].

³¹⁶ Third parties we spoke with have, at times, described this assessment as determining whether Sky content is “must have” to compete in retail telecommunications markets. Content will only be “must have” if it has no close substitutes for a substantial number of customers. If there were no close substitutes and rivals were rendered competitively less effective by not having access to the content, then the Sky content could be considered “must have”.

³¹⁷ Sky Network Television Limited and Prime Television New Zealand Limited (Decision 573, 8 February 2006) at [98-100] and Investigation Report on the *Igloo* Joint Venture between TVNZ Ltd and Sky Network Television Ltd (16 May 2012) at [123.1].

259. We considered, for the purposes of our analysis, whether premium live sports content comprised a separate market. In our view, the evidence suggests that it does and that there is a national retail market for the broadcast of New Zealand premium live sports content.³¹⁸
260. First, live sport has significantly different properties from other types of content such as non-live sports or entertainment content. Vodafone Group has previously recognised that such content “has no close substitutes”³¹⁹ and that its live nature means that it loses value quickly soon after it is broadcast.³²⁰
261. Second, as we found in the *Igloo* investigation,³²¹ some consumers value sports content much more highly than other types of content. Prior to the introduction of FanPass, consumers needed to subscribe to Sky Basic and pay an additional fee in order to access premium live sports content. Today, this additional fee represents more than half the price of Sky Basic. The monthly subscription fee for FanPass (which only gives access to Sky Sport Channels 1-4) is more expensive than a Sky Basic subscription (which gives access to 50 channels).
262. Third, the live sport offerings of other entities (eg, EPL on BeIN or Duke’s live sports offering) do not appear to be close substitutes for Sky’s premium live sports content. The survey evidence that we have suggests that those sports are less popular than the content that Sky broadcasts.³²² Spark submitted that Lightbox Sport was not successful because it was unable to obtain a bundle of premium sports content.³²³
263. Fourth, []³²⁴
[]³²⁵ This suggests that Sky faces limited competition for these customers from other content.

³¹⁸ We note that in our 31 October 2016 Letter of Unresolved Issues, we defined markets for the retail and wholesale supply of pay TV services, consistent with our approach in the *Igloo* and *Sky Contracts* investigations. We also recognise that most consumers, other than FanPass subscribers, do not purchase premium live sports content on a standalone basis, but as part of a broader bundle of pay TV services supplied by Sky. Consistent with our purposive approach to market definition, this broader, differentiated, market will likely continue to be relevant for analysing the competition issues arising in other investigations. For purposes of the current assessment, however, what matters is whether there are close substitutes for premium live sports content.

³¹⁹ Vodafone “Public consultation on the evaluation and the review of the regulatory framework for electronic communication networks and services” (2 December 2015) at 31.

³²⁰ Vodafone “Response to Ofcom’s Consultation: Strategic Review of Digital Communications discussion document” (8 October 2015) at [3.1].

³²¹ Sky Network Television Limited and Prime Television New Zealand Limited (Decision 573, 8 February 2006) at [102].

³²² Report from Castalia (on behalf of Spark) to the Commerce Commission (12 August 2016) at 3 ([]).

³²³ Submission from Spark to the Commerce Commission (12 August 2016) at [33-34].

³²⁴ See the examples set out at [183-184], above.

³²⁵ [] provided under the cover of a letter from Bell Gully (on behalf of Vodafone) to the Commerce Commission (5 August 2016) at 30.

263.1 The Explanatory Memorandum to the proposed transaction describes Sky’s “strong lock on the key sporting rights that are significant drivers of subscription activity...”³²⁶

263.2 []³²⁷ []

[]

263.3 []:³²⁸ []

[]

]

Relevant broadband and mobile services markets

264. The Commission last considered consumer telecommunications markets in detail in a merger context in *Vodafone/TelstraClear*.³²⁹ In that decision, the Commission defined retail markets as follows:

264.1 the national retail market for the provision of residential fixed-line broadband services; and

264.2 the national retail market for the provision of mobile services (for residential and business consumers).

265. In this case, a substantial lessening of competition would take the form of TSPs decreasing investment in their networks, and not reinvesting to combat an exercise of market power by the merged entity in the medium to long term.

266. We consider that the approach to market definition set out in *Vodafone/TelstraClear* is broadly appropriate for our purposes. However in this case our analysis of the

³²⁶ Letter to Sky Directors “Summary of our Independent Adviser’s Report and Appraisal Report” (10 June 2016) at 10, included in Appendix 1 to Explanatory Memorandum to Sky Shareholders (14 June 2016).

³²⁷ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (12 August 2016) at 17.

³²⁸ [] provided under the cover of a letter from Bell Fully (on behalf of Vodafone) to the Commerce Commission (29 July 2016) at 9.

³²⁹ Vodafone New Zealand Limited and TelstraClear Limited [2012] NZCC 33. We considered business fixed-line, national backhaul and data tails markets more recently in *Vocus Communications Limited and M2 Group Limited* [2015] NZCC 33.

relevant broadband and mobile services markets also takes into account business broadband customers. The reason is that TSPs use many of the same assets to supply business and residential customers and the TSPs that compete for those customers are largely the same. Broadband and mobile services providers could use the revenues from either set of customers to cover the costs of operating and maintaining their networks.

267. We also considered whether to separate the mobile services market into pre-pay and on-account services. However, we did not need to reach a definitive view on whether separate markets for these services exist. Instead, we take these different types of services into account as relevant when assessing the likely effects of the proposed merger.
268. Fixed voice services are also relevant to our assessment. However, for the purposes of our analysis we consider broadband and fixed voice services together because fixed voice is normally purchased from the broadband supplier.³³⁰ A customer that switches broadband supplier will almost certainly also switch their fixed voice service supplier.

Conclusion

269. Based on the evidence before us, for the purpose of our analysis that follows we consider the following markets:
- 269.1 the national retail market for the broadcast of New Zealand premium live sports content;
- 269.2 the national retail market for the provision of fixed-line broadband services (residential and business); and
- 269.3 the national retail market for the provision of mobile services (for residential and business consumers).

270. []

Competition analysis

271. Many of the factors relevant to our assessment of the proposed merger are substantively the same in both the broadband and mobile services markets. Our assessment, for the most part, therefore considers the effects on both markets together.
272. Where appropriate however, we discuss these markets individually, before concluding, separately, on each relevant market.

³³⁰ See, for example, Vodafone New Zealand Limited and TelstraClear Limited [2012] NZCC 33 at [79-83].

The merged entity's control of premium live sports content

273. Sky is New Zealand's leading pay TV provider, with a portfolio of premium entertainment and sports content.³³¹ The importance of premium live sports content was discussed earlier in the market definition section. We conclude it is likely that the merged entity would retain control of Sky's premium live sports content over the medium to long term.
274. Post-merger, the merged entity will control the rights to broadcast all New Zealand premium live sports content: rugby, cricket, NRL and netball until at least 2020.³³² This means that rivals, including pay TV and FTA providers, would be unable to obtain the rights for this premium content in the first three years post-merger.
275. Based on the evidence before us, we consider it likely that the merged entity would continue to control the rights to this premium live sports content after the dates on which these rights come up for renewal.
276. [
-]
277. Moreover, there are significant hurdles to winning the broadcast rights to this content.
- 277.1 [
-]³³³
- 277.2 Sky has a large, established subscriber base, meaning that it faces less uncertainty about potential returns on investment when bidding for content. By contrast, a new or smaller rival faces a higher degree of uncertainty given it would need to build up a subscriber base to provide a return on its investment.³³⁴ Third parties' submissions were consistent with this view. They submitted that Sky has an advantage in competing for premium live sports rights because it has an established subscriber base, can provide a guarantee of FTA and pay TV coverage, and owns a company that produces and broadcasts the content.³³⁵ Spark described this as a "vicious circle", in that

³³¹ Vodafone and Sky NZX announcement of the proposed merger (9 June 2016) at 2.

³³² Sky has the rights to cricket until 2020, rugby and netball until 2021, and NRL until 2022.

³³³ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (29 July 2016) at 26-29.

³³⁴ The ACCC has previously found that the acquisition of content on an exclusive basis is a significant barrier to competing for content rights. See ACCC "FOXTEL – proposed acquisition of Austar United Communications Limited" (14 June 2012).

³³⁵ See, for example, submission from Spark to Commerce Commission (12 August 2016) at 10-11, report from Castalia (on behalf of Spark) to the Commerce Commission (12 August 2016) at 4, 9 and submission from TVNZ to Commerce Commission (12 August 2016) at [1.3].

278.2 [

] ³⁴¹

[

] ³⁴²

278.3 [

] ³⁴³

278.4 [

] ³⁴⁴

279. We note that there has been a growing trend for content owners to offer their sports direct to consumers. For example, as noted by the Applicants, a number of sports bodies deliver content direct to New Zealand consumers through the internet.³⁴⁵ It is possible that owners of premium content rights – including sports bodies in particular – may launch OTT services in future to reach consumers directly, alone or with partners, and rely less on Sky and pay TV providers.³⁴⁶ However, the opportunity for rights holders to decline Sky’s rights renewal in favour of OTT self-delivery would arise only when the rights come up for renewal.
280. In summary, we consider that the merged entity would enjoy a strong incumbency advantage that would enable it to retain the exclusive rights to broadcast New Zealand premium live sports rights. [] and any third party seeking them faces a number of practical difficulties competing against the merged entity.
281. In addition, we are not satisfied that delivering content directly to consumers is likely to be a viable alternative for rights holders in the medium to long term.

³⁴¹ []

³⁴² []

³⁴³ []

³⁴⁴ []

³⁴⁵ The Applications at [7.5].

³⁴⁶ See, for example, Commerce Commission interview with [] (3 August 2016).

282. For these reasons, we have concluded that it is likely that the merged entity would retain these rights when they next come up for renewal and in so doing, maintain its control of premium live sports content over the medium to long term.

For a significant number of telecommunications services consumers there are no close substitutes for premium live sports content

283. We have concluded that the merged entity would continue to control premium live sports content, and that, for those that subscribe to this content (ie, Sky Sport subscribers), there are no close substitutes.³⁴⁷ Further, for the reasons set out below, we consider that the merged entity would have market power by virtue of its control of this content.

284. A significant number of broadband and mobile customers subscribe to Sky Sport.³⁴⁸

284.1 As at 30 June 2016, out of a total of [] Sky subscribers, [] customers ([]%) subscribed to Sky Sport. This means that approximately []% of residential broadband services customers purchase a Sky package that includes Sky Sport.^{349 350}

284.2 For mobile services, out of a total of approximately 1.7 million New Zealand households, [] subscribe to Sky Sport. If mobile phones were evenly distributed among these households, this would imply that approximately []% would be in households with a Sky Sport subscription.^{351 352}

285. These figures give an indication of the percentage of Sky Sport subscribers that have broadband and/or mobile accounts with rival TSPs and that would be susceptible to switching to the merged entity if they cannot obtain this content:

285.1 either on a standalone basis from the merged entity at a competitive price, while continuing to acquire broadband and mobile services from a TSP other than the merged entity; or

285.2 in a bundle of Sky Sport and broadband and/or mobile services from a rival TSP, at a competitive price.

³⁴⁷ See the discussion on market definition at [256-263], above.

³⁴⁸ As at October 2016 there were also [] FanPass subscribers.

³⁴⁹

[

]

³⁵⁰

[

]

³⁵¹ There are approximately [] mobile connections in New Zealand, implying an average of just over three mobile handsets per household.

³⁵² If the December 2016 Sky Sport subscriber figure is used, this would imply []% would be in households with a Sky Sport subscription. Again, however, this did not materially affect our analysis.

Would customers be likely to have access to premium live sports content other than through the merged entity on competitive terms?

286. Given our view that the merged entity is likely to control premium live sports rights past the end dates of the current contracts with content owners, and that there is no close substitute for premium live sports content for a significant group of customers, we next considered whether the merged entity would have both the ability and the incentive to leverage its market power, derived from control of these rights, into each of the relevant broadband and mobile services markets. We concluded that we cannot exclude a real chance of this occurring in a manner that substantially lessens competition.
287. As discussed above, we concluded that:
- 287.1 the merged entity would be likely to continue to offer Sky Sport to customers on a standalone basis. However, we cannot rule out a real chance that the merged entity would make buying Sky Sport on a standalone basis relatively less attractive than purchasing it in a bundle (because of the lower price and/or higher quality and other features available in these bundles);³⁵³ and
- 287.2 the merged entity would continue to offer Sky services on a wholesale basis to rival TSPs. It is possible that TSPs could bundle those services with their own broadband and/or mobile services. However, we cannot rule out a real chance that rival TSPs would be unable to access content from the merged entity on terms that would allow them to effectively compete with the merged entity's offerings.
288. In the sections that follow, we summarise the submissions that we received relating to the merged entity's ability and incentive to achieve these outcomes and explain our conclusions in more detail.

Applicants' submissions

289. The Applicants submitted that access to Sky content is not, and will not become, necessary in order for rival TSPs to viably compete with the merged entity.³⁵⁴
290. The Applicants submitted that bundled telecommunications and content offerings are not currently a major feature of the relevant markets.
- 290.1 Vodafone submitted that fewer than 10% of the 1.5 million broadband customers in New Zealand currently buy a bundle of Sky content with Vodafone broadband, and Sky Sport is not offered as part of any mobile bundle.³⁵⁵ Similarly, Sky submitted that premium live sports content is not a "must have" that could be leveraged as part of a foreclosure strategy because

³⁵³ See [228], above.

³⁵⁴ The Applications at [11.1(a)] and letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (23 August 2016) at [22].

³⁵⁵ Submission from Vodafone to the Commerce Commission (10 October 2016) at [4.3].

most households do not have Sky Sport and most TSPs do not offer bundles that include Sky Sport.³⁵⁶

290.2 Vodafone provided a chart showing that

[].³⁵⁷

290.3 Vodafone submitted

[].³⁵⁸

290.4 Sky submitted that Sky content is not “must have” for TSPs to compete in telecommunications markets, because Vodafone is the only TSP reselling Sky TV.³⁵⁹ Vodafone submitted that other TSPs have not sought to resell Sky TV because they do not believe the investment would drive sufficient demand.³⁶⁰ The Applicants noted that Spark previously re-sold Sky TV, but chose to discontinue doing so to develop Lightbox).³⁶¹

291. Vodafone submitted that

[]. In particular, premium live sports content is the content that is least likely to be viewed over mobile networks on mobile devices.³⁶² Vodafone submitted that there would need to be a “sea change” in consumer preferences before Sky content could be said to be a “must have” input into telecommunications markets. Vodafone submitted that there is no evidence indicating that this will occur.³⁶³ Indeed, Vodafone submitted that “if anything, the relative importance of SKY content as a component of a telecommunications bundle is likely to become less (not more) important in the future”.³⁶⁴

Applicants’ documents and statements

292. Other evidence attributable to the Applicants’ nevertheless emphasised the advantage of owning the exclusive rights to broadcast premium live sports content and the opportunity presented by bringing together broadband and mobile services offerings with pay TV offerings in a broader context of converging technologies and changing consumer preferences.³⁶⁵

293. As discussed above at [118], the Applicants’ internal documents indicated that Sky Sport is “key” content and likely to be very important to compete in the broadband and mobile services markets post-merger.

³⁵⁶ Letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (9 September 2016) at [43].

³⁵⁷ Submission from Vodafone to the Commerce Commission (11 November 2016) at [1.6(e)].

³⁵⁸ Submission from Vodafone to the Commerce Commission (10 October 2016) at 6-7.

³⁵⁹ Letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (9 September 2016) at [43].

³⁶⁰ Submission from Vodafone to the Commerce Commission (10 October 2016) at [1.2(a)(ii)].

³⁶¹ The Applications at [10.4].

³⁶² Submission from Vodafone to the Commerce Commission (11 November 2016) at [1.8].

³⁶³ Submission from Vodafone to the Commerce Commission (10 October 2016) at [4.4-4.5].

³⁶⁴ Ibid at [4.7(g)].

³⁶⁵ Indeed, this is part of the stated rationale for the proposed merger. See [3-8], above.

294. In addition, as noted above, public statements by Vodafone Group in other jurisdictions have also recognised that live sports content has “no close substitutes”. Further, it has recognised that access to this content is important to compete in telecommunications markets.³⁶⁶

295. In October 2015 Vodafone UK stated in a submission to Ofcom that:³⁶⁷

Key content is by its nature exclusive, or put simply a monopoly input, which in any other scenario would be subject to appropriate regulation...sport stands apart due to its very specific characteristics: propensity to lose value after live broadcast; its degree of exclusivity to individual pay TV services and the sums invested to secure those relevant exclusive broadcast rights. In particular, SKY [UK] and BT’s willingness to spend so much on sports broadcast rights ...indicates the value they believe they can recover from utilising this content. Given the combination of these factors, sports appears to be uniquely placed to drive consumer choice in Pay TV services and beyond. this raises the concern that given the rise in converged services, content providers will be incentivised to leverage their rights of such ‘key content’ and limit distribution.

296. Vodafone submitted that these comments were made in light of concerns about the behaviour of infrastructure owners BT and Openreach in the UK.³⁶⁸

297. In terms of the importance of bundled content in the future, a number of the Applicants’ documents also appear to recognise the importance of bundling content with telecommunications content in the future:

297.1 []³⁶⁹

[]

297.2 []³⁷⁰

[]

297.3 []

³⁶⁶ At [260], above.

³⁶⁷ Vodafone “Response to Ofcom’s Consultation: Strategic Review of Digital Communications discussion document” (8 October 2015) at [3.1].

³⁶⁸ Submission from Vodafone to the Commerce Commission (11 September 2016) at [7.6].

³⁶⁹ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (29 July 2016) at 3.

³⁷⁰ [], provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (29 July 2016) at 2.

]

Third party submissions

298. Consistent with our conclusion that the merged entity would be likely to have control of premium live sports rights post-merger, and that customers would have no close substitutes for that content, a number of third parties submitted that Sky's live sports content (in particular, rugby, NRL, cricket and netball) is "premium" content because of consumers' strong preferences for it (since it can reflect national identity, and live viewing is highly prized).³⁷¹ For example, 2degrees submitted that premium live sports content is the key differentiator of telecommunications bundled offerings, leading to higher ARPU and greater customer loyalty.³⁷²
299. Third parties also submitted that sports rights not currently held by Sky have proven to be less attractive to pay TV subscribers in New Zealand. For example, Spark advised that it and Coliseum Sports closed their Lightbox Sport joint-venture, which was formed to distribute the English Premier League and several other secondary sports, citing insufficient subscriber interest.³⁷³
300. Further, Castalia, on behalf of Spark, submitted that Sky's package prices are significantly higher than those of OTT rivals, such as Netflix, due to the power of premium sports content.³⁷⁴
301. While other content could be offered in a bundle with telecommunications services, third parties submitted that Sky content is "a compelling and non-replicable "must have" source of entertainment for a significant proportion of New Zealanders".³⁷⁵
302. Third parties also submitted that, to the extent that Sky Sport is not "must have" for rival TSPs to compete in the broadband and mobile services markets now, it will become so in the future.³⁷⁶
303. Plum, on behalf of 2degrees and TVNZ, provided data showing an increase in take-up of multi play bundles in New Zealand and overseas, and suggested that Sky content would become necessary for competition between these bundles.³⁷⁷

³⁷¹ Report from Covec (on behalf of 2degrees and TVNZ) to the Commerce Commission (12 August 2016) at 15, report from Plum (on behalf of 2degrees and TVNZ) to the Commerce Commission (12 August 2016) at 20-22, submission from Spark to the Commerce Commission (12 August 2016) at 6-10, submission from TUANZ to the Commerce Commission (12 August 2016) at [29], report from Castalia (on behalf of Spark) to the Commerce Commission (12 August 2016) at 2-3 and submission from Trustpower to the Commerce Commission (14 August 2016) at 7-8.

³⁷² 2degrees submission to the Commerce Commission (12 August 2016) at 2.14. Plum, to which the 2degrees submission refers, notes an increase in viewing of live NFL matches at the same time that entertainment viewing has decreased. Report from Plum (on behalf of 2degrees and TVNZ) to the Commerce Commission (12 August 2016) at 20.

³⁷³ Submission from Spark to the Commerce Commission (12 August 2016) at [33-34].

³⁷⁴ Report from Castalia (on behalf of Spark) to the Commerce Commission (12 August 2016) at 2-3.

³⁷⁵ Submission from Spark to the Commerce Commission (5 October 2016) at 10.

³⁷⁶ See, for example, report from Covec (on behalf of 2degrees and TVNZ) to the Commerce Commission (30 September 2016) at [54-55].

304. As to the reason why only Vodafone currently offers Sky content in a bundle, third parties submitted that this is because Sky does not offer TSPs access on reasonable terms.

304.1 []³⁷⁸

304.2 2degrees advised that, in its view, Sky's terms were unattractive.³⁷⁹

304.3 Trustpower advised that Sky's wholesaling terms were restrictive.³⁸⁰

Third parties' documents and statements

305. We note that [] did not appear to be initially concerned by the proposed transaction. For example, Spark's public statements immediately following the announcement of the proposed merger suggest that Spark believed it would be able to compete against the merged entity. A June 2016 Spark announcement stated:³⁸¹

The reality is that Spark has been competing successfully with a tightly integrated partnership between Vodafone NZ and Sky TV for a couple of years now. Vodafone NZ has been bundling and deeply discounting SKY TV products while SKY TV actively resells Vodafone NZ broadband ...we don't believe a merger Sky TV and Vodafone NZ poses a greater challenge to Spark than the existing partnership has achieved to date.

From a competitive perspective, Spark competes hard with Vodafone NZ every day. But we don't really see ourselves competing head-to-head with Sky TV. The real competition in the future of media is with global over-the-top players like Netflix, YouTube and Apple or with direct-to-consumer premium sports content owners.

306. []

307. []³⁸²
[]³⁸³ []³⁸⁴

³⁷⁷ Report from Plum (on behalf of 2degrees and TVNZ) to the Commerce Commission (12 August 2016) at 18-20.

³⁷⁸ []

³⁷⁹ Submission from 2degrees to the Commerce Commission (12 August 2016) [5.10].

³⁸⁰ Submission from Trustpower to the Commerce Commission (14 August 2016) at 11.

³⁸¹ <http://www.scoop.co.nz/stories/BU1606/S00229/spark-ready-to-compete-with-merged-sky-tv-and-vodafone-nz.htm>.

³⁸² [] provided under the cover of an e-mail from Spark to the Commerce Commission (1 December 2016).

³⁸³ Ibid at 12.

³⁸⁴ Ibid.

[]

308. Spark advised that it did not

[³⁸⁵]

309. [

[]³⁸⁶ []³⁸⁷
[]³⁸⁸

310. [

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311. [

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312. [

] ³⁹⁰

[]³⁹¹
[]

313. [

]

³⁸⁵ Commerce Commission interview with Spark (19 December 2016).

³⁸⁶ []

³⁸⁷ []

³⁸⁸ []

³⁸⁹ []

³⁹⁰ []

³⁹¹ []

The potential for the merged entity to foreclose a substantial customer base from rival TSPs through bundling

314. We consider that the merged entity would be likely to continue to offer standalone Sky services to customers as well as wholesale services to other TSPs.³⁹² However, we cannot rule out a real chance that the merged entity would have both the ability and the incentive to leverage market power over premium live sports content into the relevant broadband and mobile services markets through a bundling strategy that forecloses a substantial number of customers from rival TSPs.
315. We consider that it could do this by:
- 315.1 making Sky Sport, on a standalone basis, relatively less attractive to customers than purchasing it in a bundle (in terms of price, content and other features), which would be likely to drive broadband and mobile customers of rival TSPs to switch to the merged entity; and
- 315.2 preventing rival TSPs from accessing premium live sports content on terms that would allow them effectively to compete with the merged entity's bundled offerings.
316. In the sections that follow we consider the merged entity's likely ability and incentives further. We also discuss what its bundles would look like with reference to the features that it would be likely to offer. We then go on to consider the likelihood of a significant number of customers being foreclosed to rival TSPs such that it gives rise to a substantial lessening of competition in broadband and mobile services markets.

The merged entity would have the ability and incentive to offer relatively more attractive bundles than would be available via rivals and on a standalone basis

317. Control over premium live sports rights, for which there are no close substitutes, would clearly provide the merged entity with the *ability* to structure the relative price, quality and content of standalone and bundled offers in whatever way it expects to be profit maximising.
318. We also conclude that the merged entity would have the *incentive* to do so in a way that induces Sky Sport subscribers, and some non-Sky Sport subscribers, to switch TSP so that they acquire their broadband and/or mobile services with Sky Sport in a bundle offered by the merged entity. We discuss this ability and incentive further below.
319. As discussed earlier, the Applicants have said that the synergies associated with putting together a pay TV and telecommunications company would allow the merged entity to develop new products and features, and more effectively cross market pay TV and broadband and mobile services.³⁹³ In our view, this implies that

³⁹² See [228].

³⁹³ See [3-8], above.

this would be more difficult to achieve with two separate companies. Indeed, this is an aspect of the very rationale claimed for the merger.

320. The transaction costs of dealing with one another as separate entities are higher than will be the case for the merged entity. It also suggests that it would be more difficult for TSPs to offer competitive bundles of services, particularly if they are required to bundle together services that they resell, rather than services that they control and provide themselves.

321. As discussed above, Sky advised that, at present, it is challenging to construct bundles because each of the Applicants has different incentives. Post-merger, the incentives of Sky and Vodafone would be aligned.³⁹⁴

322. []³⁹⁵

[

]

323. These sentiments are reflected elsewhere in the Applicants' discussion of the rationale for the merger.³⁹⁶

324. We consider that the context in which the merger will take place also supports the ability and the incentive for the merged entity to leverage its market power over

³⁹⁴ Commerce Commission interview with Sky (21 July 2016).

³⁹⁵ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (29 July 2016) at 3.

³⁹⁶ See [3-8], above.

premium live sports content rights into the relevant broadband and mobile services markets.

325. In our description of the industry background, we described the history of consistent improvements in the quality and availability of broadband and mobile networks and the steady increase in internet based broadcasting and viewing of content over the internet. The means to deliver content has converged with broadband and mobile services and is expected to continue to do so.³⁹⁷
326. There is evidence suggesting that premium live sports content will increasingly be viewed over the internet in the future as broadband and mobile services and pay TV converge. As this happens, we consider that consumers are likely to value more highly bundles containing both content and the means to deliver that content (broadband and mobile). Bundles offered by a single supplier such as the merged entity are likely to be even more attractive to consumers who view their content and broadband and/or mobile services as closely related, if not as one and the same thing.
327. Post-merger the merged entity would be uniquely positioned to exploit changing consumer preferences by offering bundles that bring together pay TV services and broadband and/or mobile services.
328. We cannot exclude the real chance that the relative terms of these bundles would be significantly better (and have additional features) than those that would be available to consumers of standalone Sky Sport or alternatives offered to consumers by other TSPs. We discussed these features and pricing incentives in detail in the factual section, above, but for the purposes of this section we note:
- 328.1 currently, and in the counterfactual, consumers would be able to subscribe to Sky on a standalone basis and ‘build their own’ bundles by taking up offers from other TSPs (including bundled offerings containing content such as Lightbox and Spotify). For example, a consumer could subscribe to Sky Sport on a standalone basis,³⁹⁸ but save money buying a bundle of broadband and mobile from their choice of TSP;
- 328.2 post-merger, however, the merged entity would control premium live sports content and have interests in the broadband and mobile services markets. This would give it the ability to offer bundles at prices lower than rival TSPs can offer (or that consumers can construct). This, in turn, would be likely to drive consumers to take-up bundles of Sky Sport from the merged entity, at the expense of rival TSPs; and
- 328.3 as noted above, the merged entity’s ability to develop and offer attractive bundles combining Sky and broadband and/or mobile services would be greater than Vodafone’s is today, further enhancing its ability to attract consumers.

³⁹⁷ See [129-137] and [163-172], above.

³⁹⁸ Either by subscribing to Sky TV and Sky Sport, or by purchasing FanPass each month.

329. Thus, post-merger Sky Sport subscribers are likely to be driven more towards taking up the merged entity's bundles to take advantage of the preferential terms on offer and the opportunity to meet their converging content and technology needs with a single integrated supplier. As discussed at [182], above, these customers are also likely to become 'stickier' – that is, less likely to switch away – once they take up these bundles.
330. The merged entity's ability to bring together Sky services and broadband and/or mobile services in an attractive way will be enhanced as the UFB rollout improves the ability to deliver pay TV services over broadband.
331. However, we also consider that the UFB roll-out provides the merged entity with a unique opportunity to win customers. It is unique not only because increased viewing of content over the internet and changing consumer preferences are strongly influenced by the improved quality of broadband delivered by the roll-out of UFB, but also because it is a 'one off' event that puts consumers in play and looking to make changes to their services and potentially their service provider.³⁹⁹ Evidence provided by the Applicants supports this view.
332. For example:
- 332.1 the Applicants submitted that the merger, and the merged entity's product development, would allow greater participation in the opportunities presented by the Government's fibre and rural broadband Initiatives;⁴⁰⁰
- 332.2 [];⁴⁰¹ and
- 332.3 [].⁴⁰²
333. As set out in Figure 5, above, the number of residences connecting to UFB has increased steadily over time. However, the vast majority of residential customers have still to be connected. The Government's UFB Initiative means that 75% of New Zealanders will have access to UFB by 2019, and 85% by 2024.
334. Once customers have switched to the merged entity's bundles, they are less likely to be in play in future. Hence, it is likely to be more difficult for rival TSPs to win them back at a later date. The UFB rollout will only happen once, customers on bundles will face 'unbundling costs' and the evidence suggests that customers on bundles are

³⁹⁹ See [129-132], above.

⁴⁰⁰ The Applications at 2.

⁴⁰¹ [] provided under the cover of a letter from Bell Gully (on behalf of Vodafone) to the Commerce Commission (19 August 2016) at 3.

⁴⁰² Ibid at 7.

likely to be much stickier than those that are not. Rival TSPs will have to provide greater inducements and invest in greater promotional efforts to win back customers in the future.

335. The Applicants note that video content is being increasingly delivered to consumers using both fixed and mobile networks.⁴⁰³ Vodafone has, however, submitted that [].⁴⁰⁴
336. Nevertheless, []. Consistent with this, Sky CEO John Fellet stated in February 2016 that “[l]ike most traditional pay-television companies, we are losing traditional satellite customers, but gaining in our online products like Neon and FanPass.”⁴⁰⁵ []⁴⁰⁶
337. We consider conflicting evidence such as this in more detail in a later section discussing the likelihood of switching.⁴⁰⁷ However, we note that the clearance test that we must apply is forward-looking. Evidence of past behaviour, while it can be useful, is not necessarily determinative of the behaviour of a newly integrated pay TV/telecommunications services provider, or consumers and rival TSPs, in markets undergoing significant and rapid change.
338. We have concluded that the historical evidence before us does not support a conclusion that there is no likelihood of the newly merged entity leveraging its market power over premium live sports content to substantially lessen competition in the relevant broadband and mobile services markets. The market conditions and evidence of evolving consumer preferences that we have described above lead us to conclude that we cannot exclude a real chance that it would do so.
339. Finally, we consider that the same factors discussed above would provide the merged entity with the ability and incentive to restrict wholesale access by rival TSPs to terms not favourable enough to enable them to compete with bundles offered by the merged entity. We have had close regard to evidence provided to us about historical wholesale relationships, the take-up of bundles containing Sky Sport and submissions as to whether it is necessary for TSPs to offer Sky Sport in order to compete in the relevant broadband and mobile services markets. We also examine this evidence more closely in our discussion of the likelihood of switching that

⁴⁰³ The Applications at [4.4].

⁴⁰⁴ Submission from Vodafone to the Commerce Commission (11 November 2016) at 17.

⁴⁰⁵ <https://www.nbr.co.nz/article/sky-tv-first-half-profit-falls-58-competition-drives-content-costs-b-185435>.

⁴⁰⁶ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (5 August 2016), [] provided under the cover of an e-mail from Buddle Findlay (on behalf of Sky) to the Commerce Commission (22 September 2016) and [] provided under the cover of an e-mail from Buddle Findlay (on behalf of Sky) to the Commerce Commission (26 September 2016).

⁴⁰⁷ See [390-393], below.

follows. Again we note our view that not all evidence of past or present conduct or events provides a reliable predictor of future given the context in which the proposed merger would take place.

340. In summary, we consider that a number of factors prevent us from excluding a real chance that the merged entity would have the ability and the incentive to encourage customers to take up their services by rendering standalone Sky Sport significantly less attractive on a standalone basis and restricting rival TSPs' access to content that they need to effectively compete:
- 340.1 it will have control over premium live sports content, with associated market power;
 - 340.2 the merged entity would have different incentives to each of the Applicants in the counterfactual and would seek to maximise profits across both its pay TV and telecommunications services businesses;
 - 340.3 reduced transaction costs associated with the merged entity would facilitate new integrated products being available more quickly;
 - 340.4 technology and consumer preferences are converging across broadcasting and telecommunications services;
 - 340.5 the UFB rollout provides a re-contracting opportunity for the merged entity to capture market share with offers that rival TSPs are unable to match, since they lack access to premium live sports content; and
 - 340.6 once customers switch, they are likely to become stickier and be less contestable to rival TSPs in the future.

What would the merged entity's bundles look like?

341. We have concluded that the merged entity would control premium live sports content post-merger and that there are no close substitutes for that content for those who subscribe to it. The merged entity would have both the incentive and the ability to offer bundles that maximise the opportunities presented by converging technologies, improving service delivery in the form of UFB (and 5G when it arrives) and changing consumer preferences. It would be likely to have both the incentive and ability to make its bundles relatively more attractive than customers would be able to otherwise acquire, either by acquiring standalone Sky Sport alongside broadband and/or mobile services supplied by a rival TSP, or by acquiring a bundle offered by a rival TSP.
342. It is difficult to predict exactly how much more attractive to consumers the merged entity's bundles would prove to be. This will depend on the incentives faced by the merged entity. We set out our assessment below of why we cannot exclude a real chance that these bundles would induce a significant number of customers of rival TSPs to switch to the merged entity.

343. The merged entity would want to maximise profits by maximising additional margins from bundles across its pay TV, broadband and mobile telecommunications services businesses, and minimising any foregone margins from sales of standalone pay TV services.
344. The attractiveness of the bundle offered by the merged entity would depend on a number of factors:
- 344.1 it would depend in part, on technical considerations and the synergies that eventuate from the merger;
- 344.2 importantly, it would also depend on how the merged entity would perceive the expected reaction of consumers in both the short and long run; and
- 344.3 the assessment of the expected reaction of consumers would itself depend on the details of how particular bundles are structured and marketed.
345. There is a real chance that the merged entity would be incentivised to sacrifice short term margins for long term gain, if it expected bundled customers to be stickier and rival TSPs to be unable to constrain a subsequent increase in prices or reduction in quality.
346. As discussed in the ‘factual’ section, above, there is significant uncertainty about the features of the merged entity’s bundled offerings. The Applicants advised us that they had not had detailed conversations about how their products and services would be bundled and so were unable to provide significant detail in this regard.⁴⁰⁸
347. Nevertheless, as described above at [224-226], the Applicants’ submissions and internal documents described a range of potential options and third parties also suggested some features, [], that might be expected in bundles offered by the merged entity.
348. As discussed above,⁴⁰⁹
[]
349. A number of third parties submitted concerns that the merged entity would offer bundles containing Sky that rival TSPs would be unable to match.⁴¹⁰ They suggested that recent offers that Vodafone has made (eg, offering Sky Sport free for 12 months

⁴⁰⁸ Commerce Commission interview with Sky (14 July 2016) and Commerce Commission interview with Vodafone (21 July 2016).

⁴⁰⁹ At [225].

⁴¹⁰ For example,
[]

].

to its customers) may be indicative of the offers that the merged entity would make, at an even greater discount.⁴¹¹

350. Sky submitted that offering bundles at a heavy discount to the price of buying Sky TV on a standalone basis would result in the certain loss of high margin customers, for the uncertain gain of low margin customers.⁴¹²
351. Plum, on behalf of 2degrees and TVNZ, submitted that as data usage increases and mobile operators are forced to either charge more for data and/or introduce more stringent data caps, it is likely that Vodafone will choose to 'zero rate' Sky TV data.⁴¹³ Evidence of this practice overseas suggests that there is a real chance of it occurring here. Trustpower, Blue Reach and InternetNZ noted that [],⁴¹⁴ and we note that Optus does this for its EPL coverage in Australia. InternetNZ submitted that the merged entity would have the ability and incentive to do this in New Zealand post-merger.⁴¹⁵
352. Even without discounting, demand for bundles would be likely to increase in future if the merged entity significantly improves the quality of its bundles and/or if consumer preferences shift towards them for other reasons (eg, if consumer preferences for an integrated bundled products such as quad play becomes more established in New Zealand).
353. With discounting, there is a real chance that the merged entity would see opportunities to drive even wider uptake of bundles than has previously been seen, particularly in the context of the UFB rollout, when more consumers are in play. With significantly improved bundles, the discounts and profit sacrifice required may not be very large, and if the absolute price and quality of Sky Sport on a standalone basis remains unchanged then the merged entity may not lose customers. The merged entity would be able to recoup any profits immediately sacrificed due to discounting through reduced churn costs and by raising prices later when asymmetries in consumer switching behaviour makes these bundled customers less likely to switch back to rival TSPs.
354. Accordingly, we consider it is likely that the merged entity would make bundled offers that are attractive, compared to standalone Sky Sport offers, to a large group of Sky Sport customers who are not also currently customers of Vodafone. Just how

⁴¹¹ For example, Spark suggested that Vodafone's offer of free Sky TV that followed shortly after the announcement of the proposed merger [], and submitted that it expects that the merged entity would further incentivise customers to switch to bundles. Submission from Spark to the Commerce Commission (12 August 2016) at [85-87].

[

]

⁴¹² Letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (9 September 2016) at [70].

⁴¹³ That is, not charge users for the data used to watch Sky TV on its mobile network. Report from Plum (on behalf of 2degrees and TVNZ) to the Commerce Commission (12 August 2016) at 37.

⁴¹⁴ Submission from InternetNZ to the Commerce Commission (17 August 2016) at [2.12(c)], submission from Trustpower to the Commerce Commission (11 November 2016) at [7.9], and submission from Trustpower, Blue Reach and InternetNZ to the Commerce Commission (11 November 2016) at [7.6].

⁴¹⁵ Submission from InternetNZ to the Commerce Commission (17 August 2016) at [2.12(c)].

attractive these offers are likely to be is difficult to predict, as it depends on a number of variables and expectations. In the short term, these offers are likely to be pro-competitive, but in the long term we cannot rule out a real chance that they would result in a substantial lessening of competition if there is substantial customer foreclosure and a diminished ability and incentive for rival TSPs to respond. We discuss the reasons for this conclusion in the next section.

These new bundles are likely to be pro-competitive in the short term

355. The Applicants submitted, and we accept, that the merger would be likely to deliver benefits to consumers in the short term, taking the form of new and innovative products⁴¹⁶ and lower prices⁴¹⁷ being offered by both the merged entity and competitors compared with the counterfactual.
356. Differentiated bundled competition also would provide benefits to consumers in the short term. Those that value Sky Sport would be able to purchase bundles containing this content at a lower price, and/or higher quality, while consumers that do not value Sky Sport (or do not value it as highly as other services) would also benefit from this competition, as rival TSPs offer alternative content or other non-content offers (such as lower prices, more data, bundled hardware or other services) in an effort to win these customers.

Bundling could be harmful in the medium to long term

357. Notwithstanding that there may be benefits in the short term, we cannot exclude a real chance that the medium to long term reveals a substantial lessening of competition.
358. This is because, as noted above, we cannot predict with confidence what bundles the merged entity would offer, and on what terms. This makes it difficult to predict with any certainty what effects might occur in the medium to long term.
359. This assessment is made more difficult by the fact that significant changes are taking place in the relevant telecommunications markets, including the roll-out of UFB and the associated opportunity for TSPs to win broadband customers, changing consumer preferences to view content over the internet, and convergence of broadband and mobile services markets with each other, and with pay TV. Assessing how these changes would affect consumer behaviour in response to the merged entity's bundles, and how rival TSPs would be likely to respond, is challenging and involves dealing with a considerable degree of uncertainty.
360. Over the medium to long term, if the merged entity is able to capture Sky Sport customers such that the size of the effectively contestable broadband and/or mobile services markets is significantly reduced, then this could result in rival TSPs losing scale, or failing to achieve scale. This could, in turn, reduce their incentives to invest and innovate and hence reduce the competitive constraint on the merged entity.

⁴¹⁶ The Applications at 2.

⁴¹⁷ Commerce Commission interview with Sky (14 July 2016).

361. We explore whether these medium to long term effects are likely to arise and, if so, if they are likely to give rise to a substantial lessening of competition in either or both of the relevant broadband and mobile services markets, in the remainder of this Determination.

Whether a significant number of customers would switch to the merged entity

362. As discussed above, we cannot rule out a real chance that the merged entity:

362.1 would retain the rights to its New Zealand premium live sports content in the medium to long term, for which a significant group of consumers have no close substitutes; and

362.2 would have the ability and incentive to offer premium live sports content in bundles that are more attractive than acquiring this content on a standalone basis. However, the extent of the difference is difficult to predict, given the number and complexity of the underlying variables involved.

363. We now turn to consider whether a significant number of customers of rival TSPs would be likely to switch to the merged entity's bundles. If a large enough number of customers switch and are then foreclosed to rival TSPs, then this could impact their competitiveness, and substantially lessen competition, in the medium to long term.

Broadband services market: would a significant number of customers be likely to switch?

Applicants' submissions

364. The Applicants' submitted that levels of switching in response to bundles have, in the past, been low.

365. Vodafone submitted
[

].⁴¹⁸ This is shown in Figure 14.

[

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Source: Vodafone

366. Further, Vodafone submitted that the Applicants' own assessment of the impact of the proposed merger shows that only a small increase in market share is expected – an increase in consumer broadband and mobile services market shares of only a few percentage points by FY19/20.⁴¹⁹ Vodafone submitted that these estimates can be

⁴¹⁸ Letter from Bell Gully (on behalf of Vodafone) to the Commerce Commission (18 October 2016) at 2-3 and submission from Vodafone to the Commerce Commission (11 November 2016) at 21-22.

⁴¹⁹ Submission from Vodafone to the Commerce Commission (10 October 2016) at [4.8].

Zealand's UFB roll-out, and therefore Singapore is a bellwether for what could occur in New Zealand.⁴²⁷

371. Plum also submitted that growth in multi play bundle take-up is strongest in countries with highly developed cable networks. Plum submitted that high take-up rates of bundles in Singapore are a bellwether for similar market developments in New Zealand, given this high take-up is likely to have been facilitated by the widespread availability of high speed broadband and a structurally separated industry.⁴²⁸

The evidence

372. On the basis of the evidence before us, we have been unable to rule out the real chance that, as a result of the proposed merger, a significant number of the approximately []%⁴²⁹ of broadband customers of rival TSPs that are Sky Sport subscribers would be likely to switch to the merged entity.
373. In coming to this view we considered:
- 373.1 evidence of historic switching;
 - 373.2 consumer surveys;
 - 373.3 evidence of switching in other jurisdictions in response to an increase in triple play bundling; and
 - 373.4 the Applicants' and third parties' submissions and evidence.
374. We also had regard to the current and future significant changes occurring in the relevant broadband services market, described above in the industry background and earlier in the competition analysis sections.
375. The relationship synergies presented by the proposed merger, converging technologies and consumer preferences, the roll-out of UFB and the likelihood of more attractive bundles being offered by the merged entity in the future all provide context for the assessment of other evidence.
376. We consider evidence of past and current switching, before turning to consider what switching may occur in the future.

Evidence of historic switching

377. As noted above, Vodafone submitted that [].

⁴²⁷ Report from Plum (on behalf of 2degrees and TVNZ) to the Commerce Commission (12 August 2016) at 17.

⁴²⁸ Ibid at 17.

⁴²⁹ See [284], above, for how we calculated this figure.

378. We attempted to gauge whether Vodafone’s Sky promotions have had any clear effects on market shares, taking into account the wider market context. To do this, we obtained data on promotions and monthly customer movements from Vodafone and its large TSP rivals – Spark, Trustpower, Vocus and 2degrees – since January 2014.
379. Figure 15, below, shows the total number of promotions run by Vodafone and each of these TSPs over the same period. There is a separate line for each TSP showing the aggregate number of promotions.⁴³⁰ The figure also shows the periods over which Vodafone ran Sky promotions (grey shaded areas).⁴³¹

Figure 15: Broadband TSP promotions (January 2014 – July 2016)

[]

Source: Commerce Commission analysis of data from TSPs.

380. Figures 16 and 17 below show trends in TSPs’ net monthly customer gains during the last three years.

Figure 16: Broadband TSP customer gains (January 2015 – July 2016)

[]

Source: Commerce Commission analysis of data from TSPs.

Figure 17: Vodafone broadband customer gains (January 2014 – July 2016)

[]

Source: Commerce Commission analysis of data from TSPs.

381. []
382. [] The impact of particular promotions will depend on their terms and conditions, how they are promoted and consumer awareness. We had insufficient evidence available to us to control for those influences. Furthermore, the overall offer, not just promotions, will be important to consumers. []
383. Similarly, it is difficult to make reliable predictions about the likely rates of switching in the future [] from historic bundles offered by Vodafone. Issues that may have impacted [] take-up of Vodafone’s Sky promotional bundles are set out below.

⁴³⁰ The chart does not reflect the relative value of the promotions but merely counts them.

⁴³¹ Further detail on Vodafone and rival TSPs’ promotions are set out at **Attachment A**.

383.1 The bundles are relatively basic: they are a combination of two products for a price discount only and necessarily did not include new and innovative features that are anticipated being developed post-merger.

383.2 The bundles have been on a resale/referral basis only and so are not a truly integrated product offering.

383.2.1 Vodafone and Sky's promotional activity has not been coordinated. Post-merger, the merged entity would be able to coordinate promotions to reduce 'cannibalisation' of customers (ie, promotions of the merged entity competing for the same customers).

383.2.2 Sky advised that, currently,
[
].⁴³² This would be overcome with synergies and reduced transaction costs and the changed incentives of the merged entity.

383.3 The bundles were offered in the context of standalone offers.

383.4 Vodafone's previous Sky bundled offerings have been time limited (eg, 'free Sky Sport for 6 months'). After this time, subscribers need to pay full price for the promoted service or discontinue their subscription. Post-merger, we cannot rule out the real chance that the merged entity would have the incentive to offer bundles with more durable discounts or new features than have historically been the case, which would entice higher levels of switching.

383.5 Vodafone has only offered bundles containing Sky and its broadband services (not its mobile services) in the past.

384. Consumer preferences are, to some degree, linked to changing technology.

384.1 As noted above, the roll-out of UFB presents a significant opportunity for TSPs to win customers, and more customers will be in play.

384.2 As UFB is rolled out and pay TV and broadband services converge (as Sky Sport is increasingly watched over broadband), consumer attitudes are likely to shift as they associate pay TV and broadband more closely, and so too their attitudes towards bundling are likely to shift.

384.3 [
]⁴³³

⁴³² Commerce Commission interview with Sky (14 July 2016).

⁴³³

[
] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (29 July 2016).

[
]

384.4 As the cost of viewing content on mobile networks decreases (as per the trend to date), this may also stimulate consumer demand to watch more content over broadband.

384.5 Post-merger, as discussed above, the bundles are likely to have added features that would affect how consumers value them. For example, Sky Sport may be zero rated on mobile, making it cheaper for the merged entity's customers to watch content on the go.

Consumer surveys

385. We reviewed a number of consumer surveys provided by the Applicants, and third parties, which relate to how important content is for purchasing decisions in telecommunications services markets. For example:

385.1 []⁴³⁴
[]
];

385.2 []⁴³⁵

385.2.1 []
]; and

385.2.2 []
];

385.3 []⁴³⁶

⁴³⁴ Submission from Vodafone to the Commerce Commission (10 October 2016) at 6.

⁴³⁵ Ibid at 7.

⁴³⁶ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (29 July 2016) at 11-12.

385.4 []
⁴³⁷
 []
]; and

385.5 []
⁴³⁸
 [⁴³⁹]
].

386. While the above results suggest that, historically, [], it is, again, difficult to make reliable predictions about the likely rates of switching in the future based on these survey results.

386.1 The responses were provided in the context of the bundled offers that existed at the time of the survey, and not the merged entity’s improved bundled offerings. As discussed above, and as accepted by the Applicants, the merged entity’s bundles are likely to be more attractive than have been offered in the past.

386.2 The responses were provided in the context of Sky TV (including Sky Sport) being available on a standalone basis on comparable terms to acquiring it in a bundle. We have concluded that we cannot rule out a real chance that the merged entity would have the ability and incentive to make Sky Sport less attractive on a standalone basis post-merger.

386.3 As discussed above, the pay TV and telecommunications markets are converging, and as consumers increasingly view content over broadband and mobile networks, their preferences are likely to change.

386.4 The consumption of content over broadband and mobile networks has been accelerating, which suggests that these modes of delivery are becoming more important to consumers. As this trend continues, the importance of content to competition in relevant telecommunications markets is also likely to increase (especially as broadband and mobile services become more closely aligned with the delivery of content).

⁴³⁷ [] provided under the cover of an e-mail from 2degrees to the Commerce Commission (9 December 2016).

⁴³⁸ [] provided under the cover of an e-mail from 2degrees to the Commerce Commission (9 December 2016).

⁴³⁹ []

386.5 The responses are based on past preferences, which may not reflect future preferences (especially given the trends towards triple and quad play packages, and the potential for TSPs to zero rate mobile content use, which has happened in other jurisdictions).⁴⁴⁰

Switching in other jurisdictions

387. As set out in Figure 11, above,
[

]. The experience in other jurisdictions must also be considered in the context of New Zealand conditions. Low levels of historic take-up in other jurisdictions in the past does not establish that increased take-up is unlikely in New Zealand in the future.

388. New Zealand is different from many other countries, in that there is one broadcaster (Sky) that holds the rights to the vast majority of premium live sport, and there are no anti-siphoning or other laws mandating access to premium live sports content. This potentially makes the rights to these sports more valuable than elsewhere, and switching to the merged entity may be higher than might be expected elsewhere, given there would be only one provider of integrated broadband bundles containing premium live sports content.

389. Further, as noted above, the roll-out of UFB is expected to promote increased rates of switching in New Zealand, with approximately 1.1 million premises in play by 2019. Given this, and changing consumer preferences, we do not consider that historic rates of switching from other jurisdictions provide a reliable predictor of future switching in New Zealand.

Applicants' documents

390. Vodafone advised that it anticipated only modest rates of switching post-merger, and that its predictions can be relied on because it needs to make accurate and honest disclosures to the market.⁴⁴¹ However, we do not consider that these predictions mean that higher levels of switching post-merger are unlikely.

390.1 [

].⁴⁴² Nevertheless, these bundle features are a key aspect of the Applicants' rationale for the proposed merger and we have concluded that there is a real chance that it would have the ability and incentive to offer more attractive bundles.

⁴⁴⁰ For example, Vodafone Ireland has zero rated live sports content, and Optus in Australia zero rates its coverage of the EPL over its broadband and mobile networks: Report from Plum (on behalf of 2degrees and TVNZ) to the Commerce Commission (12 August 2016) at 37 and <http://www.optus.com.au/shop/support/answer/how-is-premier-league-data-charged?requestType=NormalRequest&id=6990&typeld=5>, respectively.

⁴⁴¹ Submission from Vodafone to the Commerce Commission (10 October 2016) at [4.10].

⁴⁴² Submission from Vodafone to the Commerce Commission (11 November 2016) at 12.3].

390.2 [

] ⁴⁴³ A significant proportion of these customers are also likely to be Sky Sport subscribers. The customers that migrate to these bundles post-merger would then be less likely to churn to rival TSPs (because the customers would become stickier).

390.3 [

] ⁴⁴⁴

[

]

391. The Applicants' internal documents also point in the direction of convergence and more bundling in the future. ⁴⁴⁵ As we have discussed previously, we consider that this is likely to drive increased switching.

391.1 [

] ⁴⁴⁶

[

]

⁴⁴³ See n422, above.

⁴⁴⁴ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (5 August 2016).

⁴⁴⁵ Vodafone submissions in other jurisdictions also suggest access to premium live sports content is very important.

⁴⁴⁶ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (12 August 2016) at 9.

391.2 []⁴⁴⁷

392. A number of documents prepared by, or on behalf of, the Applicants are consistent with an expectation that bundles of Sky’s and Vodafone’s products are likely to be attractive to consumers and so result in significant switching to which rival TSPs are unable to effectively respond.

392.1 []⁴⁴⁸

392.2 []⁴⁴⁹
 []⁴⁵⁰

392.3 []⁴⁵¹

392.4 []⁴⁵²

392.5 []⁴⁵³
 []

⁴⁴⁷ [] provided under the cover of a letter from Bell Gully (on behalf of Vodafone) to the Commerce Commission (29 July 2016) at 32.

⁴⁴⁸ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (29 July 2016) at 6.

⁴⁴⁹ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (29 July 2016) at 17.

⁴⁵⁰ Ibid at 33.

⁴⁵¹ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (12 August 2016) at 2.

⁴⁵² [] provided under the cover of a letter from Bell Gully (on behalf of Vodafone) to the Commerce Commission (29 July 2016) at 24.

⁴⁵³ [] provided under the cover of a letter from Bell Fully (on behalf of Vodafone) to the Commerce Commission (5 August 2016) at 43.

392.6 []⁴⁵⁴
 []

393. On the other hand,
 []⁴⁵⁵

Conclusion

394. We faced a range of challenges in assessing the extent to which the evidence before us provided a reliable predictor of the likely future impact of the merged entity's pay TV and broadband (and mobile) bundles.

395. The evidence before us provided some insight into the potential future impact of the merged entity's bundles. However, for the range of reasons described it did not positively persuade us one way or another as to how the proposed merger would impact the broadband services market, or the timeframe over which any impact might eventuate.

395.1 It is difficult to assess the effectiveness of Vodafone's Sky bundles to date. Although we discerned no clear effect on market shares, there are a range of reasons why this may have been the case. We consider that it is likely that bundles would be more attractive post-merger.

395.2 []

395.3 Overseas data shows various levels of multi play bundle take-up, but this does not provide a reliable predictor of the future in New Zealand for the reasons described above.

395.4 Finally, despite some submissions and evidence to the contrary, the Applicants' documents recognise the potential for significant customer switching. Indeed, these documents are consistent with expectations of changing consumer preferences.

396. The broadband services market is undergoing a period of significant change, and this is likely to persist into the future. In particular, the roll-out of UFB is expected to lead

⁴⁵⁴ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (12 August 2016) at 3 and 9.

⁴⁵⁵ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (29 July 2016) at 6.

to greater customer switching, and affect both consumer demand and TSP behaviour as more New Zealand households switch to high speed internet and are able to consume more content across multiple devices.

397. We have earlier considered in some detail evidence of the relationship synergies presented by the proposed merger, converging technologies and consumer preferences, the roll-out of UFB and the likelihood of more attractive bundles being offered in the future by the merged entity. This context renders more uncertain the reliability of evidence of past or present conduct or events as a predictor of likely future impact.

397.1 The Applicants have identified opportunities to provide consumers with more attractive bundles,⁴⁵⁶ and we consider it likely that this will result in increased switching.

397.2 []⁴⁵⁷

[]

397.3 As the Applicants recognise, the roll-out of UFB is likely to provide a significant opportunity for TSPs to win customers. In particular, the merged entity is likely to be in a strong position to attract Sky Sport subscribers to its bundled offerings using premium live sports content that only it would possess.

397.4 As telecommunications and broadcast services continue to converge, it is likely that consumers will continue to consume ever increasing amounts of content over broadband (and mobile) networks, which will further enhance the attractiveness of the merged entity's bundles.

397.5 To the extent that the merged entity's bundles are relatively lower priced than the bundles that would prevail in the counterfactual (taking into account differences in quality), the merged entity is also likely to be able to attract additional customers not currently subscribed to Sky Sport. By definition, these additional customers would be marginal, however they would nevertheless be less likely to churn, given that they would be purchasing a bundle, rather than a standalone service.

397.6 Given that bundled customers that have UFB would be less likely to switch, we cannot exclude the real chance that a significant proportion of customers who switched to the merged entity's bundles would remain with the merged

⁴⁵⁶ The Applications at 2.

⁴⁵⁷ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (29 July 2016) at 3.

entity in future, even after the merged entity raises prices and/or decreases quality.

398. While we accept that some broadband customers, particularly those that do not subscribe to Sky Sport, would be likely to switch from the merged entity to rival TSPs in response to differentiated bundled offers timed with the roll-out of UFB, we cannot exclude the real chance that a significant proportion of the []% of rival TSPs' customers that subscribe to Sky Sport would be likely to switch to the merged entity and would effectively be foreclosed to competition from rival TSPs.
399. Assessing in the round all of the evidence relevant to the likelihood of switching in the broadband services market, we cannot exclude the real chance that a significant proportion of the []% of rival TSPs' broadband customers that subscribe to Sky Sport would be likely to switch to the merged entity.

Mobile services market: would a significant number of customers be likely to switch?

Applicants' submissions

400. Vodafone submitted that content is not a major driver of sales of mobile plans;⁴⁵⁸ rather sales are driven by price, handsets and data allowances.⁴⁵⁹ This, it submitted, is illustrated by 2degrees, which has grown swiftly in the market through the use of strong marketing and attractive offers.⁴⁶⁰
401. Vodafone submitted that,
[
].⁴⁶¹
402. To the extent that the merged entity offered highlights or interview content to its customers for viewing on mobile devices, Vodafone submitted that these would be unlikely to drive consumer demand since such content is not live.⁴⁶²
403. Vodafone accepted that there has been an increase in consumption of data over mobile networks. However, it submitted that Sky content has not been a material driver of this increase, and would not be in future.⁴⁶³ Vodafone provided charts showing that:
- 403.1 []
- 403.2 []

⁴⁵⁸ Submission from Vodafone to the Commerce Commission (11 November 2016) at [14.1].

⁴⁵⁹ Ibid at [14.1].

⁴⁶⁰ Ibid at [14.1].

⁴⁶¹ Ibid at [14.2].

⁴⁶² Ibid at [14.4].

⁴⁶³ Ibid at 25-26.

404. Vodafone submitted that, although it offers mobile packages that include live sports content in other countries, [].⁴⁶⁴

404.1 [

404.2

404.3

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405. []⁴⁶⁵

406. []⁴⁶⁶

407. In our view, these statements indicate that the Applicants view live sports content viewing on mobile as likely to increase in the future and, more importantly, that offering bundles of premium live sports content would be likely to be attractive to a significant number of consumers.

⁴⁶⁴ E-mail from Bell Gully (on behalf of Vodafone) to the Commerce Commission (16 December 2016).

⁴⁶⁵ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (29 July 2016) at 33.

⁴⁶⁶ [] provided under the cover of a letter from Bell Gully (on behalf of Vodafone) to the Commerce Commission (29 July 2016) at 12.

Third party submissions

408. Spark submitted that viewing live sport on mobile is “the next big trend”.⁴⁶⁷ Spark referred to overseas analyses that indicated an increase in the consumption of video on mobile devices. For example, Spark highlighted the following reports:

408.1 A Cisco report dated February 2016 estimating that by 2020 “three-fourths of the world’s mobile data traffic will be video”.⁴⁶⁸

408.2 An OOOYALA report dated January 2016 stating that, in the UK and Ireland, “more than 45% of sports viewing occurs on smartphones and tablets”.⁴⁶⁹

409. Spark noted that French mobile provider SFR⁴⁷⁰ has had success with its quad play offer, with 35% take-up.⁴⁷¹ It submitted that the reason for this strong uptake overseas is that TSPs are making it increasingly difficult to buy component products on a standalone basis. Spark submitted that the merged entity would engage in a similar strategy.⁴⁷²

410. Similarly, 2degrees submitted that

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The evidence

411. On the basis of the evidence before us, we have been unable to rule out the real chance that a significant number of the []%⁴⁷⁴ of mobile customers of rival TSPs that are Sky Sport subscribers would switch to the merged entity.

412. In coming to this view we considered:

412.1 consumer surveys;

412.2 evidence from other jurisdictions; and

412.3 the Applicants’ and third parties’ submissions and evidence (as set out above).

413. We also had regard to the current and future significant changes occurring in the relevant mobile services market, and the context this provides for the assessment of

⁴⁶⁷ Submission from Spark to the Commerce Commission (23 November 2016) at 9.

⁴⁶⁸ Cisco “Cisco Visual Networking Index: Global Mobile Data Traffic Forecast Update, 2015-2020 White Paper (3 February 2016) at 3.

⁴⁶⁹ OOOYALA “State of the Broadcast Industry 2016 – OTT Moves to Centre State” (6 January 2016) at 8.

⁴⁷⁰ Société Française du Radiotéléphone.

⁴⁷¹ Submission from Spark to the Commerce Commission (11 November 2016) at 17.

⁴⁷² Ibid.

⁴⁷³ Commerce Commission interview with 2degrees (3 August 2016).

⁴⁷⁴ See [284], above, for how we calculated this figure.

other evidence, as we did in our assessment of the relevant broadband services market.

414. We consider consumer survey evidence and evidence from overseas, before turning to consider what switching may occur in the future. Unlike in the relevant broadband services market, no TSP currently, or has in the past, bundled Sky content with mobile services.

Consumer surveys

415. We were provided with evidence from two surveys that touched on consumer preferences for quad play bundles (ie, those containing mobile services) in New Zealand.

415.1 []⁴⁷⁵
 []⁴⁷⁶
 []⁴⁷⁷

415.2 []⁴⁷⁸

Switching in other jurisdictions

416. We considered several studies and reports that related to the proportion of households that buy mobile services in a bundle.

416.1 An EU study found that on average 13% of households purchased a bundle of telecommunications services with mobile included.⁴⁷⁹ The countries with the highest levels of bundling mobile with another service (at least one of internet, pay TV or fixed voice) were: Luxembourg (35%); France (30%); Malta (28%). The study found that, on average, 5% of households had a bundle that included pay TV and mobile services.⁴⁸⁰

⁴⁷⁵ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (29 July 2016) at 102.

⁴⁷⁶ Ibid at 12.

⁴⁷⁷ Ibid at 101.

⁴⁷⁸ [] provided under the cover of an e-mail from 2degrees to the Commerce Commission (9 December 2016).

⁴⁷⁹ European Commission “E-Communications and Telecom Single Market Household Survey” (March 2014) at 68.

⁴⁸⁰ Ibid at 69. The figure of 5% includes all types of bundles that include mobile and television.

416.2 []⁴⁸¹

416.3 Plum and Ofcom data from 2016 indicates that approximately 3% of UK households purchase mobile bundles that contain internet or pay TV services.⁴⁸²

416.4 Another 2016 UK study by EY found that take-up of bundles containing mobile services is growing but from a low base: 2% of households had a bundle with mobile and pay TV services in 2013 and around 5% had one in 2016.⁴⁸³

416.5 A UK CMA report on the proposed merger between BT and EE in 2015 found that the proportion of households that have a bundle of mobile and another telecommunications service ranges from 2% (USA) to 36% (Spain).⁴⁸⁴ On average across the nine countries surveyed, the proportion of customers with a bundle that included mobile services was 3%.⁴⁸⁵ However, the study found that there was rapid growth in Spain and France of bundles that included mobile, where over 30% of households now have telecommunications bundles that include mobile.^{486 487}

417. In addition to the above, we note that in the UK, BT offers a BT Sport app that enables its broadband and mobile subscribers to replay footage, choose their own camera angles, access detailed statistics, connect to online communities, and take advantage of commercial offers.⁴⁸⁸ Subscribers can also watch sports on multiple screens and this viewing may be eligible for zero rating on its mobile network.⁴⁸⁹

⁴⁸¹ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (29 July 2016).

⁴⁸² Report from Plum (on behalf of 2degrees and TVNZ) to the Commerce Commission (12 August 2016) at 17-18.

⁴⁸³ EY "Navigating the Bundle Jungle" (2013), Chart 1 and EY "Navigating the Bundle Jungle" (2016) at 5.

⁴⁸⁴ CMA "BT Group / EE Merger Decision" (15 January 2016) at H2.

⁴⁸⁵ CMA "BT Group / EE Merger Decision" (15 January 2016) at H3.

⁴⁸⁶ Ibid at H4.

⁴⁸⁷ The CMA report refers to a 2013 report by Analysys Mason in 2013 found that the high take-up of fixed-mobile bundles in France and Spain was as a result of high mobile prices, which allowed fixed operators to offer significant discounts. This made bundles attractive to consumers, and the strong, converged operators were able to respond to aggressive competition by new entrants. Analysys Mason "Multi-play services in Europe: forecast and analysis 2012-2017" (Report on behalf of BT, 2013). A report by GSMA Intelligence found that the discounts were 30-40% of the standalone price. GSMA Intelligence "Convergence: repositioning in an expanding mobile ecosystem" (November 2015).

⁴⁸⁸ BT Sport product description, available at <http://sport.bt.com/watch-now/programmes/download-the-bt-sport-app-for-your-device-S11363860641475>.

⁴⁸⁹ BT Sport terms and conditions summary, available at <https://www.productsandservices.bt.com/mobile/sport/>.

418. Despite these attractions, uptake of BT Sport bundles appears to have been modest. As noted above only around 3-5% (depending on the survey) of UK consumers have taken up bundles that include both mobile and pay TV services.⁴⁹⁰
419. However, historic uptake of bundles in the UK, and in other overseas jurisdictions, may not be a reliable guide to future uptake in New Zealand.
- 419.1 Although football has a similar status in the UK as rugby has in New Zealand, the supply of pay TV and telecommunications services in the UK is quite different to New Zealand. Due to anti-siphoning laws, UK football fans can access some marquee matches on FTA TV, potentially diminishing demand for pay TV, whether standalone or in bundles.⁴⁹¹
- 419.2 UK consumers may also find providers' bundles relatively unattractive since they can effectively construct a bundle by buying standalone services to their particular tastes. This is now assisted by the fact that there are multiple sources of live football: Sky, BT Sports and FTA. New Zealand consumers do not have such wide opportunities.
- 419.3 As discussed above, consumers' preferences are changing as an increasing amount of content is being consumed on mobile networks. The Applicants appear to recognise that more viewing of live sports on mobile networks is likely to occur post-merger.
- 419.4 Finally, there are indications that 5G technology will be deployed in New Zealand within the next five years. This is likely to result in better and faster content viewing on mobile at cheaper prices and would represent a significant opportunity to attract more customers to bundles.⁴⁹²

Current and future significant changes to the market

420. As set out earlier, the mobile services market is going through a period of significant change. The amount of data – both paid and free – being consumed over mobile networks has been doubling year on year (see Figure 8 above).
421. This is true for both entertainment and sports content. Although we do not have data on the consumption of sport over mobile,
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⁴⁹⁰ Ofcom, Communications Market Report 2016, at 13. Available at <https://www.ofcom.org.uk/research-and-data/cmr/cmr16/the-communications-market-report-uk>. Nevertheless, the Applicants' documents indicate that they consider sport on mobile to be a "proven proposition" in the UK. See [224], above.

⁴⁹¹ Report from Plum (on behalf of 2degrees and TVNZ) to the Commerce Commission (12 August 2016) at 50.

⁴⁹² Blue Reach submitted that the overall network cost of 5G is expected to be lower than older technologies because cell sites will be able to use existing infrastructure such as power poles and multi-story buildings, rather than purpose-built cell towers. Blue Reach submission to the Commerce Commission (10 November 2016) at 6.

422. New technology, such as 5G, is expected to make viewing content over mobile less expensive, and content quality can be expected to improve. As discussed above, this may also represent a significant opportunity for TSPs to win customers.
423. These factors suggest that content will be increasingly viewed over mobile networks in the future. On the basis of the evidence that we have, we consider that this increased mobile viewing usage would be likely to include premium live sports content.

Analysis of the evidence

424. Based on the evidence before us, we have been unable to rule out a real chance that a significant proportion of the approximately []% of Sky Sport customers that are mobile customers of rival TSPs would be likely to switch to the merged entity.
425. The survey data from New Zealand and overseas, as well as the evidence of overseas rates of switching to bundles, was of limited assistance. However, it did indicate that there is a trend towards increased bundling of pay TV and telecommunications services take-up by consumers.
426. Post-merger, a bundle of pay TV (including premium live sports content) and mobile would be attractive to consumers in two ways.
- 426.1 First, if the bundle is less expensive than purchasing premium live sports content and mobile services separately.
- 426.2 Second, if consumer behaviour changes in response to new and exclusive features such that more content is being viewed on mobile networks. This is more likely to evolve over the medium to long term, and influenced by factors such as developments in mobile technology (eg, mobile devices trending towards bigger screens) and the convergence of the pay TV and mobile services markets that we have described previously.
427. As to the first consideration, the merged entity could attract mobile as well as broadband services customers that subscribe to Sky Sport by offering a discount on the bundle. This would also give these consumers the optionality of watching live sports content on mobile (even if watching live sports content on mobile is not prevalent in the short term). Further, as the merged entity seeks to take advantage of the roll-out of UFB and attract broadband services customers, it could use this opportunity to also entice consumers to switch mobile accounts at the same time.
428. It is difficult to know how many mobile customers might switch to take up the merged entity's bundles. However, if the merged entity is able to entice at least one mobile account in each household with a Sky Sport subscription to switch to Vodafone, Spark and 2degrees could together lose around [] mobile connections or around []% of their consumer connections in aggregate.⁴⁹³

⁴⁹³

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429. As to consumer preferences, we accept that content may not have been a major driver of mobile subscriptions in the past, and that Sky’s premium live sports content has not, to date, been a major driver of increased data usage on mobile networks. We also accept that Sky Sport content may not be viewed as much as other content (although we note that much of this content, such as Facebook and YouTube, is ‘free’ in the sense that there are no charges, other than for data usage).
430. However, there are indications that consumers are viewing content in new and different ways.
[
] As mobile prices continue to fall, and as technology improves, we consider that it is likely that more people will view content over mobile, including premium live sports content.
431. This trend could accelerate post-merger, depending on the features and prices of the merged entity’s bundles. For example, if Sky Sport was zero rated on mobile, we consider that this would be very attractive for consumers. Further, specific mobile apps that take advantage of the synergies of the proposed merger (such as the product development opportunities we identified earlier) would also be like to drive increased viewing over mobile networks.
432. Therefore, over the medium to long term, the likely increased viewing of live sports content over mobile means that consumer preferences will evolve, and that more customers would be attracted to the merged entity’s bundles.
433. A number of internal documents recognise these opportunities.
- 433.1 As discussed in the factual section, above,
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- 433.2 [

] ⁴⁹⁴
- 433.3 [

] ⁴⁹⁵

⁴⁹⁴ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (29 July 2016) at [4.3].

⁴⁹⁵ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (29 July 2016) at 33.

434. This suggests that the impact in the mobile services market may be more likely to be felt over the medium to long term, rather than in the short term.
435. We considered this evidence in the context of the current and future significant changes occurring in the relevant mobile services market, and concluded that we could not exclude a real chance of a significant proportion of the []% of rival TSPs mobile services customers that are Sky Sport subscribers switching to the merged entity's bundled offerings.

Broadband: would rival TSPs rendered competitively less effective?

436. To this point, we have found:

436.1 the merged entity would be likely to have control of premium live sports content, for which there are no close substitutes for a significant number of consumers. This is likely to persist in the medium to long term;

436.2 we cannot exclude a real chance that the merged entity would offer bundles of premium live sports content with broadband and mobile services, on terms (price and quality) that are significantly more attractive to Sky Sport subscribers than would be available from a rival TSPs or to consumers on a standalone basis; and

436.3 that we cannot exclude a real chance that a significant number of broadband and mobile consumers would switch to the merged entity.

437. Next we consider whether the loss of a significant proportion of the []% of broadband customers of rival TSPs that are Sky Sport subscribers:

437.1 would be likely to render any rival TSP less competitively effective; and, if so

437.2 whether this would be likely to lead to a substantial lessening of competition.

What is a 'significant' number of broadband customers?

438. We sought to define what a 'significant' number should be for the purposes of analysing the impact of switching on rival TSPs.

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439. Applying this result to the []% of non-Vodafone broadband customers that are also Sky Sport customers implies potential switching of up to []% of non-Vodafone customers.⁴⁹⁷ However, it is unclear whether interviewees' responses to this survey

⁴⁹⁶ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (12 August 2016) at 9.

⁴⁹⁷ Being []% of the []% of Sky (including Sky Sport) subscribers. This is a conservative approach, given that it does not account for the possibility that others may switch as well; that is, Sky subscribers that do not currently subscribe to Sky Sport and the []% of non-Sky customers that would consider switching.

were given in the context of considering whether to switch TSPs. On a conservative basis, we therefore adopted a range of between []%, reflecting the possibility that the survey may overstate the amount of potential switching by Sky Sport customers.

440. On the other hand, there is some evidence to suggest that this level of switching may underestimate the impact on rivals. This is because there is some evidence that Sky Sport subscribers, and those likely to switch to the merged entity, are higher ARPU telecommunications customers than non-Sky customers. The loss of higher ARPU customers has a greater impact on a TSP than the loss of a lower ARPU customer.

441. Spark submitted data indicating that [].⁴⁹⁸

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Source: Spark.

Notes: [].

442. []⁴⁹⁹

443. However, NERA, on behalf of Vodafone, submitted that Sky subscribers are not likely to be particularly high ARPU.⁵⁰⁰ NERA submitted that:

443.1 Sky subscribers, including Sky Sport subscribers, come from a wide range of demographics and have a wide range of income levels; and

443.2 Vodafone customers, across all demographics, who subscribe to Sky TV, are less likely to purchase higher-priced unlimited broadband packages.

444. We note that NERA’s submission, while it is consistent with the claim that Sky TV subscribers are not higher ARPU customers, does not include details of how much Vodafone customers with a Sky TV subscription actually spend on broadband

⁴⁹⁸ [] attached to an e-mail from Spark to the Commission (16 December 2016).

⁴⁹⁹

[]

⁵⁰⁰ Report from NERA on behalf of the Applicants (24 November 2016) at [16-25].

services. On the other hand, the survey evidence from Spark does relate to actual ARPU spend.

445. Next, we examined whether this level of market switching would affect rival TSPs in different ways (ie, whether some TSPs had a higher or lower percentage of broadband customers that were also Sky Sport subscribers).
446. None of the TSPs that we spoke with were able to provide definitive data on the number of customers that subscribe to Sky Sport. However, each provided estimates.

446.1 Spark

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446.2 Vocus

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446.3 [

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446.4 Trustpower [

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446.5 [

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⁵⁰¹ Submission from Spark to the Commerce Commission (5 October 2016) at 32-33.

⁵⁰² Commerce Commission interview with Spark (19 December 2016).

⁵⁰³ E-mail from Vocus to the Commerce Commission (4 October 2016).

⁵⁰⁴ Commerce Commission interview with Vocus (14 December 2016).

⁵⁰⁵ E-mail from Trustpower to the Commerce Commission (23 September 2016).

⁵⁰⁶ Commerce Commission interview with Trustpower (13 December 2016).

submitted that fixed network access is purchased on regulated terms from Chorus on a variable base, which means that entry and expansion is not difficult. It further submitted that other components, such as national and international backhaul, are provided in competitive markets and so there is no need for TSPs to invest in their own infrastructure.⁵¹⁰

452. Vodafone submitted that a lack of required scale economies is reflected by the large number of broadband suppliers (over 80) of different sizes competing in the market.⁵¹¹ Vodafone provided data on the service plans that the different TSPs offer, which it submitted showed price competitiveness, and did not appear to be linked to scale.⁵¹²

453. The Applicants also provided an analysis by NERA that assesses the variable costs involved in supplying fixed broadband.⁵¹³ NERA submitted that even if it was profitable for the merged entity to foreclose rivals, there would only be a competition problem if:⁵¹⁴

453.1 the conduct undermined the competitiveness of its rivals; and

453.2 the merged entity was then able to exercise market power.

454. NERA advised that if consumers were attracted to the merged entity's discounts, then they would equally revert back to other TSPs if those discounts were reversed.⁵¹⁵ If so, the merged entity would not be able to exercise market power.

455. NERA also provided an analysis of Vodafone's costs of supplying broadband. According to the data, NERA submitted that:⁵¹⁶

455.1 The major recurring cost is that paid to Chorus, which is the same for TSPs regardless of size. For customers that purchase from Chorus on a wholesale basis, that charge is between \$41 and \$54 per customer per month depending on the type of broadband. TSPs that only use Chorus' local loop pay \$30 per customer.

455.2 The costs that can vary with scale are: bandwidth costs; co-location costs; and a one-off cost for a modem of \$91-\$180. NERA calculates that, spreading those costs over a year, this equates to around \$[] per customer per month. This compares to a typical ARPU of a broadband customer of \$[] per month.

⁵⁰⁹ Submission from Vodafone to the Commerce Commission (10 October 2016) at [1.2(e)].

⁵¹⁰ Submission from Vodafone to the Commerce Commission (11 November 2016) at 29.

⁵¹¹ Submission from Vodafone to the Commerce Commission (10 October 2016) at [7.2-7.10].

⁵¹² Ibid at 15 and Annexure 1.

⁵¹³ Report from NERA on behalf of the Applicants (10 October 2016).

⁵¹⁴ Ibid at [29].

⁵¹⁵ Ibid at [30].

⁵¹⁶ Ibid at 9 and Appendix C.

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462. Three small TSPs that we spoke with ([]) each started out offering a fixed wireless network in a remote location and then expanded to offer broadband over copper and fibre as an additional service. These TSPs each submitted that

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Analysis of the evidence

463. As discussed above, we consider that we cannot exclude a real chance that a significant number of the []% at risk broadband customers of rival TSPs that are also Sky Sport subscribers would switch to the merged entity.

464. At this level of customer loss, and potentially a disproportionate loss of revenue, we consider there is a real chance that one or more of the three large TSPs, and in particular Vocus and Trustpower, would lose scale and be rendered materially less competitive in a way that substantially lessens competition.

465. We took the following factors into account in reaching this view:

465.1 the position of each of these TSPs as important drivers of competition in the broadband services market in the future;

465.2 the impact of a loss of a significant number of customers ([]%) on the planned and future investments of these TSPs (ie, whether revenues would be reduced to such an extent that the TSPs would be likely to become materially less competitive); and

465.3 whether each of these TSPs would be likely to expand if the merged entity sought to exercise market power in the future (ie, raised prices and/or reduced the quality of its broadband services).

466. At our request, Vocus and Trustpower both submitted models showing the impact on profitability of various levels of switching. However, we were unable to place material weight on these models as the underlying assumptions were highly uncertain, and the results were highly sensitive to those assumptions. We discuss this further below.

⁵²⁶ Letter from Trustpower to the Commerce Commission (15 November 2016) at 3.

⁵²⁷

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The TSPs that are likely to drive competition in the broadband services market in the future

467. Vodafone submitted that there are over 80 broadband suppliers in the market, which suggests that scale is not important in the market. However, it is not clear that all those TSPs provide the same constraint or would do so as the market evolves.
468. Despite the presence of the many TSPs we observe today, a relatively small number have been significant drivers of competition, and this is likely to continue to be the case. These TSPs have invested significantly in their networks, including equipment installed in exchanges for the purpose of unbundling, and in their backhaul networks. These investments gave these TSPs a higher fixed to variable cost ratio structure, and enhanced ability to control, and compete on, the quality of their service. This equipment will also remain an important part of their networks (requiring ongoing investments in maintenance) so long as Chorus' copper network remains operational.
469. In addition to acquiring access to Chorus' network, TSPs also require access to a backhaul network. This represents a potential source of difference between TSPs. The TSPs that do not own backhaul networks have a small market share and some focus on only limited geographic areas.
470. At present, the owners of backhaul networks are Chorus, Vodafone, Spark and Vocus. Chorus is not a retailer, but the other three backhaul network owners account for the vast majority of the retail broadband services market. We consider that owning a backhaul network allows a TSP greater flexibility as to the prices and services that it can provide, and these players are therefore likely to be important drivers of competition.
471. Other TSPs can gain access to backhaul networks by purchasing capacity from one of the backhaul network owners. Although this provides those TSPs with the means to provide broadband services, it is not clear that it places them in a position to provide a strong competitive constraint.
472. As discussed above, the roll-out of UFB is likely to generate increased demand for backhaul capacity, and even TSPs with significant networks may need to make additional investments and/or acquire capacity from third parties. Ownership of backhaul capacity is therefore likely to be a significant advantage in future.
473. There is uncertainty about what assets will be necessary to compete as customers move to UFB, and those services are unbundled. The terms upon which unbundling would occur have yet to be determined.⁵²⁸ It is therefore difficult to say how important it will be for parties to unbundle in order to compete and the extent to which scale will play a part in the economics to unbundle. Although we requested information from market participants on the likely investment required, we did not receive any indication of the likely costs.⁵²⁹

⁵²⁸ As discussed earlier at [79].

⁵²⁹ [

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474. We consider that the drivers of competition are likely to be the network owners (Spark and Vocus as well as Vodafone) and Trustpower. In particular, we consider that, as the ‘third players’ in the market, Vocus and Trustpower, are likely to provide a significant amount of competition. Competition in the market could be significantly impacted by the reduced competitiveness of these players.
475. Vodafone, Spark and Vocus compete in different ways.
476. Vodafone and Spark are the largest broadband retailers and have the strongest content offerings. Vodafone offers discounts on Sky content. Spark offers Lightbox and Spotify with selected services. Spark also has a low cost brand, Bigpipe.⁵³⁰ Vodafone and Spark are both able to offer bundles that include broadband, TV and mobile.
477. While Vocus and Trustpower have relatively low overall broadband services market shares, they both have a history of competing aggressively for customers and Vocus, in particular, has made significant network investments. Indeed, [], suggesting that they are each, separately, likely to be a significant source of potential competition in the future.
478. Vocus [].⁵³¹ It competes via differentiated offerings using several brands. The evidence suggests each of these brands has had an impact on the market, albeit in different ways.
- 478.1 Orcon []⁵³² The evidence suggests that Orcon has been an innovator and was the first to market various new services and offers. For example:
- 478.1.1 In 2009 Orcon was the first telecommunications provider to introduce new phone and internet plans following the Government’s 2006 decision to unbundle the local loop; and the first telecommunications provider to unbundle small business broadband and phone services.⁵³³
- 478.1.2 []⁵³⁴

⁵³⁰ Spark’s low cost FWA brand is Skinny.

⁵³¹ Commerce Commission interview with Vocus (29 July 2016).

⁵³² Commerce Commission interview with Vocus (14 December 2016).

⁵³³ https://www.orcon.net.nz/about/article/orcon_launches_unbundled_broadband_and_phone_calls and <http://www.newshub.co.nz/business/orcon-first-to-unbundle-small-business-broadband-phone-2009042707>.

⁵³⁴ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (29 July 2016) at 26.

478.1.3 Orcon claims that in 2012 it was the first telecommunications provider to announce its national UFB pricing plans for consumers, businesses and schools.⁵³⁵

478.2 Slingshot []⁵³⁶ Vocus advised that []⁵³⁷ Slingshot is a winner of internet service provider (ISP) awards.⁵³⁸

478.3 Flip []⁵³⁹ According to one article, Flip became one of the fastest growing ISPs following its entry in 2012.⁵⁴⁰ It amassed more than 10,000 customers in just over a year, which Vocus claimed was due to “disrupting the Kiwi broadband market with its unique business model and price leadership”.⁵⁴¹

479. Trustpower is different from Spark and Vocus in that it does not own backhaul infrastructure, []⁵⁴²

480. []⁵⁴³
[]

480.1 []⁵⁴⁴

480.2 Vocus advised that []⁵⁴⁵

The impact of []% customer switching on the broadband services market

481. Maintaining a modern network requires considerable levels of capital expenditure (CAPEX) with additional investments required on an ongoing basis. As new technologies come to market, TSPs must invest to keep pace with consumer needs

⁵³⁵ <https://www.orcon.net.nz/about/article/orcon-ultra-fast-broadband-now-available-in-ten-cities>.

⁵³⁶ Commerce Commission interview with Vocus (14 December 2016).

⁵³⁷ Ibid.

⁵³⁸ See, for example: <http://www.computerworld.co.nz/article/573604/who-nz-top-broadband-provider/> and Slingshot “Slingshot tops customer satisfaction again” (19 February 2015) at <https://www.slingshot.co.nz/news>.

⁵³⁹ Commerce Commission interview with Vocus (14 December 2016).

⁵⁴⁰ <https://itbrief.co.nz/story/flip-becomes-one-of-the-fastest-growing-isps/>.

⁵⁴¹ Ibid.

⁵⁴² [] provider under cover of an e-mail from Trustpower to the Commerce Commission on 15 November 2016.

⁵⁴³ Commerce Commission interview with Trustpower (13 December 2016).

⁵⁴⁴ [] provided under the cover of a letter from Buddle Findlay (on behalf of Sky) to the Commerce Commission (29 July 2016) at 105.

⁵⁴⁵ Commerce Commission interview with Vocus (14 December 2016).

and with their rivals. For example, the roll-out of UFB has required significant investment by TSPs in their networks and consumer premises equipment. Future investments are likely to be needed to expand the capacity of backhaul networks to meet growth in data usage. TSPs that choose to unbundle fibre post-2020 are also likely to have to make significant investments.

482. A loss of actual and/or potential customers (and the subsequent loss of revenue) reduces the capital that a TSP can use to cover asset maintenance and other planned CAPEX. This affects not only the funding of investment, but also incentives to invest in the future, which depend on expected profits to be earned in the contestable portion of the market (customer numbers and ARPU), as well as incentives to innovate and develop new products.
483. If rival TSPs expect lower returns in future, then they may have less incentive to invest in their networks. In the present case, we cannot exclude a real chance that this would arise, because:
- 483.1 there would be fewer contestable customers;
- 483.2 the customers that are contestable would be lower value (in terms of ARPU); and
- 483.3 customers are likely to be stickier in future, given that an increased number will purchase telecommunications services in a bundle. This will require higher customer acquisition costs to entice them to switch.⁵⁴⁶
484. If any of the three TSPs significantly reduced the level of investment to maintain, expand, enhance and innovate in relation to their network, then we cannot exclude the real chance that this would substantially lessen competition.
485. We focussed our inquiries on the impact on Vocus and Trustpower, given that they are smaller and less well-resourced than Spark, but have been drivers of competition in the market. Although they may be less exposed to a loss of customers than Spark, because a smaller proportion of those customers may currently subscribe to Sky Sport, as noted above we cannot rule out the real chance that they still have significant exposure. We considered that these TSPs would decrease CAPEX, and therefore be materially weakened, before Spark.

The likely impact on Vocus

486. On the basis of the evidence before us, we consider that there is a real chance that the loss of a significant number of residential customers would render Vocus less competitively effective.
487. []

⁵⁴⁶ This could include alternative bundled products and services as well as advertising and promotion costs.

488. Vocus had more than [] residential broadband subscribers as at October 2016. For the financial year 2016, Vocus had revenues of about []⁵⁴⁷
[]

489. []⁵⁴⁸
[]⁵⁴⁹
[]⁵⁵⁰

490. []⁵⁵¹

491. []⁵⁵²
[]
]

492. We considered how Vocus might be affected by losing []% of its customer base.

493. At our request, Vocus provided calculations that estimated how its residential broadband profits might be affected by the loss of a given level of customers.⁵⁵³

494. []
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495. []

496.

⁵⁴⁷ Commerce Commission interview with Vocus (14 December 2016).

⁵⁴⁸ Ibid.

⁵⁴⁹ Ibid.

⁵⁵⁰ E-mail from Vocus to the Commerce Commission (11 November 2016).

⁵⁵¹ Commerce Commission interview with Vocus (29 July 2016).

⁵⁵² Ibid.

⁵⁵³ E-mail from Vocus to the Commerce Commission (3 October 2016).

496.1

496.2

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498. Therefore, we were unable to exclude a real chance that Vocus would lose a significant proportion of its existing customer base and be significantly hindered in

[]⁵⁵⁸

506. [

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507. [

] ⁵⁵⁹

508. At our request, Trustpower provided calculations on how a given loss of customers would impact its profitability. []

509. [

510.

511.

512.

512.1

]

⁵⁵⁸ Ibid.

⁵⁵⁹ Letter from Trustpower to the Commerce Commission (15 November 2016) at 3.

512.2 [

] ⁵⁶⁰

513. []
We therefore cannot exclude a real chance that Trustpower would lose a significant proportion of its existing customer base and also be significantly hindered in its ability to win higher value customers.

514. We therefore cannot exclude a real chance that Trustpower would:

514.1 significantly reduce CAPEX and,
[]
and/or

514.2 [].

Would broadband TSPs be likely to increase investment in the future?

515. The prospect that Vocus and/or Trustpower could be rendered competitively less effective in the future raises the real chance that competition is likely to be significantly weaker with the merger compared to without the merger, that given Vocus and Trustpower are both active competitors in the relevant broadband services market. Lower levels of investment and innovation by one or both of these TSPs would reduce the price and non-price competition faced by the merged entity. This reduction in competition could manifest in prices being higher or service quality lower; and/or reduced incentives to invest in innovation, all of which would be harmful for consumers.⁵⁶¹

516. We have considered whether rival TSPs would be likely to enter or expand in the market if prices later rose. We would normally apply the LET test to see whether such entry would be sufficient to constraint prices.⁵⁶² However, the uncertainty associated with the timeframe for our analysis (the medium to long term), and the

⁵⁶⁰ E-mail from Trustpower to the Commerce Commission (3 October 2016).

⁵⁶¹ Given there is already a downward trend for telecommunication prices, prices could be lower in with the merger but nevertheless be higher compared to without the merger.

⁵⁶² The LET test is satisfied when entry or expansion in response to a price increase or other exercise of market power is Likely, and sufficient in Extent and Timely enough to constrain the merged firm. See Commerce Commission, *Mergers and Acquisitions Guidelines* (July 2013) at [3.96].

uncertainty about how competition in the relevant markets will evolve, means that applying the LET test is difficult. Nevertheless, we make five observations.

- 516.1 The convergence driven by the roll-out of UFB and the delivery of content over the internet is likely to mean that a higher proportion of customers will take up bundles in future. Further, we cannot rule out the real chance of significant switching driven by the merged entity's bundles.
- 516.2 Neither Vocus nor Trustpower is likely to be in a position to offer a competitive bundle containing premium live sports content, which would make expansion more difficult. There may be a significant percentage of the market foreclosed, and focusing on those customers that are not interested in a bundle containing premium live sports content may not be sufficient, particularly if those customers generate low ARPU. Rival TSPs would expect lower rates of return on network investments and spending on advertising and promotion to win new customers.
- 516.3 The dynamics of switching to bundled products, especially the event of the roll-out of UFB, are likely to involve significant asymmetries in consumer responses. The merged entity would be able to induce switching to bundles as consumers switch to UFB. Once the roll-out is complete, consumers will likely be less open to switching. Importantly, these consumers will face unbundling costs associated with multiples accounts and customer service contacts. As set out above, the evidence we have suggests that customers on a bundle are stickier than those that are not, and that Sky Sport subscribers as a group are []. This would make it more costly for rival TSPs to win customers back.
- 516.4 Rivals may also face strategic barriers to entry. Even if prices were to rise, Vocus and Trustpower may be dissuaded from entering or expanding due to the threat that the merged entity could respond aggressively to render investments unprofitable.
- 516.5 Although TSPs that operate on a regional basis could expand, it is unclear that regional expansion would impose a strong constraint on the merged entity nationally.
517. We therefore cannot exclude a real chance that third parties would not re-renter or expand to constrain the merged entity in the face of increased margins.

Conclusion – the impact of the merger on competition in the broadband services market

518. Vocus and Trustpower are significant competitors in the relevant broadband services market, and the evidence suggests that they have had an important impact on competition. We do not have sufficiently reliable data to rule out a real chance that they could lose, and fail to win, a significant number of customers (in particular high ARPU customers) as a result of the merged entity's bundled offers. The timing of the proposed merger, at a time of significant migration to UFB, is significant.

519. A loss of a significant number of customers, and foreclosure of the ability to effectively compete for a significant proportion of the broadband services market, would be likely to impact their profits and their ability and incentive to make investments (including product development, advertising and promotions). We cannot exclude a real chance that this would materially lessen the competitive constraint that they impose on the merged entity. Diminished investment and competitive constraints would likely manifest in higher prices and/or lower quality from the merged entity.
520. We attempted to quantify the likely impact of the proposed merger on both these TSPs, however due to the uncertainties outlined above this proved difficult, and we were unable to exclude a real chance that both would be sustain significant losses.
521. Poorer offerings from the merged entity over time would be expected to induce re-expansion or entry by rival TSPs. However, there are likely to be asymmetries in switching behaviour by consumers on bundles once they have switched to UFB, reducing the ability and incentive for rival TSPs to make investments in re-expansion.
522. What constitutes a substantial lessening of competition is in the end a matter of judgement informed by as much practical evidence as possible.⁵⁶³ While we had insufficient evidence available to us to quantify precisely the likely impact of the merger on competition in the broadband services market, we had available sufficient evidence which, when viewed in the round, meant that we could not exclude the real chance of a substantial lessening of competition in this market, over the medium to long term, as the competitive constraint imposed by Vocus and Trustpower is significantly weakened.

Mobile: would rival mobile TSPs be rendered competitively less effective?

523. This part of the assessment considers whether the loss of a significant proportion of the []%⁵⁶⁴ of mobile customers of rival TSPs that reside in a household subscribing to Sky Sport:
- 523.1 would render any rival TSP less competitively effective; and if yes
- 523.2 whether this would be likely to lead to a substantial lessening of competition.
524. As with broadband, we focussed our inquiries on the impact of the third player (ie, 2degrees) given that it is smaller and less well-resourced than Spark. Again, although it may be less exposed to customer loss than Spark, as noted above we cannot rule out the real chance that it would still have significant exposure. We considered that 2degrees would decrease CAPEX, and therefore be materially weakened, before Spark, particularly given the stage of its growth cycle.

⁵⁶³ *Commerce Commission v Woolworths Ltd (CA)* above n10 at [101].

⁵⁶⁴ See [284], above, for how we calculated this figure.

Applicants' submissions

525. Vodafone submitted that any concerns about 2degrees – the smallest of the MNOs – not achieving scale are unfounded.⁵⁶⁵ Vodafone submitted that 2degrees is a major player, accounting for 23% of all mobile connections.⁵⁶⁶
526. Further, it submitted that, as MNOs have high fixed costs and low variable costs, an operator that loses scale will have the ability and incentive to offer any spare capacity at low prices.⁵⁶⁷
527. Vodafone submitted that this is in contrast to an operator at scale, which will tend to have rising variable costs, meaning that it would start to experience diseconomies of scale.⁵⁶⁸ Vodafone submitted that the loss of scale would not affect future competition: greater competition will instead encourage investment in order to create a differentiated product; and a firm could compete without investing by focusing on other factors of competition.⁵⁶⁹
528. Vodafone submitted that in the event that 5G is rolled out, scale will not be crucial as it can be rolled out on an incremental basis (eg, Auckland, Wellington, Christchurch, Hamilton) and it is unclear whether early rollout of 5G would be an advantage given that Vodafone did not appear to materially benefit from its early rollout of 4G.⁵⁷⁰

Third party submissions

529. 2degrees indicated that, []⁵⁷¹ In particular it would only be able to compete for lower ARPU customers, which would confine it to smaller revenue pools, limiting its ability to generate the revenues required to invest and compete aggressively in all customer segments.⁵⁷²
530. []⁵⁷³

531. Link Economics, on behalf of Blue Reach, submitted that the loss disclosed in 2degrees' 2015 financial statements indicated that it had not yet reached minimum efficient scale. To the extent that the proposed merger reduced the customer base contestable to 2degrees, this would make it harder to reach minimum efficient scale.

⁵⁶⁵ Submission from Vodafone to the Commerce Commission (11 November 2016) at [22.3].

⁵⁶⁶ Ibid at [22.3].

⁵⁶⁷ Ibid at [23.2].

⁵⁶⁸ Ibid at [23.2].

⁵⁶⁹ Ibid at 34.

⁵⁷⁰ Ibid at 34-35.

⁵⁷¹ Commerce Commission interview with 2degrees (19 October 2016).

⁵⁷² Submission from 2degrees to the Commerce Commission (6 October 2016) at [3.23].

⁵⁷³ E-mail from 2degrees to the Commerce Commission (11 October 2016).

This could negatively impact competition for both residential and business mobile services customers.⁵⁷⁴

Analysis of the evidence

532. As discussed above, we are unable to exclude a real chance that a significant number of the []% at risk mobile customers would switch to the merged entity. At this level of customer loss, we could not exclude a real chance that 2degrees would lose scale and be rendered materially less competitive, resulting in a substantial lessening of competition in the relevant mobile services market.

533. We took the factors below into account in reaching this view.

533.1 We consider that the loss of a significant number of customers (or inability to grow) would affect 2degrees' ability and incentive to reach a sustainable scale. Such a lack of scale would be likely to adversely affect 2degrees' ability to continue to invest in assets, as well as product development and innovation, and render it less competitively effective in the future.

533.2 As discussed above, 2degrees appears to have driven price competition since it entered in 2009. We consider that the loss of 2degrees as a strong competitive constraint would therefore reduce competition in the market.

533.3 [

]

534. As noted above, we estimate that approximately ([]%) of mobile customers are in a household with a Sky Sport subscription. These are the customers that we consider would be most susceptible to switching. If these customers were uniformly distributed among MNOs, then we would expect that []% of each TSP's residential customers would be in a household that subscribes to Sky Sport. We considered the evidence on the proportion of MNOs' customers that actually subscribe to Sky Sport in order to identify the extent to which these MNOs' current customer bases would be at risk of switching.

535. Spark provided []⁵⁷⁵

536. 2degrees provided []⁵⁷⁶

⁵⁷⁴ Report from Link Economics (on behalf of Blue Reach) to the Commerce Commission (10 November 2016) at 16.

⁵⁷⁵ Submission from Spark to the Commerce Commission (5 October 2016) at 33.

537. [

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Impact of significant switching on 2degrees

538. We consider that a large proportion of the []% of mobile customers that are at risk could be attracted to the merged entity. A large proportion of these customers are likely to be [].

539. While we cannot be certain how 2degrees would be impacted by the merger, we cannot exclude the real chance that 2degrees would fail to reach sustainability and reduce its CAPEX spending, reducing its competitive constraint on the relevant mobile services market in the future.

540. 2degrees entered the market in 2009 and []⁵⁷⁷
[]⁵⁷⁸
[]⁵⁷⁹

541. 2degrees is still expanding its network, and []⁵⁸⁰ 2degrees submitted that,
[]⁵⁸¹.

542. When 2degrees entered the mobile services market in 2009, it initially focused on winning pre-pay customers. However, []⁵⁸².

543. []⁵⁸³ It submitted that,

⁵⁷⁶ E-mail from 2degrees to the Commerce Commission (3 October 2016).

⁵⁷⁷ Commerce Commission interview with 2degrees (3 August 2016).

⁵⁷⁸ Ibid.

⁵⁷⁹ [] attached to an e-mail from 2degrees to the Commerce Commission (24 November 2016).

⁵⁸⁰ Commerce Commission interview with 2degrees (19 October 2016).

⁵⁸¹ Ibid.

⁵⁸² Commerce Commission interview with 2degrees (3 August 2016).

⁵⁸³ [] attached to an e-mail from 2degrees to the Commerce Commission (4 October 2016) at 5.

[]⁵⁸⁴

544. []⁵⁸⁵
 []⁵⁸⁶
 []⁵⁸⁷

545. We asked 2degrees to provide an estimate of how its profitability would be affected by a given loss of customers.

[]

546. []

547. As with the Vocus' and Trustpower's models, there were too many uncertainties surrounding the calculations for us to have any degree of confidence in the results.

548. The stage of 2degrees' growth cycle made it challenging to determine how it would be impacted by a given loss of customers.

[]

549. []

550. We therefore could not rule out the real chance that the proposed merger would cause 2degrees to lose a significant number of actual and potential customers. We note that:

550.1 []

550.2

]

⁵⁸⁴ Commerce Commission interview with 2degrees (19 October 2016).

⁵⁸⁵ Commerce Commission interview with 2degrees (3 August 2016).

⁵⁸⁶ Ibid.

⁵⁸⁷ Commerce Commission interview with 2degrees (19 October 2016).

550.3 As discussed above, customers on bundles are stickier and less prone to switching, and some of these customers may remain with the merged entity in future, even if the merged entity raised prices.

551. []⁵⁸⁸
[

552.]

552.1 []⁵⁸⁹

552.2 2degrees may also face barriers to expansion in the business sector. In 2015 the Commission commissioned a study that looked at whether there were any factors inhibiting competition in the business mobile sector.⁵⁹⁰ The study found that:⁵⁹¹

2degrees loses heavily on perceptions of coverage and confidence and is not considered far enough ahead on cost and customer service to be competitive overall. They are weakest on ‘confidence’ with many not aware of their experience in the business market and the ability to cater to the needs of businesses. Longevity is also an issue with many saying that ten years was the milestone they viewed as the length of time required to show that a company is established and likely to be around for the long haul.

553. Nevertheless, the study also found that there appear to be good opportunities to expand market share and 2degrees has []⁵⁹²
[]⁵⁹³

⁵⁸⁸ [] attached to an e-mail from 2degrees to the Commerce Commission (4 October 2016) at 5.

⁵⁸⁹ E-mail from 2degrees to the Commerce Commission (1 December 2016).

⁵⁹⁰ UMR “Competition for Business Customers in the Mobile Industry: A Report for the Commerce Commission” (December 2015).

⁵⁹¹ Ibid at 4.

⁵⁹² Letter from 2degrees to the Commerce Commission (24 November 2016) at 7.

⁵⁹³ [] provided under the cover of an e-mail from 2degrees to the Commerce Commission (24 November 2016).

554. []

555. If 2degrees reduces investments in its network, then there is a real chance that its ability to compete for business customers would also be frustrated.

Would mobile TSPs be likely to increase investment in the future?

556. The prospect that 2degrees could be rendered competitively less effective in the future raises the real chance that competition is likely to be significantly weaker with the merger compared to without the merger, given it as an active third player. This reduction in competition could manifest in relative prices being higher or service quality lower; and/or reduced, incentives to invest in innovation, which may be weaker with the merger than without the merger.⁵⁹⁴

557. We have considered whether 2degrees would be likely to expand in the market if prices later rose and/or quality was reduced for mobile services. We would normally apply the LET test to see whether such entry would be sufficient to constraint prices. The uncertainty associated with the timeframe for our analysis (the medium to long term), and the uncertainty about how the competitive dynamics of the relevant markets may evolve, means that applying the LET test is difficult. However, we make three observations.

557.1 To the extent customers have taken up bundles with content, 2degrees (or another MNO) may find it difficult to attract these customers back in future, particularly given the evidence that bundled customers are less prone to churn, and Sky Sport customers (as discussed above)

[]. If 2degrees is confined to competing for customers that are not interested in a bundle containing Sky Sport, and which may be low ARPU, it may not be incentivised to make investments and compete as hard in future.

557.2 As discussed above, 2degrees

[].

557.3 New entry is unlikely given high barriers to entry associated with substantial sunk costs and economies of scale in mobile networks.

558. We therefore cannot rule out a real chance that 2degrees (or a new entrant) would be unable to expand to constrain an exercise of market power by the merged entity.

Conclusion – the impact of the merger on competition in the mobile services market

559. We have considered whether the loss of 2degrees as an effective competitor would result in a substantial lessening of competition (notwithstanding that Spark may still

⁵⁹⁴ Given that there is already a downward trend for telecommunication prices, prices could be lower in with the merger but nevertheless be higher compared to without the merger.

be an effective competitor). As noted earlier, the Commission has previously found that 2degrees has had a significant positive impact on competition.

560. Since 2degrees' entry, the Commission has observed decreases in mobile prices, increases in mobile phone usage and an improvement in New Zealand's OECD benchmark ranking.⁵⁹⁵ MBIE, in its review of the Telecommunications Act 2001 has acknowledged the impact of 2degrees' entry and stated that it is important to "maintain and build on the competition gains achieved over the last decade".⁵⁹⁶
561. We cannot exclude a real chance that 2degrees' ability and incentive to continue its growth path of investment and innovation would be adversely affected by the merged entity's bundled offers. This, in turn, would reduce the future competitive constraint offered by 2degrees.
562. We encountered similar challenges assessing the evidence in the relevant mobile services market as we did in the relevant broadband services market. We had insufficient evidence available to us to positively persuade us that a substantial lessening of competition was, or was not, likely. Therefore, on the evidence available to us, we were not able to exclude a real chance that the proposed merger would be likely to substantially lessen of competition in the relevant mobile services market.
563. As noted above in relation to the broadband services market, what constitutes a substantial lessening of competition is in the end a matter of judgment informed by as much practical evidence as possible.⁵⁹⁷ As with the broadband services market, we had insufficient evidence available to us to quantify precisely the likely impact of the merger on competition in the mobile services market. Therefore, based on the evidence before us, judged in the round, we concluded that we could not exclude the real chance of a substantial lessening of competition in this market, over the medium to long term, as the competitive constraint imposed by 2degrees is significantly weakened.

⁵⁹⁵ Commerce Commission, Final MTAS report above n108 at [230] and Commerce Commission, "International Price Comparison for Retail Mobile Telecommunications Services 2013" (March 2014).

⁵⁹⁶ MBIE discussion paper "Regulating communications for the future" (September 2015) at 44.

⁵⁹⁷ *Commerce Commission v Woolworths Ltd (CA)* above n10 at [101].

Determination on notice of clearance

565. The Commission is not satisfied that the proposed merger will not have, or would not be likely to have, the effect of substantially lessening competition in a market in New Zealand.

566. Pursuant to s 66(3)(b) of the Commerce Act 1986, the Commerce Commission determines to decline to give clearance for:

566.1 the acquisition by Vodafone Europe B.V., or an interconnected body corporate of Vodafone Europe B.V., of up to 51% of the shares in Sky Network Television Limited; and

566.2 the acquisition by Sky Network Television Limited, or an interconnected body corporate of Sky Network Television Limited, of up to 100% of the assets and/or shares of Vodafone New Zealand Limited.

Dated this 22nd day of February 2017

Dr Mark Berry
Chairman

Attachment A: TSP Promotional activity, 2014-2016

A1. []

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[

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A2. [

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[

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Source: TSPs.

A3. [

A3.1.

A3.2.

A3.3.

A3.4.

A3.5.]