PUBLIC VERSION

Sky TV / Vodafone merger clearance

Submission | Commerce Commission

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Contents

Executive Summary

1. Spark New Zealand welcomes the opportunity to comment on the merger clearance applications submitted to the New Zealand Commerce Commission (**Commission**) on 29 June 2016 by Sky Network Television Limited (**Sky**) and Vodafone Europe B.V. (**Vodafone Europe**) in respect of the acquisition by Sky of Vodafone New Zealand (**Vodafone**).

2. Sky is New Zealand's largest pay TV provider, and has a monopoly on premium sports rights. It has historically bundled these premium sports rights with its own distribution platform (satellite delivery to a Sky set-top box), but now faces the reality that its distribution platform is incapable of meeting the needs of customers, who increasingly prefer to watch media content over fixed line and mobile broadband networks.

3. This shift in consumer behaviour and requirements threatens to force Sky to un-bundle its content from its distribution platform and wholesale that content to Spark and other RSPs who have the ability to deliver it over their broadband networks.

4. Vodafone operates New Zealand's second largest fixed and mobile broadband network. The proposed merger is intended to enable Sky to re-bundle its monopoly content holdings with this new distribution platform rather than wholesale its content on competitive terms.

5. Spark's view is that the proposed merger between Sky and Vodafone will substantially lessen competition in the New Zealand markets for:

   a. Residential / consumer retail broadband and mobile services;

   b. Pay TV; and

   c. The acquisition and wholesale of New Zealand premium sport content rights.

Sky has a monopoly on premium sports rights in New Zealand. Premium sports rights are "must have" content rights.

6. The key bottleneck input for media content providers is premium sport. It is an essential input for providing a competitive (as opposed to complementary) pay TV offering to Sky. It is "must-have" content. This is clear from the price differentials between Sky's pay TV packages and the other movie / TV series-based SVOD pay TV offerings in the market, and is supported by international and local market evidence.

7. Spark's experience as a provider of media content through Lightbox Sports is further evidence of this. Even though New Zealanders show interest in a wide range of sports, these sports are complements, rather than substitutes, for interest in premium "national sports". It is Spark's belief that non-exclusive wholesale access to Sky's premium sports content at economically sustainable prices remains key to the development of a competitive and vibrant media content market in New Zealand.

Sky-Vodafone will have the ability and the incentive to use its market power in relation to sports content to reduce competition in downstream markets.

8. If the merger were to proceed then the merged entity would have the ability and incentive to use its substantial market power in the markets for the acquisition and wholesale of premium sports rights and pay TV to distort competition in the broadband / mobile markets in order to gain and retain large numbers of residential broadband and mobile customers. That ability and incentive does not exist today as Sky does not have its own broadband or mobile product offering, nor does it own the platforms for digital distribution of its pay TV products.

9. After the merger, Sky / Vodafone can be expected to engage in exclusionary conduct including initial deep discounting of bundles and restrictive or uneconomic wholesale deals; and then ultimately, once smaller/newer RSPs have been squeezed from the market, to offer a lower quality / higher priced pay TV product as compared with the Counterfactual.

10. In simple terms, Sky / Vodafone will bundle a further, competitive, product (broadband and / or mobile) with its monopoly sports rights, and in doing so will reduce competition for that product.

11. There is likely to be less innovation and less digital distribution of pay TV content; increased barriers to entry and expansion, and reduced switching between broadband suppliers; and lower uptake of UFB as compared to the Counterfactual. Ultimately this will lead to higher overall prices for consumers than would prevail in the Counterfactual.

Sky has used its acquisition of Prime TV to foreclose competition for free to air premium sports rights, and will use its acquisition of Vodafone to do exactly the same for digital and mobile premium sports rights

12. Similarly, in adding a broadband network and subscriber base, and a mobile network and subscriber base, Sky / Vodafone will also have the ability and incentive to foreclose competition in the markets for digital and mobile content rights.

Without the merger, Sky would be forced to shift from being a reluctant wholesaler to a proactive one, because customers want to watch TV content everywhere and at any time

13. In the Counterfactual, Sky must look to contract competitively with RSPs for premium sports digital distribution as its satellite-based distribution is eroded by digital offerings as a result of increased consumer preference for consuming content via broadband and mobile channels, and the roll-out of UFB. In the Counterfactual, wholesale access to key Sky content – especially Sky Sports channels - is likely to be provided to Spark and other RSPs on fair and reasonable terms, which would enable those RSPs to provide genuinely competitive broadband and content bundles that appeal to a range of consumers.

14. Those bundles will, over time, allow the development of a workably competitive market for the acquisition and wholesale of premium sports rights. That market does not exist today, nor will it exist in the Factual due to the merger's maintenance of Sky's market power in pay TV, and the acquisition and wholesale of premium sports rights.

Sky and Vodafone are, independently, reluctant wholesalers today. All evidence – historical behaviour as well as forward-looking incentives – suggests a merged Sky-Vodafone would be an even more reluctant wholesaler.

15. Our expectation is that a merged Sky / Vodafone will have little incentive to offer compelling wholesale services, and therefore little propensity to do so. Whereas wholesale markets for access to premium content are emerging to support increasingly competitive content markets in other countries, those same markets will not emerge in New Zealand, that same competition will not emerge in New Zealand - and consumers will be worse off because of it.

The parties

16. Sky has a unique position in the New Zealand media landscape and indeed a unique position compared with any other pay TV operator in the world. This has led the Commission to previously conclude that:[1]

> Sky is likely to have a substantial degree of market power (SMP) in the pay TV market. Sky's share of the supply of the pay TV market has been close to a monopoly for a sustained period of time, and new entrants face significant barriers to entry that they must overcome.

17. Spark agrees with the Commission's assessment that Sky has a substantial degree of market power in the pay TV market, and this is founded in, and supported by, its substantial degree of market power in the market for the acquisition (and wholesale supply) of premium (live) sports rights. This position of market power is due to Sky:

    a. Being New Zealand’s only full service pay TV operator, including being the only pay TV operator that has its own satellite distribution platform, with a network of set top boxes in its customers' premises throughout New Zealand;

    b. Being, by orders of magnitude, New Zealand's largest pay TV operator, with an estimated 830,000 subscribing households;[2]

    c. Owning exclusive rights to all key premium sports content in New Zealand;

    d. Being vertically integrated into the Free-to-Air (**FTA**) TV market by also owning a FTA channel (Prime TV); and

    e. Owning New Zealand's largest outside broadcast operator - Outside Broadcasting Ltd (**OSB**).

18. The fact that Sky has exclusive rights to all key premium sports content in New Zealand is a result of:

    a. as the Commission has observed, Sky's large subscriber base; significantly higher subscription prices; and economies of scale; which mean it can pay significantly greater sums of money for exclusive content than any other pay TV provider in New Zealand;

    b. Sky's vertical integration as not only a content acquirer, but also the only content acquirer in New Zealand that has its own pay TV distribution platform; and

    c. Sky's vertical integration into the FTA market through its ownership of the Prime FTA channel.

19. We expand in more detail below on how this plays out in rights negotiations with sports rights holders and RSPs seeking wholesale supply of premium sports rights from Sky.

20. Sky's market power is further exacerbated by the fact that in New Zealand, unlike in most other developed countries around the world, there are no "anti-siphoning" or "designated events" broadcasting regulations to prevent a single broadcaster from monopolising the acquisition of sports content in New Zealand.

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[1] New Zealand Commerce Commission "Investigation Report on Sky TV contracts" (8 October 2013) at [27].

[2] Sky Network Television Limited "Notice of Meeting and Explanatory Memorandum Relating to the Merger of the Businesses of SKY and Vodafone NZ" at 6.

21. As a result of this unique position internationally, Sky has historically provided only limited, restrictive and, in Spark's view, uneconomic wholesale access to their pay TV products to Spark and (as we understand it) other RSPs. This is, in effect, a constructive refusal to deal by a firm with market power. Sky's wholesale terms have enabled Sky to maintain its dominant position in the pay TV market while significantly constraining the ability of retail broadband operators to meaningfully compete with it in relevant TV / content markets – either by bundling broadband services with Sky content or other content sourced independently.

22. Demonstrating this point, in 2013 the Commission concluded that Sky had sought to implement terms in its contracts with RSPs that breached ss 27 and 36 of the Commerce Act "by hindering competition in the market for pay TV in New Zealand",[3] including by "leveraging its market power... to prevent or hinder RSPs from assisting or developing rival pay TV products."[4]

23. Vodafone is New Zealand's second largest retail broadband service provider and (depending on the timing of market reports) either the largest or second largest mobile operator in New Zealand by subscriber numbers and / or revenue. Vodafone also owns a hybrid fibre coaxial cable (**HFC**) network in Wellington and Christchurch, which is connected to 145,000 New Zealand homes (11% of New Zealand homes).[5] The HFC cable was originally deployed in Wellington and Christchurch by Kiwi Cable / Saturn to deliver a cable pay TV service to consumers.

24. Vodafone supplies / resells Sky TV packages to its customers and, we understand, retransmits Sky TV broadcast feeds in the geographic areas where it has a HFC hybrid fibre coaxial cable network.

25. The fact Vodafone is the only RSP that currently supplies Sky TV products in a bundle with its broadband services is indicative of the current practical and economic challenges of reaching viable wholesale terms with Sky (see paragraph 20 above). The fact that Vodafone has managed to negotiate an arrangement with Sky may well reflect that Sky is willing to offer more attractive terms to Vodafone, vis-à-vis other RSPs, because Vodafone owns its own HFC cable distribution platform that can be used for retransmission of Sky content.

Sky's premium sports rights content monopoly

26. As the Commission knows, it investigated Sky for taking advantage of its market power in 2013. In that in investigation, the Commission observed that:[6]

> New entrants focussing on a SVOD model have told us that they do not necessarily need sport. Quickflix has entered in New Zealand and Australia without sport content.

27. Spark agrees that it is indeed possible for new entrants to offer SVOD pay TV without sport content, as evidenced by entry of Spark's Lightbox, as well as Netflix and Quickflix. Whether that proposition is competitive with, as opposed to merely complementary to, Sky's pay TV offering, is another matter.

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[3] New Zealand Commerce Commission "Investigation Report on Sky TV contracts" (8 October 2013) at [9].
[4] At [14.1].
[5] Tom Pullar-Strecker "Govt rejects Vodafone UFB plea" (6 March 2014) Stuff. Accessed at: http://www.stuff.co.nz/technology/digital-living/30020945/govt-rejects-vodafone-ufb-plea.
[6] New Zealand Commerce Commission "Investigation Report on Sky TV contracts" (8 October 2013) at [346.1].

28. In that same investigation, the Commission observed that "[n]ew entrants focussing on a fuller range of service may need sport."[7] Spark agrees with that observation, and would add that without other revenue (from other services) or cost advantages, (e.g. an international content portfolio such as Netflix) a standalone competitive pay TV offering without sport is unlikely to be self-sustaining. This is reinforced by comments Sky has previously made to the Commission (for example, in *Sky / Prime*):

> SKY advised the Commission that live sport is its main driver of subscriptions in New Zealand, and the cornerstone of its sports programming is rugby.

29. Similarly:

    a. In discussing its resale arrangement with Sky, the former CEO of TelstraClear (now part of Vodafone) observed: "of course what drives pay TV is the sport ... I'm afraid if you look at our stats for Sky usage, sport is the key. Followed then by movies, but sport is the big one."[8]

    b. Rupert Murdoch famously described sport as the "battering ram" of pay TV, noting: "[s]port absolutely overpowers film and everything else in the entertainment genre".[9]

    c. Vodafone UK observed in 2015 that live sports events "have no close substitutes",[10] and submitted to Ofcom:[11]

> Key content is by its nature exclusive, or put simply a monopoly input, which in any other scenario would be subject to appropriate regulation. Ofcom acknowledges that consumers value a wide range of content genres; however Vodafone agrees with the findings of the 2014 WMO Consultation; that **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 and BT's willingness to spend so much on sports broadcast rights (most notably for Premier League and Champions League content), than on other genres indicates the value they believe they can recover from utilising this content. **Given the combination of these factors, sport appears to be uniquely placed to drive consumer choice in Pay TV services and beyond**. [Emphasis added]

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[7] At 346.3.

[8] Sarah Putt "Sky TV and the telcos: TelstraClear boss tackles content issues" (21 March 2012) Computerworld. Accessed at: http://www.computerworld.co.nz/article/492309/sky_tv_telcos_telstraclear_boss_tackles_content_issues/.

[9] Robert Milliken "Sport is Murdoch's 'battering ram' for pay TV" (16 October 1996) Independent. Accessed at: http://www.independent.co.uk/sport/sport-is-murdochs-battering-ram-for-pay-tv-1358686.html.

[10] Vodafone submission to "Public consultation on the evaluation and the review of the regulatory framework for electronic communications networks and services" (2 December 2015). Accessed at: https://www.vodafone.com/content/dam/group/policy/downloads/01_12_2015_DSM_Framework_Review_Vodafone_submission.pdf.

[11] Vodafone "Response to Ofcom's Consultation: Strategic Review of Digital Communications discussion document"
(8 October 2015) at 3.1. Accessed at: http://stakeholders.ofcom.org.uk/binaries/consultations/dcr_discussion/responses/Vodafone.pdf.

30. This means that for a significant number of consumers, sport is not substitutable with other video content. For this reason, SVOD services such as Netflix and Lightbox are typically regarded as complementary to, not substitutable with, full service pay TV services such as Sky:[12]

> "The rise of Netflix doesn't mean the demise of pay-TV," said Paul Lee, the director of technology, media and telecommunications (TMT) at Deloitte. "The impact of Netflix has been greatly exaggerated."
>
> Deloitte's annual TMT Predictions report, out next week, suggests SVOD should be seen less as a direct competitor to pay-TV and rather as complementary and a replacement for DVD box sets.
>
> Three-quarters of British subscribers to an SVOD service also subscribe to a "linear" pay-TV service, Deloitte estimates.
>
> Mr Lee said: "In the United States, they've had Netflix since 2008 as a streaming service. In that time, the number of pay-TV homes has barely shifted even as we've gone from zero to 37 million Netflix customers."

31. This is demonstrated in New Zealand by the significant price difference between Sky's Basic + Sky Sport package in comparison to other SVOD services in New Zealand, as illustrated in Figure 1 below.

Figure 1 - Price of pay TV offerings in New Zealand pay TV market in comparison to Sky's sport offerings

Offering	Headline price per month	Price differential vs. Sky Basic + Sky Sport	Price differential vs. Sky Fanpass
Sky Basic + Sky Sport	$79.81/month	N/A	+30%
Sky Fanpass	$55.99/month	-43%	N/A
Lightbox	$12.99/month	-514%	-331%
Netflix	$9.99 to $15.99/month	-699% to -399%	-460% to -250%
Quikflix	$12.99/month	-514%	-331%

32. The fact that sport is not substitutable with other content for a significant number of consumers has previously been observed by competition regulators, both in New Zealand and overseas. For example:

    a. The Commission has noted:[13]

> Industry participants advised the Commission that although some marginal SKY customers would switch (or disconnect) in the face of a 5% price increase, for the majority of customers there would be no substitute for pay-TV. **Industry participants noted that this is particularly true for fans of live sport**. [Emphasis added]

[12] Gideon Spanier "Netflix: Effect of video streaming boom on pay-TV subscriptions 'greatly exaggerated' " (6 January 2015) Independent. Accessed at:http://www.independent.co.uk/news/business/news/effect-of-netflix-boom-on-pay-tv-subscriptions-greatly-exaggerated-9959451.html.
[13] New Zealand Commerce Commission Decision No 573 *Sky Network Television Limited / Prime Television New Zealand Limited* (8 February 2006) at [79].

b. Similarly, Ofcom in the UK has noted:[14]

> [B]ecause Premier League and other football is a key driver of demand for pay TV services, we consider that it is appropriate to focus on the substitutability of sports content available elsewhere. The simplifying assumption is that other elements of the bundle, such as basic TV content and broadband, can be substituted relatively easily.
>
> …
>
> In order to conclude that Sky did not have market power, it would be necessary to believe either that at competitive prices general entertainment programming would be a close substitute to sports, or that Sky was unlikely to retain a material proportion of the sports rights it currently controls. Both are highly improbable.

c. The European Commission has observed that access to premium football and movies was indispensable for new pay TV operators, as premium content drove subscriptions to pay TV,[15] and stated that access to premiums sports is "decisive" and has the potential to lead to dominance by pay TV operators.[16]

33. In considering whether there are alternatives for fans of live sport (a description which includes a large proportion of New Zealanders), Spark's experience has been that it is not sufficient to have a handful of discrete, even if popular, sports content rights to establish a successful full service pay TV offering. For example, Spark sought to establish a full scale pay TV offering by entering into a partnership with Coliseum, known as the Lightbox Sport partnership, to distribute and market English Premier League (**EPL**) content with a view to the partnership being used to bid for further sports rights and develop a set of sports products for distribution. Lightbox Sport also acquired the rights to distribute:

a. Top tier international golf in New Zealand (LPGA, USPGA, PGA European Tour); and

b. Some European rugby.

34. However, the Lightbox Sport partnership did not achieve sufficient subscription levels to be sustainable. That was, based on Spark's experience, due to its lack of a sufficient bundle of premium sports content. The service was closed in early 2016. Spark's Lightbox Sport experience is that to attract sufficient subscribers to establish a viable sports pay TV service it is necessary to have a bundle of content rights to the most popular sports in New Zealand, namely rugby, cricket, rugby league, and / or football, as well a range of other niche sports - and that those niche sports are a complement to, rather than a substitute for, consumers' demand for viewing the most popular sports.

35. The need to offer a bundled package of content has been recognised by competition regulators, for example Ofcom in the UK:[17]

> As we set out in the following analysis, by far the most highly-valued TV sport content in the UK (and elsewhere) is football....

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[14] Ofcom "Sports and general market definition and market power appendices" Annex 4 to Pay TV Statement (31 March 2010) at [3.9], and Ofcom "Pay TV statement" (31 March 2010) at [1.22].
[15] European Commission "Commission clears merger between Stream and Telepiù subject to conditions" press release (2 April 2003).
[16] Speech given at the Telecommunications Industry Conference (31 May 2000). Accessed at http://ec.europa.eu/competition/speeches/text/sp2001_011_en.pdf
[17] Ofcom "Sports and general market definition and market power appendices" Annex 4 to Pay TV Statement (31 March 2010) at [3.9].

> A range of other sports are also valued by pay TV subscribers. In particular rugby union, cricket, motorsports, tennis, boxing and golf are seen as very important by some subscribers and moderately important by others. In general, the appeal of a pay TV proposition to an individual person or household will depend on its having some content that is seen as highly attractive, along with a range of moderately attractive content, and the relative importance of different content will vary according to tastes.

36. The ACCC has noted this in its Media Merger Guidelines:[18]

> To give an example of the sort of issues raised by the exclusive acquisition of premium content by a particular media organization, consider the acquisition, for example, by a pay TV operator of the exclusive rights to televise several popular spectator sports. By gaining these exclusive rights, the relevant pay television operator may have the ability to foreclose competition in pay TV to the degree that any other pay TV operator would need access to at least some of this sports content to provide a viable competitive alternative for viewers.
>
> In practice, the acquisition of exclusive premium content rights, such as the exclusive rights to broadcast a range of popular sporting events, would be likely to take place over a period of time as the rights come up for sale. The sequential acquisition of exclusive premium broadcasting content may overtime lead to a media company collecting a portfolio of exclusive rights that last for a sufficiently-long period of time to raise competition concerns.

37. Sky is the only company in New Zealand that has a package of valued premium sports content sufficient to drive substantial subscription uptake - with it holding exclusive rights to almost all premium sports content. For example, Sky currently has exclusive medium-term content arrangements to broadcast over pay TV, FTA television and digital all major sporting events in rugby, rugby league, cricket, and the Olympics (to 2024), and FIFA World Cup (to 2022), as well as many other sports.

38. The reason Sky has a monopoly over this bundle of premium sports content is because, as the Commission has previously observed, Sky's large subscriber base and economies of scale means it can pay significantly greater sums of money for exclusive content than any other pay TV provider in New Zealand - including for pay TV broadcast, digital, and mobile rights, as well as FTA broadcast rights.

39. This becomes a self-fulfilling (entrenched) source of market power over the bundle of premium sports content due to certain distinct features of the pay TV / premium sports content market (as described in the UK):[19]

    a. ***Finite pool of key content***: There is only a finite pool of key premium sports content;

    b. ***Limited duration of rights contracts for key content***: The rights to broadcast certain key events are limited in duration. The means that (i) an acquiring firm has a strictly limited time period in which to make a return on content investments, and (ii) a firm with an established subscriber base enjoys a competitive advantage when bidding for content as it can monetise its investments in content faster than firms without such a subscriber base. This allows the former to outbid the latter for future key content, thereby perpetuating its leadership downstream;

[18] Australian Competition and Consumer Commission "Media Mergers" (August 2006) at [48] - [49]. Accessed here: https://www.accc.gov.au/system/files/Media%20Mergers%20-%202011.pdf.

[19] British Telecommunications et al "Submission to Ofcom on the need for a market investigation into the pay TV industry" (3 July 2007) Ofcom at [10]. Accessed at: http://stakeholders.ofcom.org.uk/binaries/broadcast/reviews-investigations/pay-tv/submission1.pdf.

c. ***Staggered availability of key content***: Content rights are staggered in their availability, which significantly increases the barrier to entry. For example, in order to acquire a material subscriber base, a sports channel will need to offer regular coverage of attractive sporting events. Since contracts for key sports rights are staggered with several years between the sales of those rights, current holders of key content possess an advantage when bidding for additional rights;

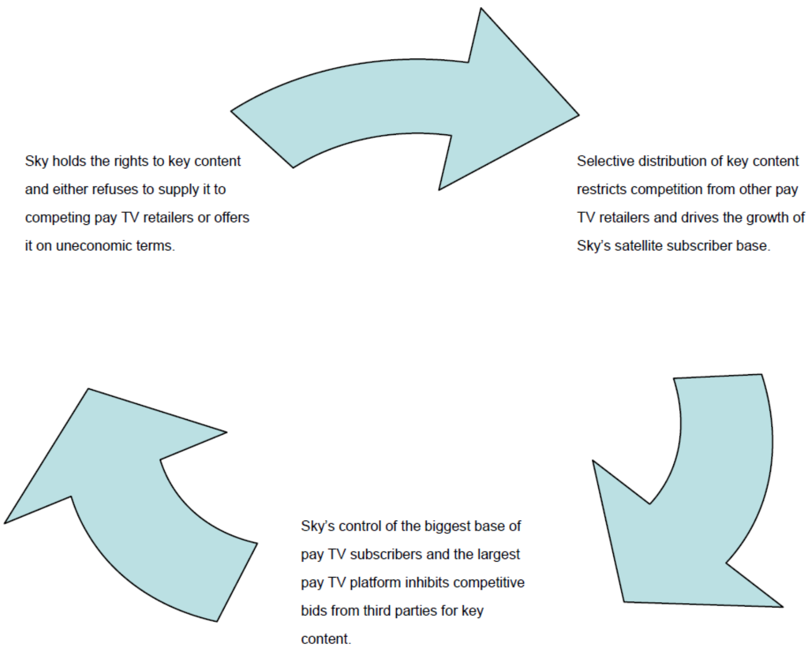
d. ***Selective distribution of key content***: The selective distribution of that key content (e.g. the refusal to wholesale channels to other pay TV providers or RSPs) inhibits downstream competition. For example, as noted at paragraph 21, Sky has failed to provide commercially viable wholesale access to their pay TV products to Spark and other RSPs; and

e. ***Economies of scale in the distribution of content***: A larger subscriber base enables a broadcaster to reduce its average content acquisition costs and this downstream advantage provides it with an ability to outbid its rivals in the competition for key content.

40. These dynamics have been referred to overseas as the "vicious circle",[20] i.e. because the only way that new pay TV entrants (e.g. RSPs) could outbid Sky to achieve a sufficient bundle of premium sports content is if they had guaranteed revenues from a sufficient subscriber base, but they only way they can grow their subscriber base is by having access to a sufficient bundle of premium sports content.

41. The vicious circle is demonstrated in Figure 2 below.

Figure 2 - The "vicious circle" of premium sports content acquisition [21]



[20] British Telecommunications et al "Submission to Ofcom on the need for a market investigation into the pay TV industry" (3 July 2007) Ofcom at [10]. Accessed at: http://stakeholders.ofcom.org.uk/binaries/broadcast/reviews-investigations/pay-tv/submission1.pdf.

[21] British Telecommunications et al "Submission to Ofcom on the need for a market investigation into the pay TV industry" (3 July 2007) Ofcom at [10].

42. Even in comparison to overseas jurisdictions, Sky's entrenched market power over the pay TV / premium sports content market is further exacerbated because:

    a. Sky is vertically integrated into the FTA market through its ownership of the Prime FTA channel; and

    b. New Zealand, unlike most other developed countries around the world, has no "anti-siphoning" or "designated events" broadcasting regulation to prevent a single broadcaster from monopolising the acquisition of sports content in New Zealand.

43. The reason Sky's vertical integration with Prime exacerbates this market power is because, when bidding for premium sports content, Sky can (i) provide rights holders with a guarantee of showing FTA as well as pay TV coverage (if having the sport shown FTA is an objective of the rights holder), and (ii) build in advertising revenue from both subscriber and FTA (and often also pay TV) channel advertisements, in addition to subscription revenues, to further ensure it outbids all other bidders for almost all premium sports content across both pay TV and FTA platforms. For similar reasons, Sky can use its market power in pay TV to ensure it outbids all other bidders for premium sport digital and mobile rights (to the extent the right owner chooses to auction those separately from pay TV broadcast rights).

44. Accordingly, despite the merging parties' assertions to the contrary, the evidence is that any party seeking to meaningfully enter or expand in pay TV in New Zealand would require access to premium sports content from Sky as a "must-have" input. Due to the vicious circle dynamic described above, unless wholesale access to Sky's content is provided on commercial / competitive terms to other entrants, including broadband and mobile RSPs, it is unlikely that any meaningful pay TV competitor to Sky will emerge in New Zealand, and likely that Sky will continue to have market power in the acquisition and wholesale of premium sports content in New Zealand.

With and without the merger

45. Spark's view is that:

    a. In the Counterfactual, Sky will be incentivised in the medium term (prior to 2021) to enter into commercially reasonable and competitive wholesale access agreements with a number of broadband and mobile RSPs in New Zealand, including more competitive digital and mobile sports content distribution - thereby enhancing content / innovation competition in the broadband and mobile markets, as well as ultimately facilitating new competition in the pay TV and premium sports content markets in New Zealand. This Counterfactual will lead to substantially more competitive:

        i. Pay TV and sports content acquisition markets vis-à-vis the Factual (and the status quo); and

        ii. Broadband/mobile markets vis-à-vis the Factual.

    b. In the Factual, the merged Sky / Vodafone will be incentivised to continue to constructively refuse to provide wholesale sports content access on commercially fair and reasonable terms to broadband and mobile RSPs in New Zealand, except for its vertically integrated Vodafone. This vertical foreclosure, given the "must have" nature of sports content, will lead to a substantial lessening of competition in the broadband and mobile markets.

WITHOUT THE MERGER:

46. The Sky / Vodafone Explanatory Memorandum (the "**EM**"), in describing the rationale for the merger, states that "Sky, and the entire media industry, is at a crossroads". Spark agrees with that assessment. The reason the pay TV / media industry has reached this crossroads is due to the ever-increasing willingness of consumers to consume TV content via digital (including mobile) channels, rather than traditional terrestrial or satellite channels. This was set out in the EM:[22]

> The growing consumption of media and entertainment services over the internet has permanently changed viewing behaviours, and requires greater ability to deliver content in new and innovative ways.
>
> SKY's Board and management team has been working on a vision to move SKY further into the media world of the future, where the focus is on enhancing the customer experience, innovation and one-on-one customer relationships.
>
> ...
>
> Throughout the world, increased smart-phone penetration and higher mobile data speeds show a clear trend towards greater consumption of entertainment content on mobile devices, which is in turn resulting in increased mobile data usage and higher data spend by mobile users.

47. This increasing consumer preference to consume TV content via digital channels has resulted in Sky suffering a 1.5% decrease in subscriber numbers last year,[23] and a decrease in net profit.[24] As Sky CEO John Fellet has said:[25]

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

48. This is leading Sky to increase its focus on digital (broadband and mobile) delivery platforms, and to look to RSPs that have expertise in providing that delivery to consumers. For example, in commenting on the merger, John Fellet has said:[26]

> *Will this remove the need for satellites, particularly in areas that have access to fibre?*
>
> Fellet: We're locked into our current satellite deal until 2021, so there'll be no movement ahead of that but one of the advantages of this deal is that it gives us access to Vodafone's expertise in UFB and **we certainly have plans to roll out internet-only packages to homeowners**. [Emphasis added]

49. If the merger were not to occur, in order to reverse its recent subscription and revenue decline, it is likely that Sky would seek to expand its distribution footprint by offering wholesale deals on fair and reasonable terms to attract broadband and mobile RSPs to resell its channels / content.

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[22] Sky Network Television Limited "Notice of Meeting and Explanatory Memorandum Relating to the Merger of the Businesses of SKY and Vodafone NZ" at 4.
[23] Tina Morrison "Sky TV shares sink 13pc as customer numbers drop" (6 May 2016) NZHerald. Accessed here: http://www.nzherald.co.nz/business/news/article.cfm?c_id=3&objectid=11634586.
[24] Paul McBeth "UPDATE: Sky TV first-half profit falls 5.8%" (26 February 2016) Scoop. Accessed at http://www.scoop.co.nz/stories/BU1602/S00878/update-sky-tv-first-half-profit-falls-58.htm.
[25] Ibid.
[26] Damien Venuto "Sky and Vodafone executives answer questions on the proposed merger" (10 June 2016) StopPress. Accessed at: http://stoppress.co.nz/news/sky-and-vodafone-executives-answer-questions-proposed-merger.

50. This trend is increasingly observed overseas. For example, in January 2015, BSkyB in the UK entered into a wholesale arrangement with mobile platform provider O2. Industry analysts CCS Insight observed in respect of this wholesale arrangement:[27]

> Sky was forced down this route. It can't afford to be left behind in the multi-play market. For now, Sky is the undisputed leader in triple-play services. Without mobile, it was vulnerable in the future. Our research suggests that consumers want to buy multi-play services from a single provider if they can.

51. Similarly, in July 2016 it was announced that Sky Deutschland and German mobile network operator Telefónica Deutschland have entered a partnership to offer Telefónica customers a suite of movies, television series, and live sports content (including the German football league Bundesliga and UEFA Champions League matches). Sky Deutschland said that "the agreement would enable it to reach a broader audience with Sky programming".[28]

52. Indeed, the EM refers to the merger as providing the combined Vodafone/Sky group "with the ability to deliver New Zealand's premium content over all forms of delivery technology, and provide customers with greater choice and an enhanced entertainment experience."[29]

53. In a world without the merger, Sky would, within a relatively short timeframe, be incentivised to enter into commercial partnering arrangements with a range of RSPs in order to deliver content over all forms of delivery technology, enhance the consumer experience, and provide the range of channel choices that consumers are increasingly demanding in their consumption of pay TV content. Given the merger proposal before the Commission, plainly the status quo is not a relevant Counterfactual, as the single distributor strategy Sky has developed with Vodafone is not sufficiently profitable for it to continue to be the sole digital distribution platform for Sky content. Instead, it is likely that Sky would:

    a. Increase the range of options of packages that it makes available at wholesale to RSPs, including resale of premium sport digital and mobile content rights;

    b. Increase the scope of RSP distribution it uses;

    c. Reduce the price of wholesale services / packages to RSPs to make the wholesale services more attractive to RSPs to bundle with broadband and / or mobile;

    d. Have the incentive to efficiently and collaboratively spread the costs of innovation, content acquisition, and development across a broad range of RSPs and content owners to achieve cost-savings in growing new delivery channels such as digital and mobile; and / or

    e. Enter partnerships with OTT providers and RSPs to enable Sky to leverage the commitment of those operators to

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[27] Christopher Williams "Sky responds to BT mobile attack with O2 wholesale deal" (29 January 2015) Telegraph. Accessed at: http://www.telegraph.co.uk/finance/newsbysector/mediatechnologyandtelecoms/telecoms/11376774/Sky-responds-to-BT-mobile-attack-with-O2-wholesale-deal.html.

[28] Jörn Krieger "Telefónica joins forces with Sky in Germany" (27 July 2016) Broadband TV News. Accessed at: http://www.broadbandtvnews.com/2016/07/27/telefonica-joins-forces-with-sky-in-germany/.

[29] Sky Network Television Limited "Notice of Meeting and Explanatory Memorandum Relating to the Merger of the Businesses of SKY and Vodafone NZ" at 4.

i. develop content delivery platforms and solutions, free up its own capital from such investment and achieve the savings and reach that it seeks to (otherwise) achieve through the merger; and

ii. more efficiently exploit digital and mobile content rights.

54. Acting independently, Sky is not incentivised to only distribute through Vodafone, because Sky sells its product to 55% of households, and Vodafone has a market share of 30% in broadband and 40% in mobile.[30] Sky needs to reach a much larger internet and mobile audience than that. Optimally it would want its products available to almost all RSPs' customers and marketed by all RSPs if it can achieve that.

55. Accordingly, in the Counterfactual, Spark expects that in the short to medium-term Sky will be incentivised to establish a sufficiently attractive wholesale offering for RSPs to obtain pay TV content from it on competitive terms in order for Sky to reach New Zealand consumers through broadband / mobile channels, to replace its declining satellite delivery platform.

56. In addition, in the Counterfactual, as RSPs grow their own pay TV media subscriber numbers through wholesale arrangements with Sky, they will each in turn, by breaking the vicious circle, become more viable competitors in the pay TV market in their own right, and over time, viable bidders for content rights in the premium sports content markets. This will in turn enable RSPs to increasingly be able to bid for further "add on" premium sports content directly, to differentiate their content package from Sky and other RSPs, thereby:

    a. Creating sports content differentiation and innovation competition between RSPs as a key driver of competition in the broadband and mobile markets, which will in turn grow consumer demand for content and increase uptake of UFB far more so than if the merger takes place;

    b. Creating new competition in the pay TV and premium sports content markets in New Zealand, being markets that are currently dominated by Sky and being competition that will not emerge if the merger takes place. As noted by the Commission in its investigation into Sky's misuse of market power in 2013, in a market that is already dominated by Sky, the loss of any potential nascent competition ought to be regarded as substantial:[31]

> [T]he higher the degree of market power already existing in a market, the more likely it is that any further lessening of competition will be substantial.

57. This is what has occurred in the UK, in particular in the form of entry and growing competition from BT Sport, as a result of the development of an active premium sports wholesale content market in that country (see the BT Sport case study in Appendix 3).

58. Spark has been a recent entrant in the New Zealand pay TV, sports content acquisition, and entertainment content acquisition markets. Spark has taken risks and sought to lead innovation and increase consumer choice and education by making high quality content options available through digital streaming on a range of devices including computers, tablets, smart TVs, video game consoles and mobile phones. Since 2014 we have learned that a successful media offering in New Zealand will be able to leverage off emerging consumer, market and technology developments. However we have also learned that access to key premium content, especially sport, is crucial to the development of any form of meaningful competition in the market.

[30] New Zealand Commerce Commission "Annual Telecommunications Monitoring Report 2015" (26 May 2016) at 22, 29.
[31] At [23.1].

59. **[ ] SPKCI**

60. The Counterfactual is accordingly substantially more competitive than the Factual in all of the New Zealand markets for:

    a. Retail mobile phone services where competitive content and mobile services will become more widely available to consumers;

    b. Retail residential broadband services where improved access to competitive media and broadband bundles will be more broadly available across the market;

    c. Pay TV as content aggregation and curation provides stronger competitive alternatives as competitive online services; and

    d. Acquisition and wholesale of live sports rights.

<u>WITH THE MERGER</u>:

61. The Sky / Vodafone clearance application asserts that "the Combined Group would not have the ability or incentive to engage in any foreclosure strategy – even putting aside that it will continue to make inputs available on a wholesale basis."[32]

62. There are two fundamental inaccuracies with that assertion:

    a. First, the Sky / Vodafone application portrays the current lack of wholesale arrangements between Sky and RSPs to be because "all but Vodafone have opted not to resell SKY services".[33] The reality is that Sky has not to date been willing to make its inputs available on a wholesale basis on commercially viable terms. As noted at paragraph 21, Sky has historically provided only limited, restrictive and, in Spark's view, uneconomic wholesale access to their pay television products by Spark and (as we understand it), other RSPs - in effect, a constructive refusal to deal by a firm with market power. This is reflected in the fact that, at present, only Vodafone has a wholesale resale arrangement with Sky, which illustrates that Sky has not, over a long period of time, offered commercially attractive terms to other RSPs. TelstraClear (as it was), for example, famously described its efforts to negotiate a wholesale content agreement with Sky as a commercial "pain point", noting that the “[t]he contract prevents us charging for content not sourced through Sky TV.”[34] The Commission itself has noted in its 2013 investigation into Sky that Sky's resale arrangements with RSPs did not reflect terms that would be offered in a competitive market,[35] and were motivated by an anti-competitive purpose.[36]

    b. Second, Sky / Vodafone are asserting that Sky's incentives will not change as a result of the merger. It is not credible to assert that a pay TV provider that increasingly needs to rely on internet / mobile distribution channels (see 46 to 49 above), will not have its incentives changed by vertically integrating with the largest / second largest RSP in the mobile and broadband channels. There is significant legal, economic, and regulatory literature confirming that incentives will change in those circumstances. For example, as

[32] Clearance Application by Vodafone Europe B.V. and Sky Network Television Limited (29 June 2016) at 3.
[33] Ibid, at [11.11].
[34] Chris Keall "TelstraClear boss - Sky TV partnership reaching 'pain point' " (17 April 2012) National Business review. Accessed at: http://www.nbr.co.nz/article/telstraclear-boss-sky-tv-partnership-reaching-pain-point-ck-116996.
[35] New Zealand Commerce Commission "Investigation Report on Sky TV contracts" (8 October 2013) at [308].
[36] Ibid, at [309].

noted by Vodafone UK in a submission to the European Commission's Digital Single Market Strategy review in 2015:[37]

> The incentive for vertically integrated providers is different. While there remains a degree of differentiation in the broadband and telephony elements that providers include in their bundles (in particular, broadband speeds), content is one of the most important ways in which providers differentiate their bundle from competing providers. Such a foreclosure strategy, in which content is only distributed over the vertically integrated network, will be successful in case of content that is sufficiently compelling to drive a significant number of consumers to switch ("ideally" the entire bundle). One of the key characteristics of such content is that it has no close substitutes, such as live sport events, where the consumer is interested in the coverage of a particular sport, league or team.
>
> …
>
> Content is not only increasingly sold in bundles, with the same company supplying content and connectivity to end users, but also increasingly owned by the distributor ... Consequently, content is more and more sold exclusively to customers of the distributor's own distributing services, e.g. broadband, or, if available to other customers, at less attractive conditions both in terms of quality and price.

63. To the extent that Vodafone is asserting something different to the Commission in the context of this transaction to what it has publicly stated elsewhere within the last 12 months, Spark suggests that the Commission should carefully test those assertions.

64. In respect of 62.a, Sky's conduct in the market to date demonstrates that unless it is forced by changed market dynamics to offer competitive wholesale terms to RSPs, it will not do so. Those changed market dynamics do arise in the Counterfactual as the "cross roads" been reached where Sky needs to expand its broadband / mobile distribution channels through contractual arrangements with third party RSPs (see paragraph 46 above).

65. Accordingly, Sky's current "willingness" to wholesale is not the relevant comparator for assessing the impact of the merger on competition. Rather it is necessary for the Commission to take a forward-looking view to consider Sky's incentives to enter into wholesale arrangements with RSPs in the future without the merger. In comparison to the Factual, that forward-looking Counterfactual is significantly more competitive than the scenario in which the merged entity can, and will, use its own broadband / mobile distribution channels (either exclusively or on preferential terms) to reach consumers.

66. In respect of 62.b, the Sky / Vodafone application asserts that no vertical issues arise because:[38]

    a. The combined group does not supply any "must have" inputs and, therefore, no *ability* to engage in foreclosure;

    b. The combined group does not have any *incentive* to do so in any event; and

    c. Even if it did, a substantial lessening of competition will not result.

[37] Vodafone submission to "Public consultation on the evaluation and the review of the regulatory framework for electronic communications networks and services" (2 December 2015). Accessed at: https://www.vodafone.com/content/dam/group/policy/downloads/01_12_2015_DSM_Framework_Review_Vodafone_submission.pdf.
[38] Clearance Application by Vodafone Europe B.V. and Sky Network Television Limited (29 June 2016) at [11.1].

67. From Spark's perspective each one of those assertions (i.e. 66.a, b, and c) is incorrect, as set out below.

Sky has "must have" sports content

68. For the reasons outlined at paragraphs 26 to 45, Sky's bundle of exclusive premium sports content is a "must have" input for others to compete with a full service pay TV offering in New Zealand.

69. Due to this "must have" nature of premium sports content as well as the convergence between pay TV and telecommunication delivery platforms, there is also a significant volume of industry, economic, and antitrust literature that identifies premium sports content as an essential / bottleneck input for competition in downstream broadband and mobile markets, in particular in the case of vertically integrated pay TV / RSP providers. For example:

    a. Vodafone UK:[39]

    > (vertically integrated) broadcaster[s] are becoming new bottlenecks and that the European Commission needs to do more to ensure the consumer has access to events of major importance and similar premium content, particular live sports events, and to enable distributors to offer this content in a consumer-friendly way.

    b. Economist Allan Fels in his submissions to the The OECD Roundtable on Competition Issues in Television and Broadcasting:[40]

    > While new platforms may increasingly provide enhanced levels of competition it seems clear that certain premium content can remain a source of market power. Sports content is a one such example. Seabright (2006) observes that post-digitisation: "content rights replace transmission bottlenecks as source of market power."

    c. Management consultants Arthur D. Little:[41]

    > In the UK, for close to 50% of broadband subscribers exclusive sport content offered by the operator plays a key role. Therefore, the acquisition of exclusive sport broadcasting rights becomes essential, especially when deploying a next generation network. Similar importance is attached to sports in Spain, Italy and France.

    d. Professor Carlo Cambini in a presentation to the Commission's 2013 Competition Matters Conference:[42]

    > - In TV, the most critical wholesale service is access to premium content (live-sports events or first-run movies).

[39] Vodafone submission to "Public consultation on the evaluation and the review of the regulatory framework for electronic communications networks and services" (2 December 2015). Accessed at: https://www.vodafone.com/content/dam/group/policy/downloads/01_12_2015_DSM_Framework_Review_Vodafone_submission.pdf.
[40]OECD Policy roundtables "Competition Issues in Television and Broadcasting 2013" at 371. Accessed at: http://www.oecd.org/daf/competition/TV-and-broadcasting2013.pdf
[41] Premium Sports Broadcasting" Arthur D Little at 2. Accessed at http://www.adlittle.com/downloads/tx_adlreports/ADL_Sports_Broadcasting_rights.pdf.
[42] Carlo Cambini "New regulatory and competitive issues in convergent communications markets" Presentation at inaugural Commerce Commission conference "Competition Matters" (Wellington, New Zealand, 17-18 October 2013). Accessed at http://www.comcom.govt.nz/dmsdocument/11560.

- Markets for such "essential" assets might emerge, when they are produced by several firms (wholesale competition).

- Does deregulation of "bottlenecks access" lead to an "efficient outcome"? **Not necessarily, especially if the companies are vertically integrated** (Bourreau et al., 2011 J Indust Ec).

70. Accordingly, for Sky and Vodafone to simply assert that the combined group will not have any "must have" inputs is disingenuous in the face of this significant volume of literature, as well the commercial realities of the New Zealand market where Sky has close to a monopoly across all premium sports content.

<u>The combined group will be incentivised to foreclose sports content to other RSPs</u>

71. As noted at paragraph 62.b, it is not credible for Sky/Vodafone to say that Sky's incentives to enter into wholesale content arrangements will not be changed as a result of the merger. The Vodafone UK submission, referred to at paragraph 62.b, accurately captures the way in which a pay TV provider's incentives change through vertical integration with an RSP.

72. It is well recognised that vertical integration by a pay TV provider into downstream telecommunications (broadband and mobile) markets will change a firm's incentives: [43]

> A principal concern arising from the convergence of content owners and network operators is the incentive for those firms to leverage their content advantage to drive subscribers to their communications networks.
>
> After a transaction, the merged parties might decide to restrict the access of competing pay-TV or OTT operators to key channels and/or content, with the objective of driving subscribers to the parties' own pay-TV platform through exclusive, or better-value, content offers.

73. Indeed Vodafone UK submitted to Ofcom just last year outlining its concern that "given the rise in converged services, content providers will be incentivised to leverage their rights of such 'key content' and limit distribution, in order to protect market share in adjacent markets... Ignoring the effects of 'key content' across wider and traditionally unrelated markets, such as mobile or broadband only customers, will have an enduring and irreversible effect, as the focus moves to TV bundled competition."[44]

74. This is also Spark's key concern, i.e. the incentives that the merged entity will have to use its market power in pay TV / premium sports content to drive consumers to Vodafone's broadband and mobile channels at the expense of other RSPs. This will either be achieved by:

    a. Full foreclosure - whereby the merged entity refuses to supply its premium sports content to other broadband and mobile RSPs; or

[43] "New powers for telecoms and media regulators? Part 2: convergence and regulation (December 2015) Oxera. Accessed here: http://www.oxera.com/Latest-Thinking/Agenda/2015/New-powers-for-telecoms-and-media-regulators-P-(1).aspx.
[44] Vodafone "Response to Ofcom's Consultation: Strategic Review of Digital Communications discussion document"
(8 October 2015) at 8-9. Accessed at:
http://stakeholders.ofcom.org.uk/binaries/consultations/dcr_discussion/responses/Vodafone.pdf.

b. Partial foreclosure - whereby the merged entity will only supply its premium sports content to other broadband and mobile RSPs on uncompetitive terms - i.e. a constructive refusal to deal (and continuation of Sky's approach to RSPs to date).

75. A vertically integrated pay TV / RSP firm's ability and incentive to engage in such a foreclosure strategy depends on:

    a. The type of content held by firm, which "must be sufficiently compelling to drive consumers to switch (ideally, across the entire multi-play bundle rather than just pay TV). In practice, this is likely to mean premium content such as sports, films or high-quality entertainment";[45] and

    b. The reach of the vertically integrated firm's platform: "if some proportion of the rival's subscribers are *unable* to switch to the vertically integrated platform—even if they wish to—the potential gains from the strategy will be muted".[46]

76. Both conditions in this case suggest that Sky / Vodafone will have both the incentive and the ability to profitably engage in input foreclosure:

    a. In respect of 75.a, paragraphs 26 to 45 and 68 and 70 illustrate that Sky's bundle of premium sports content is, and will be, sufficient to drive a significant proportion of New Zealand consumers to Vodafone for broadband and mobile if that is the only way to access Sky's sports content.

    b. In respect of 75.b, given Vodafone already has significant market share in both the broadband (~30%) and mobile (~40%) markets,[47] along with national coverage and national brand recognition, the reality is that a very significant proportion of other RSPs' customers would, and could, switch to the merged Sky / Vodafone entity for broadband and / or mobile services if that was the only way to purchase Sky Sports content on economic terms,[48] for example if Sky / Vodafone:

        i. did not offer competitive wholesale sports content packages to other RSPs, which means they could not offer their own bundled triple-play or quad-play packages; and/or

        ii. amended the pricing of its standalone (i.e. not bundle with broadband / mobile) Sky Sports packages to make the Sky / Vodafone bundled triple-play or quad-play packages appear more attractive than the standalone pay TV options.

77. Qualitatively, once the economic incentives of Sky and Vodafone are aligned through structural integration, it is evident that there would be significant scope for the merged Sky / Vodafone to shift margins between Sky and Vodafone to profitably engage in input foreclosure, for example:

    a. To forego potential standalone pay TV retail revenues by increasing, say, the price of Sky Sport Fanpass from, say, $55.99 to $65.99 if purchased as a standalone product, but

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[45] "New powers for telecoms and media regulators? Part 2: convergence and regulation (December 2015) Oxera. Accessed here: http://www.oxera.com/Latest-Thinking/Agenda/2015/New-powers-for-telecoms-and-media-regulators-P-(1).aspx.

[46] "Unscripted drama: vertical issues raised European pay-TV mergers (July 2015) Oxera. Accessed here: http://www.oxera.com/Latest-Thinking/Agenda/2015/Unscripted-drama-vertical-issues-raised-in-Europea.aspx.

[47] New Zealand Commerce Commission "Annual Telecommunications Monitoring Report 2015" (26 May 2016) at 22, 29.

[48] In this respect the vertical foreclosure ability / incentives concerns that arise from a Sky / Vodafone merger are significantly more acute than would arise if Sky was to, say, form its own start-up RSP (e.g. an RSP starting with 0% market share, no existing brand in the RSP space, no mobile network, etc).

reduce the price of Sky Sport Fanpass from $55.99 to $45.99 if purchased as part of a Sky Sport / Vodafone bundle, and recover that lost standalone revenue through increased triple-play and quad-play broadband / mobile revenue; and

b. To forego potential wholesale pay TV revenues by increasing the prices to other RSPs, so that their offers in market are not attractive, and recover that lost wholesale revenue through increased triple-play and quad-play broadband / mobile revenue.

78. In effect, the ability to internalise margin losses and gains within the combined Sky / Vodafone group will lead to Sky / Vodafone being able to offer significantly more attractive telecommunications / Sky Sports bundles than Vodafone has been able to offer to date through its arm's length contractual reseller agreement with Sky. This is why, as noted in the application, to date Vodafone's wholesale arrangement with Sky has not been a significant driver of market shares in the broadband and mobile markets,[49] but that Sky's vertical integration with Vodafone is likely to have a significant impact on market shares in the broadband and mobile markets post-merger (see further at paragraphs 81 to 98 below).

79. Spark suggests that the Commission request the necessary data from Sky and Vodafone to quantitatively demonstrate the ability / incentive for foreclosure, for example by:

a. Requesting data on the price elasticity of Sky Sport subscribers (approximately 65% of all its subscribers) - price reactions should be separated from churn arising from the scope of the product offering or other quality components of Sky's Basic + Sport package;

b. Requesting data on Sky's retail and wholesale pay TV revenue / margins, and Vodafone's retail telephone, broadband, and mobile revenue / margins, to assess whether or not there is a real risk that the upstream sacrifice of wholesale profits (from refusing to wholesale content to RSPs) could over time be compensated by the downstream increase in retail profits that the merged entity will receive from:

i. initially increasing the size of its broadband and mobile customer base, and then

ii. increasing prices to that increased customer base, without losing customers due to the "stickiness" of the sports content as a result of being the only firm that can offer an (attractively priced) triple- or quad-play bundle that includes premium sport content.

80. For example, while Spark does not have access to Sky and Vodafone's internal data, its expectation is that a significant proportion of the $435m in claimed merger revenue synergies will arise from pursuing an input foreclosure strategy. Spark cannot see where else an additional $435m of revenue could come from in the context of the pay TV market, where Sky is already leveraging its market power to the greatest extent permissible, and the broadband / mobile markets, which are currently highly competitive with low margins. Spark suggests that the Commission request modelling from Sky and Vodafone that outlines how those revenue synergies will be achieved.

<u>Foreclosure of sports content will result in a substantial lessening of competition in downstream broadband/mobile markets</u>

81. Again there is significant economic and antitrust literature that demonstrates that foreclosure of access to premium sports content to competing RSPs can result in a substantial lessening of

[49] With the terms Sky is wholesaling to Vodafone probably not significantly more attractive than the uncompetitive terms that were not accepted by other RSPs.

competition in downstream telecommunications (e.g. broadband and mobile) markets. For example:

a. The OECD's Triple and Quadruple Play Bundles of Communication Services report noted:[50]

> Communication regulators and competition authorities have been confronted with various challenges in their aim to apply conventional market definition and analysis to bundles of services. While bundling services may make economic sense for communication providers, **economic literature provides evidence that bundles can be used to substantially limit competition**: some market players may face constraints to replicate products and services if they do not have access to some important inputs that act as network bottlenecks or content (e.g. local loops, wireless access, competitive interconnection or the most popular **television content, such as the rights to offer sports and movies**). [Emphasis added]

b. The ACCC's *Media Merger Guidelines* set out that:[51]

> [A] merger between the television station and a mobile phone company may raise competition issues if it resulted in the television station's content being exclusively supplied to its just-acquired mobile phone operation where it was not previously possible for the television station and the mobile phone company to enter an exclusive agreement because of a market impediment (which the merger removed).

c. Vodafone UK has submitted that the effects of market power in the pay TV market:[52]

> are no longer isolated to TV or even Pay TV. Ignoring the effects of 'key content' across wider and traditionally unrelated markets, such as mobile or broadband only customers, will have an enduring and irreversible effect, as the focus moves to TV bundled competition. Vodafone ultimately remains concerned that if access to this content cannot be secured on Fair, Reasonable and Non Discriminatory terms, competition and consumer choice across a variety of telecommunications markets will be severely harmed.

82. Indeed, in circumstances where Sky has market power in premium sports content, the prospect that the merger will lead to Sky exclusively using Vodafone's broadband / mobile channels for the distribution of its premium sports content, or otherwise discriminating against other RSPs in wholesaling that content, is the type of outcome that has been identified in the ACCC's *Media Merger Guidelines* as of particular concern for downstream broadband / mobile competition:[53]

> Competition, for example, in the provision of access to consumers to the internet, may be stymied if companies, such as a particular Internet Service Provider (ISP) and a particular online media company with significant exclusive content, reach a mutually beneficial arrangement that discriminates against other companies. **For example, if the online media company provides preferential pricing to customers who subscribe to a particular ISP, then other ISPs may find themselves at a significant competitive disadvantage in attracting subscribers**. Alternatively, if an ISP provides a discriminatory deal for a

[50] "Triple and Quadruple Play Bundles of Communication Services" OECD Science, Technology and Industry Policy Papers. Accessed at: http://www.oecd-ilibrary.org/docserver/download/5js04dp2q1jc.pdf?expires=1470779385&id=id&accname=guest&checksum=218E6B8ACF1B4144DC3F6BBAB15D8CA2.

[51] Australian Competition and Consumer Commission "Media Mergers" (August 2006) at [48] - [49]. Accessed here: https://www.accc.gov.au/system/files/Media%20Mergers%20-%202011.pdf at 162.

[52] http://stakeholders.ofcom.org.uk/binaries/consultations/dcr_discussion/responses/Vodafone.pdf

[53] Ibid, at 50.

> particular online media company, such as not charging its subscribers for downloads from the sites associated with that online media company, then other online media companies may find themselves competitively disadvantaged in attempting to compete for consumers.
>
> Clearly, arrangements such as discriminatory pricing, the bundling of products or the tying of products such as ISP services and online media, are more likely to raise competition concerns where either (a) one or both of the companies involved in the arrangements has a significant degree of market power in one of the products relevant to the arrangement; or (b) where the arrangement itself is likely to lead to one or both of the companies involved in the arrangement achieving a significant degree of market power through the operation of the arrangement. Thus discriminatory pricing between an ISP and a particular online media company is more likely to raise competition concerns if either (a) the ISP, or the online media company, or both have a significant degree of market power in their particular parts of the service delivery chain relating to the products being priced on a discriminatory basis; or (b) the companies are so placed that the discriminatory pricing is likely to lead to the ISP, the online media company, or both gaining a significant degree of market power and, as such, reducing competition. [Emphasis added]

83. The Commission itself has also recognised the competitive disadvantage to RSPs that cannot access Sky's content:[54]

> [A]n RSP that sells Sky's content is likely to be at a competitive advantage compared to its rivals that do not ... This disadvantage arises from Sky's range and depth of services, brand etc compared to a different pay TV provider.

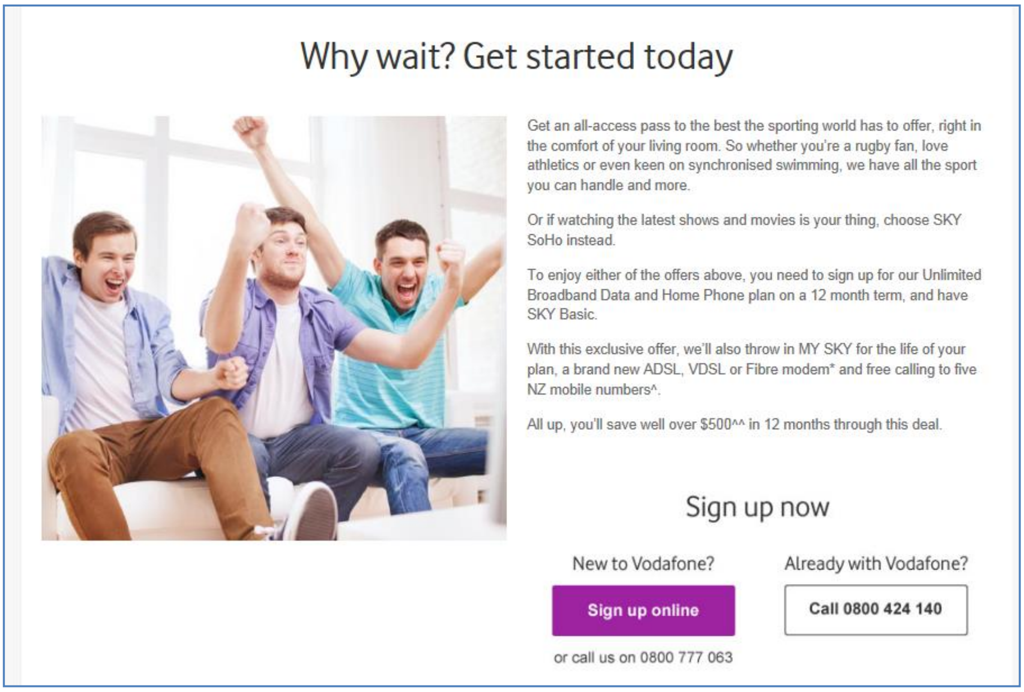
84. In the application, Sky / Vodafone seek to assert that access to Sky's content is not a competitive advantage on the basis that, despite Sky and Vodafone currently having a wholesale agreement, "broadband market shares have remained relatively constant over recent years".[55] The reason for that dynamic, as Spark understands it, is because Sky has not offered sufficiently compelling commercial terms to Vodafone to date to drive significant consumer preference for Vodafone's triple-/quad-play bundle over and above purchasing Sky and telecommunications services separately. That will change once Vodafone is part of Sky (for the reasons outlined at paragraphs 71 to 80).

85. Indeed, already since the announcement of the merger, after years of reselling Sky content, Vodafone has been active in the market announcing significantly more attractive triple-play bundles - for example free Sky Sport for a year and free My Sky, as below:

[54] New Zealand Commerce Commission "Investigation Report on Sky TV contracts" (8 October 2013) at [123] and [244.2].

[55] Clearance Application by Vodafone Europe B.V. and Sky Network Television Limited (29 June 2016) at [11.12].

Figure 3 - Recent Vodafone marketing of Sky bundles [56]



[56] "Get Sky sport or SoHo free for a year" Vodafone New Zealand. Accessed at: http://www.vodafone.co.nz/freesky/.

Figure 4 - Recent Vodafone marketing of Sky bundles [57]

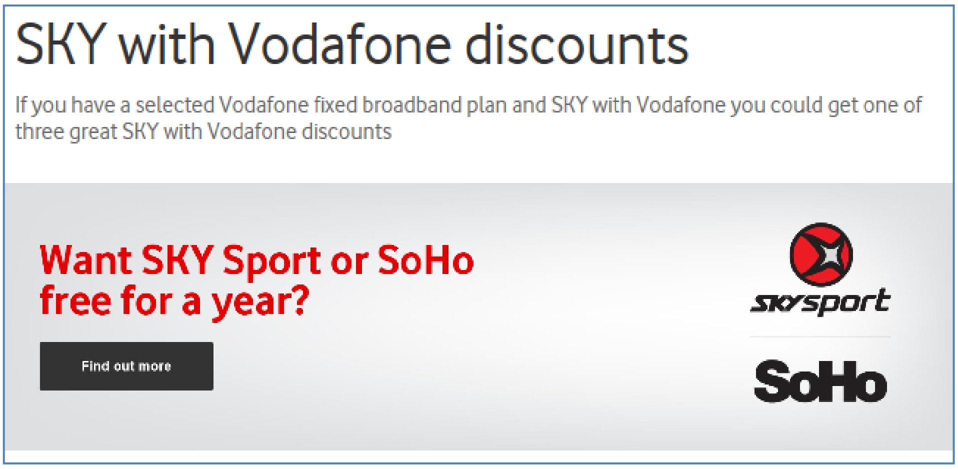


Figure 5 - Recent Vodafone marketing of Sky bundles[58]

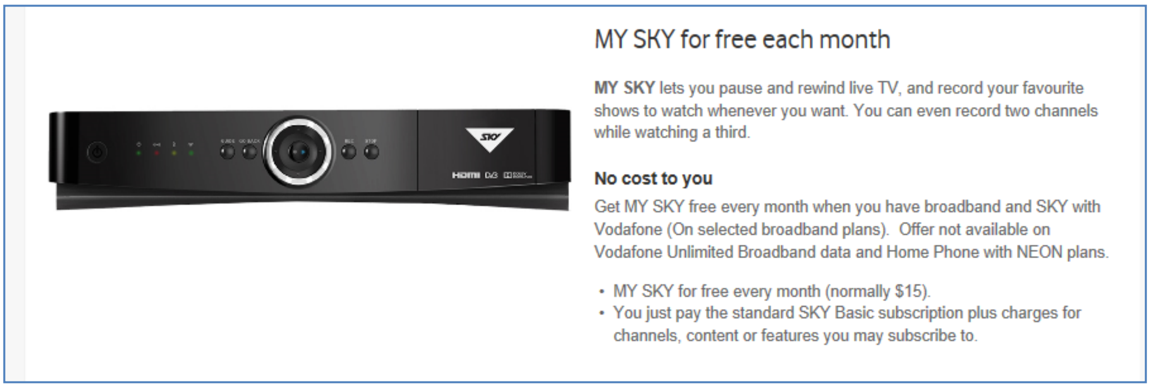
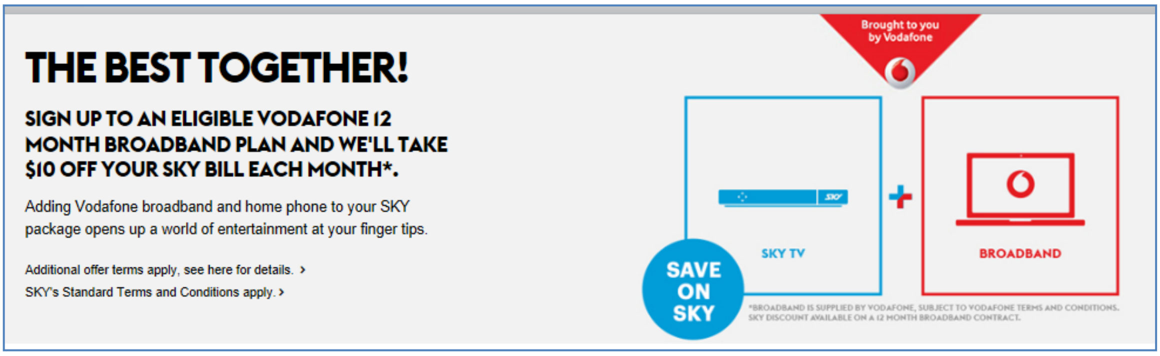


Figure 6 - Recent Sky marketing of Vodafone bundles[59]



86. **[ ] SPKCI**

[57] "Sky with Vodafone discounts" Vodafone New Zealand. Accessed at: http://www.vodafone.co.nz/tv/sky-with-broadband/package-discounts/.
[58] Ibid.
[59] "Sky TV offers and packages for new customers" Sky New Zealand. Accessed at: https://www.sky.co.nz/offers.

87. For the reasons outlined at paragraphs 71 to 80, it is inevitable that the merged entity will further focus on incentivising customers to switch to Sky / Vodafone triple-play and quad-play bundles, in comparison to pricing / terms made available on standalone Sky pay TV content, and that will be to the detriment of other RSPs ability to attract customers.

88. In particular, it is expected that the ability to receive the Sky Sports bundle will become an increasingly important element to compete for consumers in the broadband and mobile markets:

    a. At present, **[ ]** % **SPKCI** of Sky Basic customers in New Zealand subscribe to the Sky Sports package, which indicates that these customers primarily take on the basic subscription in order to access premium sports (without sports, most of the elements that make up Sky Basic would be available from other providers at significantly lower cost - see Figure 1). This equates to [ ] **SPKCI** households in New Zealand currently subscribing to Sky Sports. That in turn represents approximately [ ] **SPKCI**% of total fixed line broadband connections in New Zealand.[60]

    b. It is being observed internationally that, due to convergence, consumers increasingly want to purchase broadband services as part of a bundled offer with pay TV. For example, 44% of EU consumers now purchase their broadband and / or pay TV service as part of a bundled offer. [61] This means that access to key content is a significant driver of consumer choice of broadband/mobile provider, as outlined by Vodafone UK in its recent submission to Ofcom:[62]

    > As network convergence becomes a reality, TV and video content is now provided not just over satellite or cable systems, but over a standard broadband connection. Audio visual content has driven the take up of 4G mobile services: convergence may soon be the norm. Triple play and quad play consumer packages mean that the capacity of 'key content' to act as a significant driver of consumer choice influences not just the choice of Pay TV provider but the telecommunications services provider as a whole.

89. This demonstrates that a significant proportion of the broadband / mobile markets would switch to the merged Sky / Vodafone if either:

    a. There are material discounts for purchasing a triple-play or quad-play offer in comparison to purchasing pay TV and RSP services separately; and/or

    b. The merged Sky / Vodafone entity is the only place that consumers can access the convenience (at attractive prices) of a triple-play or quad-play bundle.

90. While that switching "may indicate the good deal that consumers are getting from bundled package in the short term... when a driver of consumer choice, key content, is left largely

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[60] New Zealand Commerce Commission "Annual Telecommunications Monitoring Report 2015" (26 May 2016) at 22, 29.

[61] "New powers for telecoms and media regulators? Part 2: convergence and regulation (December 2015) Oxera, quoting Ofcom "The Communications Market Report" (6 August 2015) at 289. Accessed here: http://www.oxera.com/Latest-Thinking/Agenda/2015/New-powers-for-telecoms-and-media-regulators-P-(1).aspx.

[62] Vodafone "Response to Ofcom's Consultation: Strategic Review of Digital Communications discussion document" (8 October 2015) at [3.1]. Accessed at: http://stakeholders.ofcom.org.uk/binaries/consultations/dcr_discussion/responses/Vodafone.pdf.

unchecked, it can easily translate into a re-monopolisation of network services" (as set out by Vodafone UK in its recent submission to Ofcom).[63]

91. Furthermore, in addition to customers willingness to switch to Sky / Vodafone, it is recognised that the ability to offer triple-play or quad-play bundles materially lowers the rate of customer churn:[64]

> "Service Providers view the multiplay bundle as both a marketing vehicle and a churn mitigation tool," said Ben Piper, Director of the Strategy Analytics Multiplay Market Dynamics ... "And survey research we've just fielded in the UK shows that quad play does provide a measurable amount of 'churn insulation,' or 'stickiness.' Customers who subscribe to four services from the same provider are less inclined to defect."

92. These views on customer churn / stickiness are backed-up by **[ ] SPKCI** and**]** the Sky / Vodafone EM, which states that Vodafone's customers that currently take mobile, fixed line and TV services together result in "lower churn rates".[65]

93. Indeed, a reduction in churn / increase in stickiness has been identified in the EM as one of the key revenue synergies from the Vodafone/Sky merger:[66]

> These synergies are expected to include... a reduction in subscriber churn rates through the bundling of products. The Combined Group will be able to sell bundled fixed line and mobile, pay television and internet packages more effectively than either business under the existing alliance arrangements. Subscribers for these bundled packages are typically much "stickier" than subscribers to a single product (e.g. pay television or mobile phone).

94. For these reasons, Spark considers it likely that the merger will substantially lessen competition in the broadband / mobile markets. This will occur as Sky / Vodafone will be incentivised to:

    a. Restrict access to wholesale content by other RSPs (either by not supplying or not supplying on fair and reasonable terms); and

    b. Bundle broadband or mobile offers with "free" or "low cost" premium live sport in a way that cannot be replicated by other RSPs to drive large numbers of customers from other RSPs to the merged entity.

95. The outcome of that conduct will be that:

    a. Sky / Vodafone will gain broadband / mobile market share off other RSPs regardless of its broadband / innovation as there will be a significant proportion of the population that see it as the "must have" provider of premium Sports content bundled offers;

    b. Other RSPs, regardless of any other broadband quality / innovation that they offer, will not be able to win market share from Sky / Vodafone;

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[63] Vodafone "Response to Ofcom's Consultation: Strategic Review of Digital Communications discussion document" (8 October 2015) at 8-9. Accessed at: http://stakeholders.ofcom.org.uk/binaries/consultations/dcr_discussion/responses/Vodafone.pdf.

[64] Ben Piper "Number of UK Quad Play Homes Will Treble 2016" (9 August 2011) press release, Strategy Analytics. Accessed at: https://www4.strategyanalytics.com/default.aspx?mod=pressreleaseviewer&a0=5089.

[65] Sky Network Television Limited "Notice of Meeting and Explanatory Memorandum Relating to the Merger of the Businesses of SKY and Vodafone NZ" at 5.6.

[66] Ibid, at Appendix One, page 3.

c. Sky / Vodafone's triple-play / quad-play offers will materially enhance customers' stickiness to Sky / Vodafone, effectively tying a significant proportion of customers to Sky / Vodafone; and

d. Sky / Vodafone will be able to cross-subsidise broadband / mobile offers from the revenue it receives from its large (and non-replicable) pay TV sports subscriber base.

96. The result will be a substantial lessening of competition as:

a. Smaller RSPs will be squeezed out of the market, and the barriers to entry / expansion for new RSPs will be raised significantly as:

i. customers will be significantly more sticky to Sky / Vodafone;

ii. other RSPs will not be able replicate the premium sport aspect of the Sky / Vodafone bundle;

b. Larger RSPs that would otherwise in the Counterfactual be able to use wholesale access to sport content from Sky to develop their own innovative pay TV content services, to compete with Sky, will not be able to develop that aspect of content and quality differentiation. That loss of content differentiation and quality competition will, consistent with Commission's previous analysis of UFB uptake, also significantly retard the uptake of UFB in New Zealand:[67]

> Video content is likely to be the primary driver behind consumers' uptake of high speed broadband over the next several years. The rate of this uptake may be affected by the diversity of video on demand services that are available and the quality of content that they offer.

97. The resulting loss in competition, from both small and large RSPs, will mean that in comparison to the Counterfactual:

a. In time, once smaller RSPs have been squeezed out, Sky / Vodafone will continue to be able to attract and retain customers at significantly higher broadband and mobile prices; and

b. Sky / Vodafone will not need to innovate on the quality / content front to continue to attract consumers from other RSPs, whereas in the Counterfactual it would need to innovate on content and quality due to the emergence of a competitive wholesale sports content market.

98. Vodafone UK, in its 2015 submission to the EC, succinctly summarised the likely outcomes from vertical integration between an RSP and a pay TV provider with exclusive sports content:[68]

> Thus for customers subscribing to bundles, the variations in the price/quality between fixed line suppliers are not likely to have the same impact on their choice of bundle, as this is dominated by the exclusive availability of the content highly valued by these customers. **Accordingly, the market available for alternative suppliers is materially reduced**. [Emphasis added]

[67] New Zealand Commerce Commission "High speed broadband services demand side study: Final report" (29 July 2012) at [5]. Accessed at: \http://www.comcom.govt.nz/dmsdocument/8917.

[68] Vodafone submission to "Public consultation on the evaluation and the review of the regulatory framework for electronic communications networks and services" (2 December 2015) at 31. Accessed at: https://www.vodafone.com/content/dam/group/policy/downloads/01_12_2015_DSM_Framework_Review_Vodafone_submission.pdf.

Foreclosure of sports content will result in a substantial lessening of competition in pay TV and sports content acquisition markets

99. In addition to the downstream loss in competition in the broadband and mobile markets, for the reasons outlined at paragraphs 56, the merger will also substantially lessen competition in the pay TV and acquisition and wholesale of live sports rights markets vis-à-vis the Counterfactual. This is because the merger removes Sky's incentives to wholesale live sports content to RSPs and, therefore, prevents the ability of RSPs to break the "vicious circle" that currently entrenches Sky's market power in those markets.

100. This means that the nascent competition that is likely to emerge in the Counterfactual for the acquisition and wholesale of sports content rights, across broadcast, Internet, and mobile channels, will not emerge in the Factual. As the Commission noted in its 2013 investigation into Sky, in a market that is already dominated by Sky, the loss of any potential nascent competition ought to be regarded as substantial.[69]

Decline or Divest

101. For the reasons outlined above, Spark considers that the Commission should decline the merger in its current form because the Counterfactual is substantially more competitive than the Factual in all of the New Zealand markets for:

   a. Retail mobile phone services;

   b. Retail residential broadband services;

   c. Pay TV; and

   d. Acquisition and wholesale of live sports rights.

102. Before the merger can be allowed to proceed, in order to preserve competition in these markets, Sky should be required to divest its exclusive ownership of the bundle of premium sports rights. For example, Sky should provide an undertaking to divest the Sky Sports channels, and associated sports rights, to a separate entity that would then be able to (and have the incentive to) enter into wholesale distribution arrangements with Sky / Vodafone, Spark, and other RSPs and wholesale customers, on an arm's length fair and reasonable basis.

103. This divestment, while structural, would be similar in effect to the undertakings that have been required by antitrust regulators overseas when considering proposals by pay TV providers and RSPs to vertically integrate (where behavioural undertakings can be accepted). For example, as a condition of Telefónica receiving approval in 2015 to acquire 56% of pay TV provider Canal+ España, Telefónica was required by Spain's competition authority to commit to making 50% of its premium channel content, including premium sports services centred on Spanish top-tier football; Formula One motor-racing; Moto GP; international basketball; and coverage of the Olympic Games, available at wholesale to rival pay TV providers.[70]

104. It is critical to continued competition in the broadband and mobile markets that the Commission make similar (albeit structural) commitments a condition of the Sky / Vodafone merger.

[69] At [23.1].
[70] "Telefónica closes Canal+ Spain acquisition" (1 May 2015) Digital TV Europe. Accessed at: http://www.digitaltveurope.net/360992/telefonica-closes-canal-spain-acquisition/.

Analogy with Sky's vertical integration into the FTA market

105. For completeness, Spark notes that an analogy of the likely effect of Sky's vertical integration with Vodafone on broadband and mobile market can be seen in the effect on FTA competition that arose from Sky's vertical integration with Prime in 2006. That transaction has eliminated all sports content competition and sports content innovation in that FTA market. The ruinous effects on competition of that Sky / Prime transaction were predicted by industry participants at the time of the Sky / Prime acquisition. For example, TVNZ predicted:[71]

> "The acquisition will allow Sky to artificially over-bid the price of stand-alone rights to free-to-air content through cross subsidy of Prime from Sky's monopoly rent in the pay TV market," TVNZ said.
>
> TVNZ asked the Commission to hold a conference about the proposed acquisition, saying the purchase would have a "substantial and long-lasting effect" on the future of the broadcasting industry.

106. MediaWorks similarly observed that Sky's vertical integration into FTA (via its acquisition of Prime) is "possibly the biggest medium term threat to the future of free to air television" and could "cause the ultimate demise of competitive free to air television in this country".[72]

107. These predictions have proven correct in respect of premium sports content competition, with Sky's leverage of its market power in the pay TV effectively eliminating any competition from commercially funded FTA broadcasters for premium sports rights in New Zealand, with all major sporting events broadcast on a Sky / Prime pay TV / FTA combination:[73]

> In New Zealand there is very little choice when it comes to watching sport on television. You can either pay a small fortune to Sky for their sports coverage or you can watch a select few events delayed, usually on Sky's free to air channel Prime, or you can wait for a news bulletin for some highlights.
>
> We're rather deprived of sport on free to air television in this country due to the strangle hold monopoly that Sky Television has on sports rights. Contrast this in Australia where there are regularly live games on free to air television from a number of sporting codes. Even in the US, big sporting events like the Superbowl are broadcast on free to air channels.

108. Sky has also been accused of degrading the quality of its FTA sports coverage, for example by showing events significantly delayed, late at night, with multiple commercial breaks,[74] and / or even not promoting in advance (or at the last minute) the FTA coverage that a sporting event will receive on Prime.[75] For example:[76]

> According to TVNZ, viewers are not being well-served by Sky's "near monopoly" on live sport. It accuses Sky of using its deep pockets to "hoard" programmes

[71] "Regulator asked to deny Sky's Prime bid" (19 January 2006) The Age. Accessed at: http://www.theage.com.au/news/Business/Regulator-asked-to-deny-Skys-Prime-bid/2006/01/19/1137553704006.html.
[72] Geoff Cumming "The 'skulduggery' behind broadcasting's Sky wars" (31 May 2008) NZHerald. Accessed at: http://www.nzherald.co.nz/nz/news/article.cfm?c_id=1&objectid=10513580.
[73] "This is what happens when you have sport on free to air TV" (9 September 2013) Throng. Accessed at: http://www.throng.co.nz/2013/09/happens-sport-free-air-tv/.
[74] Kasia Jillings "Olympic fans angry at Prime TV's coverage" (29 July 2012) NZHerald. Accessed at: http://www.nzherald.co.nz/entertainment/news/article.cfm?c_id=1501119&objectid=10822942.
[75] "Olympics should be free-to-air live in NZ" (6 August 2016) NZHerald. Accessed at: http://m.nzherald.co.nz/sport/news/article.cfm?c_id=4&objectid=11687806.
[76] Geoff Cumming "The 'skulduggery' behind broadcasting's Sky wars" (31 May 2008) NZHerald. Accessed at: http://www.nzherald.co.nz/nz/news/article.cfm?c_id=1&objectid=10513580.

> and deny free-to-air viewers the opportunity to watch most sport. Using its free-to-air channel Prime, Sky can snap up both the pay TV and free-to-air rights to sporting events - but it shows them on Prime only on a 'limited, selective and delayed basis,"

109. Those outcomes are all illustrative of a firm with market power in one market leveraging that market power in another market to encourage consumers to purchase Sky subscriptions. Spark is concerned that Sky will have the same incentive, and ability, to leverage its market power into the broadband and mobile markets if is also allowed to vertically integrate into those markets through a merger with Vodafone (for the reasons outlined above).

110. Spark considers it important that the Commission reflect on the effects of the Sky / Prime transaction on FTA competition in considering the likely effects of the Sky / Vodafone transaction on broadband/mobile competition.

PUBLIC VERSION

[Confidential Appendix 1: [ ] SPKCI

Appendix 2: Castalia Report

Enclosed.

Appendix 3: BT Case Study

Spark commissioned UK economic consultants DotEcon to prepare a case study outlining the entry of BT, through BT Sport, into the pay TV market in the UK, and its current operations in that market.

Spark considers BT Sport to be an example of the type of new entry, and competition, in the pay TV and sports acquisition and wholesale markets that would emerge in the Counterfactual. This is because in the Counterfactual Sky would be incentivised, in the short to medium-term, to establish an attractive wholesale offering for RSPs in order to reach New Zealand consumers through broadband / mobile channels to replace its declining satellite delivery platform. The emergence of that premium sports wholesale offering would enable RSPs to break the vicious circle to become viable competitors in the pay TV and premium sports content markets in their own right.

Similarly, to the active wholesale market that will emerge in the Counterfactual, BT was able to break the vicious circle in the UK due to the emergence of content wholesaling by BSkyB in the UK. This occurred following the 2010 imposition by Ofcom of a wholesale must offer (WMO) obligation on BSkyB. That WMO obligation required BSkyB to wholesale its premium sports content (Sky Sports 1 and Sky Sports 2 channels) to other pay TV providers / RSPs at a reference price that was calculated on a retail-minus basis. The aim of the WMO obligation was to ensure competitors could "replicate Sky's broader bundles which contain core premium sports channels, recognising that many consumers now buy TV broadband and telephony as part of a wider bundle."

Since the imposition of the WMO obligation:

- BSkyB has wholesaled its premium sports channels to all pay TV competitors on the basis of commercial arrangements, with the exception of BT who acquired under the WMO terms (due to a commercial disagreement);
- The pay TV sector in the UK has continued to grow with Sky's key content offered by all major TV providers. In particular, BT and Talk Talk have experienced substantial growth in pay TV - moving from around half a million and 50,000 subscribers respectively in 2009 to one million each by 2014/15;
- Premium sports are now available on a greater number of platforms;
- The supply of sports and share of sport content expenditure has become less concentrated:
  - BSkyB's share of the provision of key sports content has fallen by 10% (from 90%); and
  - BSkyB's share of expenditure on sports rights had decreased from 60% - 80% in the 2010/11 season to 50% - 70% for the 2015/16 season; and
- Innovative pay TV content and broadband bundle products have been introduced.

While it is not possible to say whether these developments arose as a result of the WMO remedy or were the result of market trends, it demonstrates the significant impact on competition that will arise in pay TV, sports content, and broadband markets through the development of an active premium sports content wholesale market. That is a market that is likely to develop in the Counterfactual but not in the Factual (for the reasons outlined in the submission).

It should also be noted that BT, as a vertically integrated provider of network access, had significantly greater scale / scope to more quickly break the vicious circle than a standalone RSP (such as Spark). Nevertheless, in the medium term, Spark considers that an RSP in New Zealand could similarly start establishing a credible bundle of premium sports content rights to drive competition in the pay TV and premium sports acquisition markets, as well as driving greater content differentiation / quality innovation in the broadband/mobile markets and, consequently, greater uptake of UFB.

DotEcon's case study is as follows.

BT Sport

BT Sport is a relatively new player and is an interesting case because it represents a substantive investment by an incumbent telecommunications operator aimed at offering attractive content that can be bundled with broadband services.

Over the past three years, BT Sport has built up its portfolio by acquiring other sports channels and bidding successfully for exclusive rights to top-level sports events.

BT Sport's proposition relies on live football matches from a large number of top-tier football leagues in the UK, Europe and further afield.

BT has continued to expand its portfolio and now also caters for (amongst others) the UK's top division Rugby Union league (Aviva premiership Rugby), MotoGPTM and the Ultimate Fighting Championships (UFC).

Although BT has acquired a significant number of exclusive rights to broadcast top-level sport in the UK, it has stated publicly that it is not really its intention to compete directly with other pay-TV platforms, but rather in the broadband space. For example Mark Watson, CEO of BT TV stated that "whilst the media had often portrayed the launch of BT Sport as a battle between BT and BSkyB, that was not how the company itself viewed it. He said there was plenty of room in the TV market for both companies and that BT had gone out of its way to make it easy for Sky Sports customers to take BT Sport. He said the real battle from BT's perspective was for broadband customers."[77]

Rights

BT Sport built its reputation by focussing on exclusive rights for top-level sports events with a strong emphasis on football.

The core of BT Sport's proposition was established in 2013 with the acquisition of the rights to show 38 live English Premier League (EPL) matches per season under a three year deal starting in the 2013/14 season for a total amount of £738m over three years.[78] In February 2015, BT announced that it had acquired rights to show 42 live Premier League Saturday and midweek matches for three years (2016/17 to 2018/19 seasons).[79] This is an increase of four matches per season compared with the previous deal, but the new rights will cost BT £320m per season compared with the previous £246m per year.[80]

[77] http://presscenter.com/bt-sport-proving-a-major-hit-with-app-users/.
[78] The rights to show the remaining 116 live EPL matches per season for the three seasons were acquired by Sky for £2.28bn. See: http://www.bbc.co.uk/news/business-23527897.
[79] The European Commission launched an investigation into the FAPL's joint selling of media rights to the English Premier League in 2002, which ultimately resulted in commitments by the Premier League that "*after 2006 the tendering procedures for TV rights will ensure that there are at least two television broadcasters of live Premier League matches: the Premier League will create balanced packages of matches showcasing the Premier League as a whole, and no one broadcaster will be allowed to buy all of the packages. The Premier League will also examine, jointly with the Commission, the way in which the auctions are conducted to ensure that they do not exclude potential competitors.*" (http://europa.eu/rapid/press-release_IP-03-1748_en.htm?locale=en).
[80] http://sport.bt.com/sport-football/news/bt-sport-wins-rights-to-more-live-premier-league-matches-S11363959914966.

BT's acquisition of the EPL rights came in addition to the signing of rights to show live top tier football matches from countries such as Italy, France, Brazil and the US[81] and its acquisition of ESPN's UK and Ireland TV business in summer 2013. This acquisition included *"the ESPN and ESPN America channels and their live sports rights portfolio, including the FA Cup, Clydesdale Bank Scottish Premier League, UEFA Europa League, and the German Bundesliga.'*[82]

Some of BT Sport's major football rights deals are as follows:

- In July 2013, BT announced that it would be showing top matches from the FA Women's Super League exclusively on BT Sport. [83]

- In July 2013 BT announced that it had secured a four year shared rights deal that will see itself and the BBC (as the free-to-air broadcaster) become home to the FA Cup in the UK from 2014 to 2018, following on from its broadcasting of live matches from the FA cup in 2013-14.[84]

- In August 2013 BT announced that it would have exclusive coverage of Liverpool FC's pre-season friendly fixtures taking place throughout August.[85]

- In August 2013, BT announced that it would have exclusive rights to show live coverage of three Scottish Premiership (SPFL) matches meaning that in total BT Sport would be showing exclusively 30 live matches from the SPFL and an additional 10 Rangers games during the 2013/14 season.

- In November 2013 BT also announced its exclusive UK TV rights to UEFA Champions League and UEFA Europa League covering all 350 matches a season for three years from 2015/16. Before this agreement, no single UK broadcaster has previously held the rights to both of these tournaments simultaneously and BT agreed to pay £299 million a season for the privilege.[86]

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[81] http://home.bt.com/news/bt-life/bt-signs-four-more-live-football-match-deals-11363796825413.
[82] http://www.btireland.com/pr_2013_07_24_btsport_womensleague.shtml.
[83] http://www.btireland.com/pr_2013_07_24_btsport_womensleague.shtml.
[84] http://www.bbc.co.uk/mediacentre/latestnews/2013/fa-cup-rights. Note that in the UK, the FA Cup is a 'listed event' and must be made available to free-to-air channels. The listed events scheme is based on the 1996 Broadcasting Act (as amended), which "gives the Secretary of State for Culture, Media and Sport the power to draw up a list of sporting events of national interest.
No definition of "national interest" has been included in the relevant legislation but the DCMS has said that a 'listed event' is 'one which is generally felt to have special national resonance' and which contains 'an element which serves to unite the nation, a shared point on the national calendar, not solely of interest to those who follow the sport in question.' The purpose of listing an event is to make it available to all television viewers, particularly those who cannot afford the cost of subscription television. The current list is divided into two categories: Group A and Group B. For Group A events, full live coverage must be offered to qualifying broadcasters – broadcasters whose channels are available without payment to at least 95% of the UK population (i.e. BBC1, BBC2, ITV1, Channel 4, and Channel 5). Events listed in Group B may have live coverage on subscription television provided that secondary coverage is offered to qualifying broadcasters. The listing of events ensures that the broadcast rights to these events, if they are offered at all, must be offered to the main free-to-air terrestrial broadcasters on 'fair and reasonable terms'. Qualifying broadcasters are not obliged to bid for these rights, so it is possible that on some occasions listed events may not be shown by a qualifying broadcaster." (J Woodhouse, Listed Sporting Events, House of Commons Library Briefing Paper No 802, April 2016). The FA Cup falls into Group A.
[85] http://www.mynewsdesk.com/uk/bt/pressreleases/bt-sport-to-show-the-pick-of-liverpool-fc-friendlies-1076802.
[86] http://www.btireland.com/pr_2013_11_11_liverights.shtml.

- In addition to the live UK TV coverage, BT Sport also won co-exclusive (shared with News UK) mobile clip rights to the UEFA Champions League: "BT Sport has cemented its position as the UK home of the UEFA Champions League and UEFA Europa League today, after winning co-exclusive on demand online and mobile clip rights to all 350 matches per season. From 2015/16 BT Sport subscribers will not only be able to watch all UEFA Champions League and UEFA Europa League action exclusively live on BT Sport, they will also be able to watch clips of the action afterwards from all the matches on their mobile, tablet or laptop via the BT Sport app and www.btsport.com."[87]

- BT has held the exclusive UK rights to broadcast the German football Bundesliga extending the rights until 2017[88] and again to 2021[89]

- In February 2015 BT Sport announced an extension of its agreement to show exclusively live Serie A football until 2018.[90]

- In April 2016 BT Sport announced that it had extended its right to show the FA Cup for a further three years from 2018 until 2021. The deal maintains its agreement with the BBC for shared coverage of the competition.[91]

In addition to football, BT Sport has also acquired the rights to a host of other sports including exclusive rights to show the American NBA, the UFC, MotoGP, Tennis, Rugby Union, cricket and the World Rally Championships:

- In November 2013, BT announced an exclusive television partnership with the American NBA: "The new agreement will see up to 200 games throughout the season, appearing across BT Sport 1, BT Sport 2 and ESPN. There will be up to seven live games per week throughout the regular season and the first and second rounds of the Playoffs, as well as every game of the Conference Finals, culminating in the NBA Finals in June ... Comprehensive Coverage Includes Exclusively Live TV Broadcast of up to Seven Games per Week, plus Highlights, Magazine Shows and Streamed Games on BT Sport.com" [Note the press release does not expand on 'multi-year' agreement].[92]

- BT Sport has exclusive rights to the UFC Ultimate Fighting Championship (UFC). The deal allows BT to show more than 30 live events per year, (including all the UFC's numbered pay-per-view events), as part of the BT Sport package.[93]

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87 http://www.mynewsdesk.com/uk/bt/pressreleases/bt-adds-co-exclusive-clip-rights-to-live-uefa-champions-league-and-europa-league-coverage-1077585.
88 http://sport.bt.com/football/news/bt-sport-extends-exclusively-live-bundesliga-coverage-S11364067853665.
89 http://sport.bt.com/football/news/bt-sport-extends-exclusively-live-bundesliga-coverage-S11364067853665.
90 http://www.mynewsdesk.com/uk/bt/pressreleases/bt-sport-extends-exclusively-live-serie-a-football-deal-until-2018-1155921.
91 http://www.bbc.co.uk/mediacentre/latestnews/2016/fa-cup-rights.
92 http://www.mynewsdesk.com/uk/bt/pressreleases/bt-sport-and-nba-announce-exclusive-multiyear-television-partnership-to-bring-the-world-s-best-basketball-action-to-fans-in-the-uk-and-ireland-1077248.
93 http://sport.bt.com/more-sport-hub/ufc/ufc-news/christian-oconnell-joins-bt-sport-ufc-team-S11363870122470.

- In February 2013, BT announced that it "has a five-year deal with Dorna Sports for exclusive rights to televise motorcycle racing's premier contest, the FIM MotoGPTM World Championship, starting from the 2014 season, with the opening race in Qatar on March 23."[94]

- In May 2014 BT announced that it has signed an agreement with the Lawn Tennis Association (LTA) to cover that year's "showpiece summer grass court tournaments" ahead of the Wimbledon Championships.[95]

- In August 2014 BT Sport announced is agreement to broadcast live matches from the new European Rugby Champions Cup, the successor to the Heineken Cup, as well as the new European Rugby Challenge Cup exclusively on BT Sport: "In the European Rugby Champions Cup, BT Sport will show at least five matches exclusively live from each of the opening rounds of the tournament, plus two quarter-finals and a semi-final. The Final, which will be shown live on BT Sport, will be shared with Sky Sports."[96]

- In March 2015 BT announced more rugby would be broadcast on BT Sport following an agreement with the Aviva Premiership Rugby league for the next six seasons in "a ground-breaking new TV deal". BT was proud to state that "The top flight of English club rugby will be live on BT Sport until at least the end of the 2020-21 campaign." This extends an initial four-year deal BT had with the Premiership.[97]

- In August 2015 BT announced that BT Sport would show the Ashes Down Under in 2017/18: "as part of 210 days of exclusively live international cricket from 2016-2021. BT Sport is to become the home of The 2017/18 Australia vs England Ashes and will show all Australian home cricket internationals exclusively live in the UK, from 2016 to 2021, after winning a five-year rights deal."[98]

- In January 2016 BT Sport announced that it has secured the exclusive live rights to show the FIA World Rally Championship (WRC) for the 2016, 2017 and 2018 seasons.[99]

- In May 2016 BT Sport signed a new deal to show up to 52 live Women's Tennis Association (WTA) tournaments every year. BT announced that "[t]he new deal from January 2017 reiterates BT Sport's commitment to women's tennis, with the UK broadcaster screening up to 52 events each year, an increase of 30 events per year on top of the current deal. BT Sport will also have the digital rights to broadcast tennis clips

[94] http://www.motogp.com/en/news/2014/02/14/bt-sport-announces-motogp-programmes-and-presenters/163397.
[95] http://sport.bt.com/more-sport-hub/more-sport/bt-sport-to-show-summer-grass-court-tennis-S11363906096130.
[96] http://www.btireland.com/pr_2014_08_28_exclusiverugby.shtml.
[97] http://www.premiershiprugby.com/news/35294.php#.V6zqUdIkq74.
[98] http://www.mynewsdesk.com/uk/bt/pressreleases/bt-sport-to-be-the-home-of-the-2017-18-ashes-1206049.
[99] https://www.mynewsdesk.com/uk/bt/pressreleases/bt-sport-extends-fia-world-rally-championship-deal-for-three-more-years-1366216.

> and WTA content on Facebook, Twitter, Instagram and YouTube."[100]

Furthermore, In January 2015 BT announced a deepening of its relationship with ESPN following its acquisition of ESPN's UK and Ireland TV business in 2013. This new relationship is based on a seven-year agreement signed between BT and ESPN granting BT even greater access to broadcast US sports: "As part of the new deal, BT Sport has the opportunity to use the ESPN brand in a range of different ways with ESPN remaining part of the BT Sport channel lineup for the long-term. The deal will see BT Sport expand the amount of programming it receives from ESPN, up to 5000 hours per year. Among a wide range of content, programming supplied during the course of the agreement will typically feature the Verizon IndyCar Series, NCAA College Football and Basketball, X Games, the AFL (Australian Football League) and more." [101]

Availability and pricing

When BT Sport was launched in August 2013, BT made the channel available for free for the first day to anyone with Freeview, TV from BT or a Sky television subscription. BT Sport remained available for free to those customers who had a BT broadband subscription, who would be able to access the content online, and via TV (either through a BT TV set-top bix or through their Sky box for customers who had a BT broadband subscription, but accessed TV from Sky). A HD version of the channel was available for £3 per month.[102]

Upon launch, customers without BT Broadband were able to access the channel via Sky for £12/month (or £15/month for the HD version).[103] In addition, BT signed a wholesale agreement with Virgin Media (the cable TV provider in the UK), which allowed Virgin Media customers subscribing to the TV XL package to view BT Sport for no extra cost.[104]

At the time of writing, the BT Sport pack remains free for all BT broadband customers (BT infinity customers with BT TV can get BT Sport in HD for a small additional fee of £5 per month).[105] BT broadband customers can also watch BT Sport through the BT Sport app and online player on their computer, smartphone or tablet. Access through the app is proving popular – in September 2013 BT reported that "[m]ore than a million homes will have soon downloaded the App and, whilst many of those can also watch via their TVs, there are literally hundreds of thousands of people who have chosen to watch exclusively online."[106]

Recently, BT has also announced that EE's monthly mobile subscribers (now part of BT's overall group following its acquisition of EE in January 2016) will be able to access BT Sport for free for six-months.[107] BT Mobile only customers can watch on their smartphones using the app. Normally, BT mobile customers will be charged £6 per month for

[100] http://sport.bt.com/more-sport-hub/more-sport/bt-sport-extends-live-womens-tennis-rights-S11364061703000.
[101] http://espnmediazone.com/espnuk/press-releases/2015/04/bt-sport-and-espn-deepen-relationship-with-long-term-collaboration/.
[102] http://www.mynewsdesk.com/uk/bt/pressreleases/bt-sport-opens-up-channel-for-first-day-on-tv-1076801.
[103] http://www.mynewsdesk.com/uk/bt/pressreleases/bt-sport-opens-up-channel-for-first-day-on-tv-1076801.
[104] https://www.btplc.com/BTToday/NewsList/BTandVirginMediasignBTSportdeal/index.htm.
[105] https://www.productsandservices.bt.com/products/manage-bt-sport-on-tv/.
[106] http://presscenter.com/bt-sport-proving-a-major-hit-with-app-users/.
[107] https://www.theguardian.com/media/2016/jul/11/ee-mobile-bt-sport-premier-league-european-club-football.

accessing BT Sport online or through the app if they do not have any BT broadband subscription.[108]

The BT Sport pack is currently available via the Sky Digital platform for non-BT customers at £21.99/month (or £26.99/month for the HD version after an initial three month period at the SD price). There is also a £15 activation fee.[109] BT broadband customers who are not using BT TV (or BT TV customers who want to have access to the pack simultaneously on Sky and BT TV) can get the channels on the Sky platform for £6/month.[110]

For Virgin Media customers, the BT Sport pack remains free for subscribers to the TV XL package, and can be added to other Virgin TV packages for £18 per month (including the HD channels).[111]

The pricing of BT Sport is a clear example of bundling of the channel with BT's broadband (and to a lesser extent mobile) offering, with BT broadband customers enjoying savings of around £20 per month. Moreover, BT has 'zero-rated' streaming of the BT Sport channel over its network. Whilst many of BT's high-speed "infinity" packages have an unlimited data allowance, some of the cheaper broadband packages available (such as "Broadband" - up to 17Mb/s and a data cap of 12GB per month for £5 a month; and "Infinity 1" – up to 52Mb/s and a data cap of 25GB per month for £10 a month[112]) have a monthly data cap. Streaming of BT Sport will not count towards this data allowance when watching BT Sport using BT Broadband or a BT Wi-Fi hotspot. However, if customers are watching over mobile data connection, this will count towards usage allowance and may incur a charge.[113] At this point in time, there are no indications that this applies differently for BT mobile or EE customers.

Subscriber figures and revenues

Within just three months of launching BT Sport, BT announced that it had passed the million subscriber mark: "More than a million households are ready and equipped to enjoy the start of the Barclays Premier League on BT Sport this coming weekend. BT only began to accept orders on May 10, so the million customers for BT Sport have been added in just three months."[114]

BT has continuously reported improved results since the launch of BT Sport, focusing in particular on the implications for broadband services. For example for the second quarter and half year to September 2013 BT reported: "BT Sport has made a confident start and is already delivering for viewers. More than two million of our customers are signed up to it and our wholesale contract with Virgin Media means it is available to around four million homes in total. It is also delivering for the business, **helping us achieve a record 93% share of broadband net adds in the quarter, our lowest line losses**

[108] https://recombu.com/digital/article/bt-sport-new-prices-sky-virgin-media-bt-tv-mobile.
[109] http://www.productsandservices.bt.com/products/bt-sport-on-sky-packages?s_intcid=con_sportoverview_to_skyonly.
[110] See BT sport FAQs, "How do I get BT Sport Pack?" https://www.productsandservices.bt.com/products/broadband-packages.
[111] https://recombu.com/digital/article/bt-sport-new-prices-sky-virgin-media-bt-tv-mobile.
[112] Prices and packages correct at the time of writing. Note that both of these packages require a monthly line rental of £18.99 per month. See https://www.productsandservices.bt.com/products/broadband-packages
[113] See BT Sport Frequently asked questions: "When I use the BT Sport app and online player will it count towards my BT Broadband usage allowance?" https://www.productsandservices.bt.com/products/broadband-packages.
[114] http://www.businessfirstonline.co.uk/other-articles/bt-sport-passes-the-million-mark-in-just-3-months/.

for five years and 4% revenue growth in our BT Retail Consumer business."[115]

In the third quarter and nine months to 13 December 2013, BT reported: "Our direct BT Sport customer base passed 2.5 million in the quarter and helped to support **6% revenue growth in our Consumer business**. We achieved some particularly strong audience figures in December and the exclusive rights to the UEFA Champions League and UEFA Europa League that we have won will further strengthen the appeal of our proposition."[116]

Again in fourth quarter and year to March 2014, BT reported "BT Sport has proved very popular and we are delighted the service is now in around five million homes. For BT Consumer it underpinned **a record 9% growth in revenue in the fourth quarter and the lowest line losses in over five years. We achieved an excellent 79% share of broadband market net additions in the quarter."** [117]

END

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[115] http://www.mynewsdesk.com/uk/bt/pressreleases/bt-group-plc-results-for-the-second-quarter-and-half-year-to-30-september-2013-1077623; emphasis added.
[116] http://www.prnewswire.com/news-releases/bt-group-plc-results-for-the-third-quarter-and-nine-months-to-31-december-2014-300028401.html; emphasis added.
[117] http://www.prnewswire.com/news-releases/bt-group-plc-results-for-the-fourth-quarter-and-year-to-31-march-2015-300079499.html; emphasis added.