BT's Response to Ofcom's review of the pay TV wholesale must-offer obligation

27 February 2015

NON-CONFIDENTIAL VERSION

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1. **<u>EXECUTIVE SUMMARY AND INTRODUCTION</u>**

1.1. BT welcomes Ofcom's review of the wholesale must-offer (***WMO***) obligation. The WMO Remedy was imposed in 2010 with the aim of facilitating the emergence of fair and effective competition in pay TV markets. Since that time, however, it is clear that fair and effective competition has not emerged: Sky's position remains entrenched and competitive constraints upon it are, at best, weak. In particular:

(i) despite the imposition of the WMO Remedy in 2010, Sky continues to be by far the largest operator at all levels of the pay TV value chain, with almost 11 million pay TV subscribers. Over the period, it has acquired an additional 1 million retail pay TV subscribers [✂] which gives it a retail revenue market share of 60% to 80% based on Ofcom's own analysis, and its adjusted operating profit has increased from £855m in 2010 to £1,260m in 2014. Sky's exceptionally low churn rate, is, today, the lowest it has been in a decade, and it has further consolidated and entrenched its overall market position in the pay TV sector with the development of NOW TV.

(ii) Sky's sports channels continue to remain an important driver of pay TV subscriptions, and underpin Sky's strong market position across the value chain. Sky continues to hold the vast majority of live sports rights on pay TV, and has further consolidated its position since Ofcom's investigation in 2010 with more live Premier League rights (in absolute and relative terms), the long-term renewal of most of the 'second-tier' rights that Ofcom identified in 2010 and the acquisition of new, important, second-tier rights such as F1 and the British Open golf championship.

(iii) In addition, the importance of Sky Sports to pay TV subscription decisions has enabled Sky to maintain a packaging structure whereby Sky TV customers must 'buy through' a pack of basic channels in order to access the Sky Sports channels, which also contributes significantly to Sky's overall pay TV revenues and profitability.

(iv) As a result of stringent wholesale regulation in the broadband sector, distortions in the pay TV sector have now spilled over into adjacent markets, where Sky is able to use its supernormal profits in pay TV to heavily discount its broadband products. As a result, Sky is now the largest provider of "triple-play" (fixed line, broadband, pay TV) bundles, and has grown to be the UK's second largest broadband retailer, with a retail market share of 23%.[1] The rapid growth of Sky's broadband position, to almost a quarter of the retail market (despite vigorous competition in retail broadband), contrasts sharply with BT's limited ability to gain purchase in retail pay TV markets,

[1] Sky's market share of retail broadband by number of subscribers estimated by BT as at the end of December 2014 based on the data in Sky's quarterly results.

and its acquisition of [✄] Sky Sports subscribers as a result of Ofcom's WMO Remedy.

1.2. It is essential, therefore that Ofcom now uses this review to address effectively the enduring issues with Sky's entrenched market position in order to ensure fair and effective competition in pay TV markets.

1.3. BT agrees that the focus of Ofcom's review should be on live sport given its continued importance for driving pay TV subscriptions, and the desire to avoid a further protracted review process. However, in conducting the review, Ofcom must have regard to market realities and the context that the strength of Sky's market position goes far beyond just its sports channels.[2] Equally, Ofcom's analysis must reflect the reality that live sporting events are sold collectively in premium sports channels and packages of sports channels. Those sports channels and packages of channels, not individual sports rights, are the products from which subscribers make their purchasing choices. Ofcom's focus must be on those sports channels and packages of channels that actually drive subscription decisions as otherwise Ofcom risks overlooking the full extent of the competition problems that undoubtedly remain in pay TV markets. Once Ofcom examines this issue comprehensively, Ofcom will conclude that access to the full Sky Sports proposition, and not a subset of the Sky Sports channels, is necessary to ensure fair and effective competition.

1.4. For the reasons set out in detail in this submission (the ***Submission***), the limited distribution of the Sky Sports proposition (either by not providing access at all, or by providing access only on terms that do not permit effective competition) materially impedes fair and effective competition. Sky currently enjoys a very high market share, typically associated with dominance, at both the wholesale and retail level and has material incumbency advantages at the retail level, as well as when bidding for sports rights (as clearly evidenced by the most recent Premier League auction). As a result, it has both the ability to impede fair and effective competition through the limited distribution of its Sky Sports proposition, and a strong incentive to do so in order to protect its strong market position across the pay TV value chain. This incentive is strongest vis-à-vis rivals such as BT, which, as a result of its considerable investment in BT Sport, is likely to be viewed by Sky as a greater threat to its market position.

[2] In particular, while BT notes that the regulation of Sky's basic and movies channels is not within the scope of the WMO Review, Sky's market strength at the retail level is also underpinned by the strength of its movies and basics propositions. This is relevant to the issue of the contestability of sports subscribers at the retail level, especially where a subscription decision is a household purchase and thus encompasses heterogeneous preferences. This context must be born in mind in Ofcom's assessment.

1.5. Going forward, BT believes that it is essential not only that the WMO Remedy is maintained, but that it is made fit for purpose. This means ensuring access to the Sky Sports proposition, on prices and terms that allow for fair and effective competition. It is manifestly clear that due to various methodological issues with the WMO Remedy, the regulated wholesale prices that Ofcom set in 2010 are too high to allow third parties to compete effectively. This has been compounded with the launch of NOW TV, with the Sky Sports channels now available at retail prices below Sky's wholesale charges. It is clear that the issue of appropriate wholesale prices for Sky Sports to ensure fair and effective competition is something that Ofcom will need to address in detail in the next phase of this consultation.

1.6. Ensuring effective competition means preventing Sky from limiting the distribution of its Sky Sports proposition by restricting the range of channels that it makes available or with-holding important additional services such as HD, interactivity, or access via multiple devices within the home. Ofcom must also ensure that it future proofs the remedy to be able to extend it swiftly to new, emerging technologies like 4K, Ultra HD or 3D, or new platform delivery technologies.

1.7. Sky must also be prevented from imposing terms and conditions that limit rivals' incentives to compete against it for sports rights by appropriating any investment in differentiation, or terms which limit or restrict package and proposition innovation.

1.8. BT also believes that Ofcom must revisit two specific aspects of its 2010 Statement, namely the applicability of the WMO Remedy to third parties on the Sky digital satellite (DSat) platform and the issue of commercial premises. Given low levels of switching in pay TV markets, Ofcom must consider the possibility of allowing rivals to sell Sky Sports on regulated terms directly to Sky's sports subscribers on the DSat platform in order to more swiftly deliver the benefits of retail competition to consumers. Ofcom must also address the fact that Sky's commercial premises revenues affords it an unchallenged, lucrative revenue source that it can use to underpin its bids for live sports rights, further underscoring Sky's bidding advantages.

1.9. Finally it is also important to be clear that given Sky's enduring market power across the pay TV value chain, it is *only* Sky that should be regulated. Unlike Sky, BT, as a new entrant has neither the ability nor incentive to limit the distribution of BT Sport in a way that would impede fair and effective competition. There is no evidential or legal basis for regulating BT Sport and it would be unlawful for Ofcom to do so. Ofcom should not, therefore, spend time unnecessarily analysing BT Sport, but rather must focus on Sky Sports as the sole source of barriers to fair and effective competition.

1.10. This Submission focuses on the fundamental issues that Ofcom must consider in discharging its obligations under the Communications Act 2003 (the ***Act***) to ensure fair and effective competition, and to enable it to design and implement a remedy that is proportionate and appropriate to address the competition concerns identified. BT's Submission, therefore, addresses:

(i) the nature and scope of market developments since 2010, which demonstrate the continued strengthening of Sky's market position, notwithstanding the introduction of the WMO Remedy in 2010 (**Section 2**);

(ii) the fact that Ofcom's analytical exercise identifying the importance of individual sporting events in isolation, which is divorced from the reality that live sporting events are sold collectively in premium sports channels and packages of premium sports channels, will fail to address the core issue as to the scope of the regulation necessary to ensure fair and effective competition in pay TV markets going forward. This section also demonstrates that Ofcom must ensure access to the full Sky Sports proposition, and not a subset of the Sky Sports channels (**Section 3**);

(iii) Sky's high and persistent market shares (at levels normally associated with dominance), at both the wholesale and retail level and its material incumbency advantages at the retail level and in bidding for sports rights. BT also addresses the fact that its strategy of monetising its sports rights investment indirectly by offering BT Sport for free to its broadband subscribers in no way undermines Sky's bidding advantages (**Section 4**);

(iv) the fact that limited distribution can take many forms including offering wholesale supply on terms and conditions that do not ensure fair and effective competition, or in a way that reduces the value of the Sky Sports proposition to consumers. BT also demonstrates that Sky (and only Sky) has the ability to impede fair and effective competition through the limited distribution of its Sky Sports proposition, to the detriment of consumers. (**Section 5**);

(v) the fact that Sky has both a static, and an even stronger dynamic, incentive to limit the distribution of its Sky Sports proposition, particularly vis-à-vis rivals such as BT, who are vertically integrated and hence also seek to acquire live sports rights. BT also shows that Sky has acted on these incentives in practice. (**Section 6**);

(vi) why supply of Sky Sports to commercial premises must form part of the WMO Review, as it cannot be divorced from the competition concerns in residential markets (**Section 7**); and

(vii) BT's views on Ofcom's conclusions and the next steps in the review, including the ways in which the WMO Remedy should be strengthened and future-proofed (**Section 8**).

1.11. In addition, BT provides the following annexes to assist Ofcom:

(i) An assessment of the legal and analytical framework applicable to the WMO Review, and the manner in which Ofcom should discharge its discretion in this review (**Annex 1**);

(ii) Responses to the questions in Ofcom's consultation document (**Annex 2**); and

(iii) Data and evidence tables supporting the substantive sections of this Submission (**Annexes 3 and 4**).

1.12. BT also provides a glossary to assist Ofcom with the abbreviations used in this Submission.

2. THE NATURE AND SCOPE OF MARKET DEVELOPMENTS SINCE 2010

The market context for Ofcom's WMO Review

2.1. This section considers the nature and scope of market developments since 2010. Although BT agrees with a number of Ofcom's descriptions of developments in the pay TV sector, BT is concerned that the implications of these developments are considered in a somewhat piecemeal fashion rather than in aggregate, and as a result in places materially overstate the extent of changes relevant to a review of the WMO Remedy. When taken together, the relevant market developments affecting the pay TV sector since 2010 have been: (i) the continued strengthening of Sky's market position, contrary to Sky's claims that the WMO Remedy would weaken its market position; and (ii) as a consequence of the limitations resulting from Sky not being effectively regulated in pay TV, the emergence of Sky as the UK's second largest broadband operator, in particular due to its ability to offer irreplicable triple-play bundles.

2.2. BT agrees with Ofcom that whilst there have been a number of developments in the distribution of pay TV content (particularly in the underlying distribution technologies) since 2010, certain features of the pay TV sector, particularly as regards the wholesaling and retailing of premium sports content, remain unchanged. In particular, BT agrees that:

(i) pay TV subscription revenues have continued to grow;[3]

(ii) pay TV subscriber numbers have also continued to grow and Sky continues to be by far the largest operator at all levels of the pay TV value chain;[4]

(iii) Sky continues to hold the large majority of important live sports rights, with many rights contracted for significant periods. Indeed Sky has consolidated its position since 2010. It now has more Premier League matches (in absolute and relative terms), has retained its strong position in relation to cricket, golf, tennis and rugby, and has also acquired additional important content such as F1 and the British Open golf championship;

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[3] As stated in the Consultation Document (paragraph 3.4 and Figure 3.1), pay TV subscription revenue has soared from £5.027bn in 2010 to £5.879bn in 2013 (5 year CAGR of 6.0%). In comparison, other forms of revenue – including advertising – are broadly flat; all have fallen when adjusted for inflation.

[4] As stated in the Consultation Document (paragraph 3.5), Sky has "*up to 10.7 million TV subscribers*", compared with 9.7 million at the end of 2010. As noted by Ofcom, Enders Analysis has estimated that NOW TV has in the region of 360,000 subscribers (as of September 2014). This would therefore suggest that Sky's DSat subscriber base is in the region of 10.34 million subscribers. This means that Sky has secured a net increase of in the region of 640,000 subscribers to its DSat platform alone since the introduction of the WMO Remedy in 2010.

(iv) the trend towards bundling of communications services which was seen in 2010 has become more prevalent; and

(v) the cost of live sports rights continues to be very high.

2.3. While Ofcom has identified these features of the pay TV sector, BT urges Ofcom as part of the WMO Review to consider critically the implications of these developments. In BT's view, the following points provide the essential factual context for Ofcom's analysis in this review:

(i) The growth in pay TV subscription revenues and pay TV subscriber numbers identified by Ofcom underscores the importance of this market for consumers, and the need for Ofcom to ensure fair and effective competition.

(ii) To date, Ofcom's regulatory intervention in this sector has not delivered effective competition. On Ofcom's own findings, Sky plainly has a market position that equates to a strong dominant market position, which has in fact strengthened since 2010. Sky has acquired an additional one million retail pay TV subscribers [✂], significantly increasing its lead over its closest rival, Virgin Media, (subscriber numbers for which have stagnated) which therefore exerts even less of a constraint than in 2010.[5]

(iii) Indeed, Sky's latest quarterly results highlighted that Sky has had its highest new customer growth in years with "*[g]rowing customer demand across the group [led by] significant outperformance in the UK and Ireland*", leading to "*TV growth that more than doubled*" with Sky adding, adding 202,000 new TV subscribers, versus 46,000 the previous quarter and 77,000 for the same quarter last year.[6] Sky's quarterly UK retail subscription revenue also grew by 4.2% to £1,659 million, and experienced similar growth in the previous quarter.[7] Moreover, despite regulatory intervention in 2010, and a difficult economic climate, Sky's profitability has

[5] As stated in the Consultation Document (paragraph 3.5), Sky has "*up to 10.7 million TV subscribers*", compared with 9.7 million at the end of 2010. By contrast, Virgin Media's base of 3.7 million subscribers remains "*broadly similar*" compared with the number it had in 2010.

[6] Q2 2014/15 Quarterly Results, page 4: "*Sky in the UK and Ireland had **an exceptional** Q2 with the investments in content and connected services delivering excellent operating growth across all areas of the business … Within this, **TV growth more than doubled to 202,000** and we saw good growth in broadband with 106,000 additions. The addition of 204,000 new retail customers in the quarter **was the highest rate of customer growth since 2005***". Jeremy Darroch commented *"[w]e have delivered an excellent operational and financial performance … the highest customer growth in nine years … the lowest churn in a decade*" (page 2).

[7] Sky results Q1 2014/2015 (page 5) and Sky results Q2 2014/2015 (page 19). Sky's Q1 2014/15 results showed that its retail subscription revenue was £1,592 million (an increase of 4% on the previous quarter). Sky's Q2 14/15 results state that retail subscription revenue for UK and Ireland for Q1 and Q2 was £3,251 million, indicating that subscription revenue for Q2 was £1,659 million, a quarterly increase of 4.2%.

increased from £855m in 2010 to £1,260m in 2014[8], with its latest quarterly results showing a 16% increase in half-year operating profit to £675m.[9]

(iv) Sky's pay TV churn rate also remains exceptionally low and has barely altered since the WMO Remedy was introduced in 2010. In Sky's recent quarterly report, Chief executive Jeremy Darroch highlighted that: "*Across the board, customers are responding to our investment in more high-quality TV and innovative new services. This has resulted in the highest customer growth in nine years, the highest total product growth in four years and* ***the lowest churn in a decade***"[10] (emphasis added).

(v) Furthermore, despite the WMO intervention, Sky also continues to have the largest subscriber base of paying sports subscribers (both wholesale and retail). Ofcom has itself found[11] that 60% to 70% of pay TV sport subscribers are on Sky's DSat platform, implying that Sky has around 5 to 6 million retail pay TV sports subscribers. Moreover, Sky has 60% to 80% of retail pay TV revenues whether considering (a) customers that take only BT Sport and/or Sky Sports, or (b) all pay TV customers.[12]

(vi) Sky has further consolidated its overall market position in the pay TV sector with the development of NOW TV, where Sky remains the exclusive retailer of its Sky Sports channels (as well as other Sky and third party channels) with approximately 360,000 incremental subscribers.[13] The Consultation Document does not set out how many Sky Sports day and week passes Sky has sold[14], but it is clear that the incremental revenues from NOW TV sales day and month passes will provide an increased ability to defray the fixed cost associated with pay TV, and sports rights acquisition in particular, further reinforcing Sky's bidding advantages (which are discussed in detail in Section 4 of this response), whilst managing the cannibalisation risk to Sky's primary DSat retail offering.[15]

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[8] Adjusted operating profit taken from Sky annual report in 2010 (page 7) and 2014 (page 10).
[9] Sky results Q2 2014/2015 (page 19).
[10] "*Sky churn at 10-yr low after CRM blitz*", Decision Marketing, 4 February 2015, available at: http://www.decisionmarketing.co.uk/news/sky-churn-10-yr-low-after-crm-blitz. Sky provides details of its churn rate in its annual reports, and the rate has been remarkably consistent across the past five years at between 10.2 and 10.9%. In comparison, Virgin Media's 2014 results (released on 13 February 2015), indicate that Virgin Media had a "*record low customer churn of 14.6%*", almost 50% higher than Sky.
[11] Consultation Document, Figure 3.10, page 27.
[12] Consultation Document, Table 6.2, page 56.
[13] See footnote 4. BT understands that Sky does not count NOW TV day and week sports passes in these subscriber numbers.
[14] However, BT notes that within 3 months of its launch, Sky had already sold 50,000 of these passes (see, "BSkyB annual results: Now TV 'day pass' sales hit 50,000, The Guardian, 26 July 2013, available at: http://www.theguardian.com/media/2013/jul/26/bskyb-annual-results-now-tv).
[15] Indeed, BT notes that despite the introduction of NOW TV, Sky's ARPU even including NOW TV subscribers remains at £564 (versus £570 for the same quarter last year), suggesting minimal cannibalisation effects, see Sky 2014/15 Q2 results for the six months ended 31 December 2014. Press release, available at: https://corporate.sky.com/documents/investors/results/2015/q2-results-press-release.pdf.

(vii) Conversely, it is inaccurate for Ofcom to describe either BT TV or TalkTalk as a "*significant*" presence in the pay TV sector.[16] Neither BT nor TalkTalk has even a tenth of Sky's pay TV subscriber base, or a third of Virgin Media's pay TV subscriber base. Despite a [✂])[17] since 2007, BT has acquired only [✂] (an increase of [✂] subscribers since the WMO was introduced in 2010).

(viii) As shown by the increasing proportion of programme spend on live sports rights, it is clear that Sky's sports channels continue to remain an important driver of pay TV subscriptions, and underpin Sky's strong market position across the value chain.[18] Sky continues to hold the majority of important live sports rights on pay TV[19], and has further consolidated its position since Ofcom's investigation in 2010.[20] As considered further below in Section 3, there is no alternative to Sky Sports: if a subscriber wants access to a range of live sports including the majority of Premier League games, golf, cricket, tennis, rugby (in particular international rugby), and Formula 1, they have to subscribe to Sky Sports. In turn, if a subscriber wants or thinks they may want to subscribe to Sky Sports, they have to subscribe to a pay TV platform operator that provides these channels (in particular, the full Sky Sports proposition).

(ix) In addition, the importance of Sky Sports to pay TV subscription decisions has enabled Sky to maintain a packaging structure whereby Sky TV customers must 'buy through' a pack of basic channels in order to access the Sky Sports channels, which also contributes significantly to Sky's overall pay TV revenues and profitability. In addition to the incremental sum of £16.50 to £24.50 that the vast majority of Sky

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[16] Although it is correct that BT and TalkTalk have both grown their subscriber bases since 2010, in both instances this was from a very low base. As noted at paragraphs 3.7 to 3.8 of the Consultation Document, from January 2010 to September 2014, BT has grown from 451,000 to around 1 million TV subscribers, and TalkTalk TV has grown from 50,000 to over 1.2 million subscribers in November 2014. It is important to note that BT's pay TV offering [✂] as a result of the fact it is unable to offer the full Sky Sports proposition, Sky's movie channels in HD or any of Sky's basic channels as part of its pay TV proposition.

[17] Estimated operational and capital expenditure on: (i) BT TV (from the financial year 2006/07 until 2014/15); and (ii) BT Sport (from 2012/13 to 2014/15).

[18] BT discusses this in greater detail in Section 3 and 4 below.

[19] This is discussed in more detail below.

[20] While not strictly within the scope of this review at this stage, it is important to note that since Ofcom's last review in 2010 Sky has also materially increased its expenditure on content other than sports. For example, Sky's non-sport spending rose to £1.3 billion in 2014, out of total programming spend of £2.6 billion (source: Sky's 2013/14 annual report and BT internal estimates), whereas Sky's non-sport spending in 2010 was approximately £800 million out of a total programming spend of £1.9 billion (source: 2010/11 Annual Reports and BT internal estimates). This means that Sky has further consolidated its position in pay TV extensively, and beyond merely the scope of its position in sports content.

Sports subscribers on the DSat platform are paying, they also pay between £21.50 and £33 in entry level costs for a Sky basic package.[21]

(x) It is notable that as a result of effective wholesale regulation in the broadband sector, distortions in the pay TV sector have now spilled over into adjacent markets. Despite offering a disaggregated proposition, Sky is now the largest provider of "triple-play" (fixed line, broadband, pay TV) bundles.[22] It is also the second largest broadband retailer, with a retail market share of 23%.[23] The rapid growth of Sky's broadband position, to almost a quarter of the retail market (despite vigorous competition in retail broadband), contrasts sharply with BT's limited ability to gain purchase in retail pay TV markets (with a market share of just 6% [✂]).

2.4. This factual context reinforces that, to date, Ofcom has not put in place measures to ensure fair and effective competition in pay TV, and as a result of increased bundling across communications services, the problems in pay TV are spilling out and creating wider distortions. As a result of its supernormal profits in pay TV, and stringent wholesale broadband regulation[24] (in contrast to pay TV), Sky is in a position to heavily discount its fibre broadband product[25], and now offers free broadband extensively.[26] Therefore, as a result of the strength of its market position in pay TV, Sky is in a position to offer deep discounts on its broader communications products.

2.5. Overall, it is clear that, despite the WMO intervention, Sky's market position has, in fact, strengthened since 2010 (both in pay TV and in wider communications markets) demonstrating that the WMO Remedy as constructed did not go far enough to address the

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[21] http://www.sky.com/shop/tv/

[22] BT estimates that Virgin Media has 3.3 million triple-play customers, whereas Sky has 4.04 million, based on their last quarterly results. As a result of the greater scope for differentiation in pay TV products when compared to broadband and telephony products, it is unsurprising that distortions in the pay TV sector will have a material impact on take-up of triple-play bundles.

[23] Sky's market share of retail broadband by number of subscribers estimated by BT as at the end of December 2014 based on the data in Sky's quarterly results.

[24] BT notes in particular the extensive cost-plus regulation of BT's wholesale business, and Ofcom's swiftness in introducing new, unwarranted, ex ante regulation on BT in the form of its proposal to regulate the margin between BT's wholesale and retail superfast broadband prices (Ofcom's Draft Statement on the Fixed Access Market Review: Approach to the VULA margin, 15 January 2015) and contrasts this with the now eight year process to introduce effective regulation in pay TV.

[25] See Annex 3-1: Evidence of Sky promotional offers, page 1. As set out in this advertisement, Sky is offering "*super fast, super Sky Fibre Unlimited* ***free for 6 months*** *… We'll also give you up to £100 of high street vouchers if your provider charges you to leav*e".

[26] See Annex 3-2 *Evidence of Sky promotional offers*, page 1, an article from IS Preview noting that "Sky Broadband Unlimited Goes FREE for 12 months and Tweaks Prices". It is also noted that "*the standard broadband price has been reduced from £10 to £7.50 per month (this price use to only be available if you also took a Sky TV package) [SIC*]". It is also noted that "*those who take the Sky Sports Bundle + Sky Broadband Unlimited can separately get 24 months of free broadband*".

competition problems with Sky's entrenched market position.[27] Fully and effectively addressing the critical issue of limited distribution of the Sky Sports proposition is an essential pre-requisite to ensuring fair and effective competition in the Pay TV sector and in the wider provision of triple-play bundles.

2.6. It is also the case that in four important respects Ofcom has materially overstated developments in the pay TV sector since 2010, specifically with respect to fair and effective competition for sports subscribers:

(i) First, there have been only limited developments with respect to rights ownership since 2010. The most significant of these actually relate to the *strengthening* of Sky's market position, namely the combination of Sky's increased share of FAPL rights (on both an absolute and relative basis), and the movement of live F1 content, US Masters, and the British Open golf championship (all previously shown on FTA) on to Sky Sports. BT's acquisition of live Champions League rights and some rugby rights does not affect the overall relative strength of Sky's position (see paragraphs 2.8 to 2.40).

(ii) Second, Ofcom's focus on the cost of sports rights absent a consideration of the market context in which bidding takes place is misplaced (see paragraphs 2.41 to 2.47).

(iii) Third, there is only limited wider availability of sports content, and the terms of supply of Sky's wholesale sports channels remain problematic (see paragraphs 2.48 to 2.59).

(iv) Finally, Ofcom overstates the importance of new ways for consumers to access content (see paragraphs 2.60 to 2.64).

2.7. BT discusses each of these in turn below.

[27] BT set out in detail its concerns about the structure of the WMO Remedy, and why it would be insufficient to deliver fair and effective competition, in its pay TV appeal, *BT v Ofcom* [2012] CAT 20. As summarised at paragraphs 61 and 62 ('BT's main contentions'), BT considered that the WMO Remedy does not achieve the statutory purpose of section 316, namely to ensure fair and effect competition because (a) it did not include the full Sky Sports proposition (by excluding SS3 and SS4. At the time as SS5, and SSF1 were not available), and (b) Ofcom set the actual price of the WMO Remedy incorrectly at a level which would not ensure fair and effective competition. In particular, Ofcom made a number of errors in determining the price and setting the mechanism by which they are adjusted including, for example, an incorrect allowance for fixed costs, adopting an unrealistic approach to discounts and churn rates and using an inappropriate financial model.

Ofcom mischaracterises developments with respect to live sports rights ownership since 2010

2.8. It is not disputed that Sky continues to hold the majority of live sports; nor is it disputed that BT Sport is a "*light sports offering*".[28] Indeed, as set out in Table 1 of Annex 3-4 Comparison of major sporting rights on pay TV in 2010 and 2014,[29] Sky continues to hold the vast majority of the sports rights it held in 2010. In particular, as predicted by Ofcom in 2010, Sky has retained the majority Premier League rights in both auctions since 2010;[30] and it also continues to have the majority of live rights to almost all top-flight sports.[31] Sky has also acquired additional major sports rights such as Formula 1, the US Masters and the British Open golf championship since 2010,[32] and has continued to consolidate its market position by acquiring further new rights and signing extensive renewal deals for those rights that it already owned.

2.9. It appears to BT that Ofcom's analysis in the Consultation Document (in particular at paragraphs 3.25 to 3.32) does not properly reflect the degree of continuity between Sky's position now and in 2010, and BT's position against the relevant comparator's (ESPN's) position in 2010. Given that the purpose of the WMO Review is to "*take account of any changes in the market since 2010*",[33] the primary focus of the WMO Review should be determining whether there have been changes to the competitive process since 2010 that would warrant a change in the underlying regulation.

2.10. In this regard, BT considers that the appropriate starting point for Ofcom's present analysis of the position of BT Sport is to consider the conclusions reached in respect of ESPN/Setanta, in particular that their offerings were not an effective constraint on the Sky Sports proposition, and to determine the extent to which BT Sport can be considered to be a materially stronger constraint on Sky today. As the evidence set out below shows, Sky's proposition has significantly strengthened since 2010, and BT's proposition is not a materially stronger competitive constraint on Sky, despite changes in rights ownership at the margin. In fact, as a result of Sky's consolidated rights position since 2010, and as the data

[28] Paragraph A8.13 of the Consultation Document

[29] As considered further below at paragraph 2.20, Sky has also recently acquired the British Open from 2017 onwards, thus further strengthening its share of live golf rights; BT Sport has no live golf content.

[30] Pay TV Statement paragraphs 5.390 to 5.394.

[31] In particular, Sky continues to hold live rights to rugby union, rugby league, the football league, most live cricket, golf and tennis (excluding Wimbledon, which is a listed event). In Sky's circular to analysts on 10 February it stated that "*We have more live football than anyone else, as well as ICC & England Test Cricket, F1, Ryder Cup and Major golf, England rugby union, Super League rugby and ATP tennis.".*

[32] This marked the first time in the modern history of F1 that races were not broadcast in full on free-to-air TV in the UK. Similarly, when the British Open Championship is broadcast on Sky from 2017, this will represent the first time it has not been broadcast by the BBC in 60 years. In addition, the US Masters rights had been shown exclusively on BBC for 24 years at the point where Sky acquired them.

[33] Ofcom, April 2014 press release.

on its market position above (and in Section 4) shows, it appears likely that Sky's ability to act independently of competitors has only got stronger.

<u>Changes in Sky's rights position since 2010</u>

Sky's position in relation to Premier League has not lessened since 2010

2.11. With regard to relevant developments in Sky's rights position since 2010, BT notes that Sky has secured seven years with the maximum number of live Premier League matches available, with an increase in both absolute and relative terms in the number of matches it holds since March 2010:

(i) Whereas in 2010 when Ofcom undertook its competition assessment Sky held 92 live matches out of 138 (or 67% of the matches made available), it currently holds the live rights to 116 live matches (more than 75% of the matches made available) and from 2016 Sky has acquired the rights to a further 10 matches, bringing its total to 126 live matches (and 75% of the matches made available).

(ii) Data for the full 2013/14 Premier League season confirms that, despite BT's acquisition of some Premier League rights, including some first picks, BT Sport has not increased the constraint that Sky faces. In fact, viewing data for the full 2013/14 season shows that overall Sky's average audiences for its Premier League matches increased to 1.2 million viewers (as compared with 1.197 million in the previous year.

(iii) Moreover, in the 2013/14 season, 74 (64%) of the Premier League matches broadcast on Sky Sports achieved an audience above 1 million viewers (with 29 achieving an audience of 1.5 to 2.7 million viewers), compared with only three (8%) on BT Sport, each of which achieved only 1.1 million to 1.3 million viewers. Since the start of the 2014/15 Premier League season, 36 out of the first 69 matches broadcast by Sky have achieved an average audience above 1 million viewers, compared with just one on BT Sport.

(iv) Indeed, Sky itself stated in a press release after its results announcement on 31 March 2014 that: "*In Sport, we built on the strong first half* ***as Sky Sports achieved its highest share of viewing for seven years. Average audiences for the Premier***

League are up 7% year on year and 49 of the 50 most watched Premier League matches this season so far have been on Sky Sports" (emphasis added).[34]

2.12. This data clearly demonstrates that BT's acquisition of some "first picks" did not alter Sky's strong market position in relation to live Premier League content. [✂]:[35][✂]. Moreover, as a result of the fact that Sky also has a large number of second picks (33 out of 38) and third picks (35 out of 35)**,** as well as other later picks, [✂]. As a result, this meant that:

(i) Over the 2013/14 full season Sky's first pick matches delivered average audiences of 1.5 million viewers, [✂]. Indeed, the average audiences for Sky's second, third, fourth and fifth pick games [✂], with even the fifth pick games delivering average audiences that were 50% greater for Sky (1.02 million for Sky's fifth pick games [✂]).

(ii) In the 2013/14 Premier League season, when BT Sport launched, [✂].[36] [✂].

(iii) In the 2014/15 Premier League season, Sky's strategy has been to focus even more aggressively on ensuring that it shows the climax of the Premier League season. Indeed, as of 1 February 2015, after 23 rounds of matches, Sky had used just 10 of its first picks,[37] meaning that in the final 15 rounds of the season, Sky will have 10 out of the remaining first picks in the "premium" Sunday afternoon slot, further increasing the number of games that are likely to achieve high audiences for Sky. Thus, it is inevitable that, as with the 2013/14 Premier League season, [✂].[38, 39]

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[34] Sky Q3 2013/14 press release, available at: https://corporate.sky.com/documents/pdf/latest_results/q3_1314_press_release.pdf. BT also notes that this statistic is still quoted on the Sky Sports product page where it states "*This season, more of the games that matter are on Sky Sports. 49 of the 50 most watched Barclays Premier League games were shown on Sky Sports last season, and we believe 2014/15's fixtures will be just as popular.*" (http://www.sky.com/shop/tv/sports/).

[35] [✂]

[36] This development was noted in the national press. See, for example, "Sky Sports freezes BT Sport out of Premier League title race", *The Telegraph*, 27 February 2014, available at: http://www.telegraph.co.uk/sport/football/competitions/premier-league/10665861/Sky-Sports-freezes-BT-Sport-out-of-Premier-League-title-race-climax.html. As noted in this article, in April 2014, 16 of the 17 live games Sky broadcast involved teams that – as of 27 February 2014 – were in the top six of the Premier League. This was a "*record-breaking*" achievement for Sky Sports.

[37] This contrasts with the 2013/14 season, where after the first 18 rounds, Sky had only 12 first picks remaining. This suggests that Sky is focusing its attention on ensuring it has a clean run of first pick matches at the end of the 2014/15 season.

[38] Given that Sky has not used a pro-rata number of its preferential first picks at this point in the Premier League season, it is not possible to make accurate comparisons between either the 2013/14 and 2014/15 Premier League seasons to date, nor a comparison between the 2013/14 season and the 2014/15 season to date. However, in light of the number of first picks that still Sky has reserved, it is clear that its average viewing figures will increase (and BT's will fall).

(iv) Moreover, Sky's relative position in terms of its preferential first picks will increase further from 2016. As Sky itself highlighted, as a result of the latest Premier League auction "*We[Sky] have almost 70% of the 1st pick of matches each week, versus 53% today*".[40] Sky also stated that it will have "*The best match picks, including 26 first picks and 31 second picks, meaning that Sky Sports will offer more of the biggest matches*".[41]

(v) Sky has also highlighted, that BT's first picks have had no impact on the constraint that Sky faces in terms of better games. Sky Sports' Managing Director Barney Francis stated: "*BT has made no difference to our selections, there isn't anything particularly game-changing about what we're seeing today... If you look here there are no games that haven't been on ESPN or Setanta before.*"[42]

(vi) Sky also undertook a comparison of BT versus Sky's games, as compared to ESPN and Setanta, which was available on its website until May 2014.[43] In this comparison, Sky made clear its position that BT's first pick matches had not afforded BT any advantages over Sky, nor over ESPN or Setanta before it. The table showed that:

a) Sky had four matches featuring two clubs that finished in the top four of the Premier League in the previous season, in contrast to BT's zero; BT's position was the same as ESPN and Setanta before it;

b) Sky had 24 matches featuring a top four club from the previous season, while BT could show only 10, which was fewer than ESPN (13) and Setanta (14);

c) Sky had 8 matches featuring two top six clubs playing each other in contrast to BT's 3, fewer than ESPN (4) but marginally more than Setanta (1). Sky also

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[39] "Sky Sports freezes BT Sport out of the Premier League title race for the second season running", *The Telegraph*, 20 February 2015, available at: http://www.telegraph.co.uk/sport/football/11425968/.html. The article notes that "*Sky fully exploited its control of which matches it picks when in order to secure every one of Chelsea and Manchester City's games in April. … It also confirmed it would be able to do the same in May,* ***all but ensuring it would once again transmit the winning moment in the title race*** *… Providing Sky does not pass up the opportunity,* ***that means BT has already shown its final Chelsea match this season, the leaders' 1-0 win over Everton just over a week ago*** *[on 11 February 2015] ... It would also mean it has just one more City game, their March 21 encounter with West Bromwich Albion*" (emphasis added).

[40] Sky circular to analysts, 10 February 2015.

[41] Sky press release, "Sky wins live Premier League rights", 10 February 2015, available at: https://corporate.sky.com/media-centre/news-page/2015/sky-sports-wins-live-premier-league-rights.

[42] "Sky claims rights to top-four clashes as BT holds first picks in reserve", *The Guardian*, 11 July 2013, available at: http://www.theguardian.com/football/2013/jul/11/sky-sports-bt-football-coverage and 'Gary Neville has not only done a top job, he's shake up everything', *The Guardian*, 16 July 2013, available at: http://www.theguardian.com/football/2013/jul/16/barney-francis-sky-sports-bt.

[43] See **Annex 3-3 '**Compare the live fixtures for 2013/14 Barclays Premier League' (no longer available online).

had 26 matches featuring any top six clubs in contrast with BT's 12. Again, BT had fewer such games than ESPN (14) or Setanta (17);

d) it was six weeks into the season before BT was able to show all of the top four teams from the previous season, whereas Sky showed all four of them in the first week. Previously ESPN was able to show all the top four teams from the previous season by week 5; and

e) Sky showed all 20 Premier League teams once by 6 October, and twice by 1 December, in contrast with BT's inability to show all teams even once. Indeed, BT was only able to show 15 teams, which was fewer teams than ESPN (16) or Setanta (17).

2.13. In relation to the 2014/15 Premier League season, Sky announced that it was able to "*offer an unrivalled schedule of live Premier League fixtures from August, providing viewers with more of the games that matter, more of the best experts and more of the best analysis*"[44]. Key features of this announcement included the following matches that would be shown by the end of November 2014, emphasising the strength of the Sky offering at the start of the season, which is the most active time for new and renewing subscribers:

(i) First, "*all of last season's top four [Manchester City, Liverpool, Chelsea and Arsenal] at least six times and every club at least three times*".

(ii) Second, "*seven live Manchester United fixtures – including Louis van Gaal's toughest tests against Manchester City, Arsenal and Chelsea*".[45]

(iii) Third, *"the opening matches of last season's top four teams Manchester City, Liverpool, Chelsea and Arsenal*".[46]

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[44] Premier League fixtures live on Sky Sports: Top four kick off unrivalled season, available at: http://www1.skysports.com/football/news/11661/9381737/premier-league-fixtures-live-on-sky-sports-top-four-kick-off-unrivalled-season

[45] As at 1 February 2015, Sky has shown 10 matches featuring Manchester United. The average viewing audience for all games featuring Manchester United on Sky Sports (in the first 23 rounds of the 2014/2015 season) was 1,571,000, and the average maximum audience was 2,431,000. The Manchester derby on November 2014 had an average audience of 1.8 million and a maximum audience of 2.77 million. In comparison, the average audience for the 5 games featuring Manchester United on BT Sport (in the first 23 rounds of the 2014/2015 seasons) was just 749,000, with an average maximum of 1,198,000 viewers.

[46] Arsenal v Crystal Palace (16 August 2014, 17:30) had an average audience of 1,415,300 and a maximum audience of 2,278,700 (Pack C, pick 2); Liverpool v Southampton (17 August 2014, 13:30) had an average audience of 1,182,600 and a maximum audience of 1,737,100 (Pack B, pick 3); Newcastle United v Manchester City (17 August 2014) had an average audience of 1,147,600 and a maximum audience of 1,945,100, (Pack E pick 4); Burnley v Chelsea (18 August 2014, 20:00) had an average audience of 920,900 and a maximum audience of 1,945,100, (Pack E, pick 5). These matches shows how Sky's control of a vast majority of matches enables Sky to secure attractive matches even using low picks.

(iv) Fourth, "*43 live matches – at least three live fixtures every week – before the end of November*".[47]

(v) In summary, Barney Francis, Managing Director of Sky Sports stated "*a quick look at our opening schedule of fixtures shows **Sky Sports is still the place to go for more of the games that matter***"[48]

2.14. Since 2010, Sky has also maintained a stranglehold over the most important viewing slots for Premier League matches, and retains this with the rights it has acquired from 2016 onwards.

(i) The strongest viewing figures are gained for matches broadcast on Sunday afternoon, with Sky showing two matches on Sundays in most weeks.[49] In fact, Enders Analysis determines that Sky's Sunday afternoon slot accounts for 25% of Sky's Premier League audiences.[50]

(ii) This reinforces the preferential nature of Sky's advantage in being able to exercise its preferential first pick: it gets to choose first, and broadcast the matches it chooses in the strongest broadcast slot.

(iii) Sky is also able to use its Sunday slots [✂]. On the two Sundays so far when BT was able to show a match (5 October 2014 and 28 December 2014), Sky showed two matches one of which featured a top 4 team.

(iv) It is also worth noting that in the 2013/14 season there were ten weekends when BT broadcast no matches and five weeks where BT broadcast no matches at all.[51] This means that, like Setanta and ESPN, BT Sport[✂]. To date, in the 2014/15 Premier League season, there have been six weekends where BT has not broadcast any matches.

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[47] The first 43 matches broadcast by Sky Sports in the 2014/2015 Premier League season delivered an average audience of 1,043,000 and an average maximum audience of 1,698,000. These audiences were delivered using just 6 of Sky's 20 first picks; 13 of its second picks; 13 of its third picks; and 9 of its fourth picks; and 2 of its fifth picks.

[48] Premier League fixtures live on Sky Sports: Top four kick off unrivalled season, available at: http://www1.skysports.com/football/news/11661/9381737/premier-league-fixtures-live-on-sky-sports-top-four-kick-off-unrivalled-season

[49] As at 1 February 2015, the average audience for Sunday afternoon matches this season is 1,146,000. In comparison the average audience for all other matches not shown on Sunday afternoon is just 770,000. The attractiveness of Sunday afternoon versus Saturday lunchtime can also be shown by a comparison of average audience share. BT's first pick matches had an average audience of 677,000 viewers. Comparatively, Sky's first pick matches, predominantly broadcast on Sunday lunchtime, had an average audience of 1.5 million viewers.

[50] "Football auction to end all auctions", Enders Analysis, 11 February 2015, page 4.

[51] BT broadcast no matches in five rounds of the Premier League season: rounds 11, 19, 28, 34, and 38. In a further five rounds (rounds 14, 18, 20, 23, and 26) BT only broadcast matches on Tuesday and Wednesday. Although from 2016, BT will have a match regularly once a week, [✂].

(v) The importance of Sky's slots relative to those of its rivals was underscored recently in a tweet by Graham McWilliam Sky's Group Director of Corporate Affairs, where, in regards to the latest Premier League auction, he stated "*Comparison of price paid ignores huge value gap. SuperSunday and MNF big prizes. Friday night fantastic addition to squad"*

2.15. Based on this evidence, it is indisputable that Sky's position with respect to Premier League content has not weakened since 2010, notwithstanding BT's entry. There is no basis to believe that the most recent Premier League Auction (in which Sky further strengthened its absolute and relative position as described above at paragraph 2.12(iv)) will alter this state of affairs. Indeed, Jeremy Darroch, Sky's Group Chief Executive stated that the most recent Premier League auction *"…confirms that Sky is the unrivalled choice for sports fans*" and Barney Francis, Managing Director of Sky Sports, stated that: "*…Only Sky Sports will have the best match picks and the best slots so our viewers will be able to follow the biggest matches, the key head to heads and every club at least four times. No other broadcaster comes close"*.[52] Finally, Graham McWilliam, tweeted "*Lots of qs [questions] over last few years about challenge to @SkySports Answer now clear @SkySports miles ahead for years to come."*

Sky has strengthened its position with respect to other sports rights

2.16. Ofcom's Consultation Document ignores the fact that since 2010, Sky has sought to emphasise the importance of rights other than football.[53] Sky has, in recent years, publicly positioned its sport brand on a much wider basis than football, by stressing the breadth of its sports offering beyond football. For instance, in a press release in January 2014 entitled 'Sky Sports shows more sport than ever before' Mr Barney Francis stated "*We are offering **more sport, more choice and more reasons to watch Sky Sports than ever before.** Our viewers can enjoy unrivalled sport across six channels, on mobile and digital platforms and while 2013*

[52] Sky press release, "Sky wins live Premier League rights", 10 February 2015, available at: https://corporate.sky.com/media-centre/news-page/2015/sky-sports-wins-live-premier-league-rights.

[53] Equally Sky has sought to reposition the Sky brand generally as broader than merely sports content. As Jeremey Darroch, Sky's Chief Executive, stated in May 2015 "We've also made further strides to increase the range and quality of content across all our platforms. Our new original dramas are working well; we've agreed 17 new sports rights deals since January; struck major new partnerships with HBO and ITV; and we've announced today the renewal of our movie output deal with Paramount giving us exclusive UK pay TV rights to hit titles like Noah and Anchorman 2. These continue to make Sky the number one destination for customers who want the best choice of TV." (http://www.skymedia.co.uk/news/another-strong-quarter-of-growth%E2%80%A6q3-results.aspx). Sky's press release announcing the results for the six months ended 31 December 2013 also states: "As an indication of the growing breath and quality of our on-screen offering, the number of shows on Sky's entertainment channels attracting audiences over 1 million increased by more than 25% in the first half." (https://corporate.sky.com/documents/investors/results/q2-1314-press-release.pdf)

was the best year yet, we're sure 2014 will be even better". Of the most televised sports listed in the press release, football makes up 8,462 hours of coverage whilst golf, cricket, F1, rugby union, tennis, rugby league and boxing combined amount to over 19,000 hours of coverage.[54]

2.17. In addition, Sky's press release accompanying its results for the nine months ended 31 March 2014 stated: "*We have **continued to strengthen the breath and quality of our sports offering**. Away from football, audiences to the start of the Super League season were up almost 30%. We have agreed 17 sports rights deals so far this year including the US Masters, IPL cricket and European rugby".*[55] In announcing the latest Premier League deal Barney Francis, Managing Director of Sky Sports, again underscored the fact that Sky's focus is now considerably broader than just football, stating that *"The best Premier League coverage **is part of an unrivalled range of sport across our seven channels** and digital platforms. This new deal follows **our recent success in the rights market, ensuring Sky Sports will be the first choice for years to come**"* (emphasis added).

2.18. As Ofcom acknowledges,[56] Sky continues to hold the vast majority of golf[57] tennis, rugby, and cricket events with a range of important sports rights, including those that Ofcom determined were of "second-tier" importance (and comparable to the UEFA Champions League rights) in the 2010 Pay TV Statement. In this regard, BT notes that in 2010, Ofcom found that in terms of driving subscription choices, the Champions League rights occupied broadly the same status as at least four other sets of rights, each of which continues to be held either exclusively or almost exclusively by Sky: (a) Test cricket; (b) rugby union; (c) League Cup football; and (d) golf.[58]

2.19. Other than the fact that the rights have changed hands it is unclear why Ofcom has singled out one set of second-tier rights (the Champions League rights) in its current review as now being "key" content, yet has not considered the relevance of Sky maintaining its stranglehold over these other second-tier rights. BT discusses this issue in detail in Section 3 below, and, in particular, demonstrates that the Champions League rights remain

[54] https://corporate.sky.com/media-centre/news-page/2014/sky-sports-shows-more-sport-than-ever-before.
[55] https://corporate.sky.com/documents/investors/results/q3-1314-press-release.pdf.
[56] Consultation Document, paragraph 3.29.
[57] BT notes that Sky's already strong position in relation to golf will become even stronger going forward, given that it has augmented its position with the acquisition of exclusive live rights to the British Open, which was previously only available FTA, as discussed further below.
[58] Specifically, Ofcom's research found that: (i) 11% of subscribers chose to subscribe to Sky's channels for access to live Test Cricket; (ii) 11% of subscribers chose to subscribe for access to rugby union; (iii) 11% of subscribers chose to subscribe for access to League Cup football (at the time, the Carling Cup, now the Capital One Cup); and (iv) 8% of subscribers wanted access to live golf.

comparable to a wide range of other second-tier rights in terms of their importance to subscribers.[59]

2.20. Since 2010, Sky has also acquired new, important sports rights, particularly rights which were previously broadcast exclusively FTA, including F1, the US Masters' golf, and the British Open.

2.21. The position in relation to F1 is particularly significant:

(i) Sky now has exclusive rights to half the F1 grand prix events (with the rights to televise the remainder on a shared basis with the BBC). Sky's exclusive and shared F1 content is strong enough for Sky to broadcast it on a dedicated channel (SSF1) – the attractiveness and brand evidently sufficiently strong for Sky to use it as a major marketing tool to attract and retain its Sky Sports subscribers. Prior to Sky's acquisition of these rights, F1 had not previously been available on pay TV. It has a large existing customer base on FTA, and evidence indicates that it is able to drive viewing figures (consistently securing over 1 million viewers when races are televised on Sky Sports exclusively[60]) and impact willingness to subscribe to a pay TV retail platform.[61]

(ii) In particular, according to BARB data analysed by BT, the average audience for live F1 races shown exclusively on Sky Sports in 2014 was 910,000 (more than twice the average audience for 2013/14 Champions League matches shown on Sky which was 419,000), and for live F1 shared with the BBC the average audience is presently 672,400. Other than live Premier League content, this makes F1 the most important driver of audience on the Sky Sports channels;

(iii) Formula 1 also delivers relatively strong average and maximum audiences when compared with other sporting events on Sky Sports. For example, the 2014 Brazilian

[59] See paragraph 3.81

[60] Six of the 10 grand prix races shown exclusively on Sky Sports F1 in 2014 achieved an audience above 1 million viewers, of the remaining four: (i) three achieved an audience of 755 to 876,000 viewers, and (ii) the Australian Grand Prix was shown at 3:30am, with an average audience of 233,200 and an average audience share of 26.9%.

[61] This is in contrast to other forms of motor sport on TV. As Ofcom's own research shows, F1 is viewed as essential by 18% of sports subscribers, whereas all other competitions are cited as important by just 3% of subscribers. This is also borne out by average audiences. While F1 on Sky Sports attracts an average audience of 243,000 viewers with an average maximum audience of 420,400 viewers (for all live F1 content i.e. F1 races, qualifying sessions and practice sessions), Moto GP on BT Sport attracts an average audience of just 155,000 viewers with a maximum audience of around 200,000 viewers. Indeed, the disparity is even greater when looking at the SSF1 content exclusively available from Sky, which has an average audience of 471,600 viewers and an average maximum audience of 465,400. This disparity is to be expected since F1 stands far ahead in terms of brand recognition and having been televised prominently on FTA for many years also has a large base of interested viewers.

Grand Prix race had a peak audience of 1.84 million viewers, and a total reach of 2.44 million viewers, which is higher than the total reach of over 80 live Premier League matches (or almost 70%) shown on SS1 over the full 2013/14 Premier League season.

(iv) Sky's Formula 1 agreement guarantees it 19 weeks of viewing spread throughout the year. Formula 1's season overlaps with both winter and summer sports, making it especially attractive. To take 2014 as an example, the 19 grand prix were spread evenly through the year from March to November with two grand prix each month aside from August (one event) and September (three events).[62] F1 also provides a vast amount of highly attractive broadcasting content. In addition to the race itself (which is usually broadcast as a 3.5 hour programme, and therefore of greater duration than a typical football match), Sky is able to broadcast the qualifying session (which is usually broadcast as a 2.5 hour programme), and three practice sessions of 1.5 to 2.5 hours in duration. As such, F1 affords Sky a vast amount of highly valuable content, spread across the year. This contrasts with Champions League, where the vast majority of the matches are shown simultaneously, limiting the amount of unique hours of broadcasting content available.

(v) Sky's F1 channel therefore undoubtedly materially enhances the attractiveness of Sky's overall sports proposition and the evidence suggests that, for those subscribers with a strong interest in watching the full range of F1 races, as well as marginal sports consumers, Sky's F1 channel may have comparable importance to Premier League. This was recently confirmed by Graham McWilliam, who tweeted, in response to a question about whether Sky's expenditure on Premier League rights would impact on future investment in F1: "*Absolutely not @SkySportsF1 is huge success and we look forward to covering @lewishamilton title defence in 2015.*"

2.22. The position in relation to the US Masters' golf and the British Open is also significant, since Sky has been in a position to win rights that have had a long association with FTA. In the case of the US Masters the rights had been shown exclusively on BBC for 24 years[63], and in the case of the British Open (a category B listed event) they had been exclusively shown on the

[62] In 2014, the grand prix dates were: (1) 13-15 March (Australian GP), (2) 27-30 March (Malaysian GP), 4-6 April (Bahrain GP), (3) 17-20 April (Chinese GP), (4) 9-11 May (Spanish GP), (5) 22-25 May (Monaco GP), (6) 6-8 June (Canada GP), (7) 20-22 June (Austrian GP), (8) 4-6 July (British GP), (9) 18-20 July (German GP), (10) 25-27 July (Hungarian GP), (11) 22-24 August (Belgian GP), (12) 5-7 September (Italian GP), (13) 5-7 September (Belgian GP), (14) 19-21 September (Singapore GP), (15) 2-5 October (Japan GP), (16) 10-12 October (Russian GP), (17) 1-2 November (US GP), (18) 7-9 November (Brazilian GP), and (19) 21-23 November (Abu Dhabi GP).

[63] *BBC loses exclusive Masters golf rights: Sky Sports ends corporation's 24 years of exclusive rights*, The Guardian, 21 September 2010, available at: http://www.theguardian.com/media/2010/sep/21/bbc-sky-sports-us-masters.

BBC for 60 years.[64] As such, similar to F1, these tournaments come with a very high associated viewer base, and large levels of interest.[65]

2.23. Sky has also continued to consolidate its market position by acquiring further new rights and agreeing extended renewal deals for those rights that it already owned in 2010. As Sky itself highlighted in a circular to analysts on 10 February 2015 it has "*secured 25 rights deals in 2014 alone including Masters & PGA golf, ICC & ECB cricket, Lions & England rugby, plus Open golf last week.*"[66] As Table 2 at Annex 3-4 shows,[67] since 2010, Sky has won or renewed well over 50 rights packages to broadcast more than 60 individual sporting events.[68] As recently as this week, Sky announced that it had won the rights to broadcast exclusively live Major League Soccer (MLS) from the US for the first time under a 4 year deal. The rights are currently held by BT. In its announcement, Sky again indicated its superiority in relation to football:

> "*This season, Sky Sports will show more football than ever before, up to 800 live matches. As well as Barclays Premier League, viewers can enjoy live coverage of European qualifiers for UEFA EURO 2016, UEFA Champions League, SkyBet Football League, SPFL, Capital One Cup, La Liga, Eredivisie, Copa del Rey and Coppa Italia, Johnstones Paint Trophy and Sky Sports Victory Shield*."[69]

2.24. Moreover, many of the deals that Sky has agreed over the period since 2010 have been for extended periods, tying up rights for many years into the future. As Table 3 at Annex-3-4 shows,[70] Sky has contracted a considerable number of important rights beyond the next three years (i.e. the normal review period for ex ante regulation) including ATP World Tour Masters, British and Irish Lions, a number of ICC cricket tournaments, England RFU Internationals (which include the autumn internationals), and SANZAR rights (which include the summer internationals), with many rights tied up to 2020 (eg Cricket New Zealand, Cricket South Africa, Cricket West Indies, NFL), and beyond (eg the PGA Tour rights, which

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[64] *Sky Sports wins rights to show Open Championship golf live from 2017. BBC says goodbye to event after 60 years*, *The Guardian*, 3 February 2015, available at: http://www.theguardian.com/sport/2015/feb/03/sky-sports-buys-open-championship-golf-bbc

[65] BT discusses the reasons why Sky was in a position to acquire these rights, long associated with FTA, in Section 4 below where it explains the extent of Sky's bidding advantages.

[66] Sky circular to analysts, 10 February 2015.

[67] Sky's new sports rights and renewals since 2010, Annex 3-4, Table 2.

[68] BT has not sought to capture every individual right that Sky has acquired or renewed (since this data is not publicly available), but, based on publicly available data and BT's own competitor intelligence, has tried to capture those renewals and acquisition that it is aware of over the period. Since BT did not track these issues closely prior to its decision in mid-2012 to launch BT Sport, its information prior to mid-2012 is less extensive.

[69] "Sky Sports adds even more choice with MLS deal", Sky press release, 25 February 2015, available at: https://corporate.sky.com/media-centre/news-page/2015/sky-sports-adds-even-more-choice-with-mls-deal

[70] Sky rights renewals beyond three years, Annex 3-4, Table 3.

are contracted until 2022, and the rights to ICC major tournaments, contracted until 2023). This table also shows that in several cases the period of the rights contract has been extended substantially from the previous rights period.[71] The problem of Sky signing rights for an extended duration is particularly acute when rights for different sporting events within different sporting genres are staggered, as it prevents BT from gaining a purchase in these sports as the rights to individual events are sequentially renewed.[72]

2.25. Finally, BT notes that analysts' reports reflect strong confidence in the unrivalled position of Sky Sports, showing that BT Sport has had no impact on Sky's market position. For example, a September 2014 paper by Nomura highlights Sky's aggregation of content as key, noting that: ***"****BSkyB **runs the strongest sports service** in the UK. The service broadcasts over 55,000 hours of sport per year"*, and "*Sky Sports has the **broadest portfolio of sports rights in the UK***" (emphasis added)[73]. Indeed, on 23 October 2014, more than a year after BT Sport entered the market, Sky announced a "*good start to the season for Sky Sports"*,[74] noting: "*since the start of the season, **the average combined audience across all our channels is almost ten times our nearest rival. Our viewers watch their sport more often and for longer**"***.**

Changes in BT (ESPN)'s rights position since 2010

2.26. In contrast, for the reasons set out below, BT Sport's position relative to Sky Sports is [✂]. However, the presentation of the sports rights on BT Sport in the Consultation Document risks materially overstating the value of BT's rights holdings. A particularly vivid illustration of this is Figure 3.4, which uses ticks and empty cells to indicate in a binary yes/no fashion whether or not a provider has any rights for a particular sporting event.[75] As shown in Annex 3-5**,** by replacing the ticks in Figure 3.4 with pie-charts showing the extent of these rights held, it is clear that whereas Sky has the exclusive live rights to eleven of the events that Ofcom has listed, [✂]. Sky also has exclusive live rights to half of the F1 races; and non-exclusive live rights to the other half. In addition, Figure 3.4 of the Consultation Document does not reflect the [✂] BT's Premier League rights in comparison to those held by Sky (as discussed in more detail below).

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[71] As discussed in more detail in Section 4, in light of its existing, long term relationships with rights holders, Sky is uniquely placed to recontract these rights (many of which are not openly tendered), and to seek to extend the contract term when it does.

[72] This issue is discussed in more detail in Section 4 below.

[73] Nomura, 11 September 2014, "*BT, Sky and Football Rights*".

[74] Sky blogpost, 23 October 2014, "*A good start to the season for Sky Sports*".

[75] BT also notes that the events in this table appear to be rather haphazardly chosen with no clear basis why Ofcom has listed some events but not others of equivalent importance.

2.27. Therefore, when properly considered in detail, the true – and persistent – extent of the disparity between BT Sport and Sky Sports position is plain. This disparity is not reflected in Ofcom's Consultation Document in part because Ofcom focuses on evidence of change, whereas the prevailing issue in relation to the sale of sports rights has been the very high degree of continuity between Sky's position in 2010 and Sky's position today.

2.28. The Consultation Document also focus extensively on BT's rights "acquisitions"[76], while failing to give due consideration to the fact that in almost all cases, [✂]. This includes, the FA Cup rights, Bundesliga, Caribbean Premier League cricket, NBA basketball, the Women's Tennis Association Tour, UFC World Championship, and some motor sports content (e.g. the World Rally Championship, Formula E, and Moto GP).[77] The only rights that Ofcom cites [✂] are the Champions League rights, and some rugby rights, both of which are discussed in detail below, at paragraphs 2.32 to 2.40.

2.29. A change in rights ownership from ESPN to BT is not in itself a relevant change to the competitive process,[78] particularly given that in both cases the underlying parent company, BT and ESPN, are of comparable scale.[79] The only difference is that, in the UK, ESPN is not a vertically integrated pay TV channel and retail platform operator, and is not present in wider communications markets. However, the fact that BT is vertically integrated cannot, in itself, be expected to lead to a change in the competitive conditions if the [✂]. As the evidence in this section shows, [✂]. Absent the ability (or incentive) to impact on fair and effective competition (as demonstrated in sections 3 to 6 below), the fact that BT is vertically integrated is an irrelevance.

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[76] See Consultation Document, paragraphs 3.25 to 3.32.

[77] BT also notes the disparity in terms of the importance of the rights Ofcom cites for BT versus those for Sky. In the case of Sky, Ofcom recognises that it holds the rights to **all** F1 races, **all** live cricket, **all** golf coverage, rugby union rights and "*a range of other sport including rugby league, darts, and the NFL*", yet for BT Ofcom cites minor, individual rights across sports (e.g. Caribbean Premier League cricket or Women's Tennis Association Tour). It is clear that despite Ofcom's presentation [✂]

[78] BT notes, in this regard that in the Pay TV Statement, Ofcom did not consider it necessary to replicate its analysis of Setanta when rights ownership moved from Setanta to ESPN, despite the fact that ESPN monetised the rights using a different model to Setanta: Ofcom was confident that its analysis would remain correct notwithstanding this change of ownership from a financially struggling broadcaster to a subsidiary of a global multinational company of comparable scale to BT, and with the added advantage of considerable experience in pay TV sports channel production.

[79] ESPN's estimated value as a stand-alone company is approximately $51bn (see, Forget Mickey Mouse: This Once Overlooked Asset Is What Makes Disney Great, Fool, *2 August 2014,* http://www.fool.com/investing/general/2014/08/02/forget-mickey-this-is-the-real-walt-disney.aspx) and, alongside Sky Sports, is perceived to be one of the most valuable sporting brands in the world (Most Valuable Sports Brands 2014 (Nike, ESPN, SKY, TSM Plug, 28 May 2014, http://www.tsmplug.com/richlist/valuable-sports-brands/). BT's market capitalisation is approximately £55bn as at 11 February 2015.

BT's Premier League rights

2.30. As noted above, BT has proportionately fewer live Premier League matches than ESPN in March 2010 with only 38 (or 24%) of live Premier League matches per season currently. Although the absolute number of games that BT will be able to show will increase from 2016 (but only by four games, compared to Sky's additional 10), it will still have proportionately fewer Premier League matches relative to Sky than ESPN at the time of Ofcom's 2010 Pay TV Statement, and previous assessment of Sky's market power.[80]

2.31. As explained above, at paragraphs 2.11 to 2.15, BT's acquisition of a minority of first pick Premier League matches has not altered BT or Sky's position (and as noted above, will further weaken from 2016/17 as a result of the latest Premier League Auction). As Graham McWilliam Sky's Group Director of Corporate Affairs, tweeted "*New deal gives @SkySports even better match selections. 75% of 1st & 2nd picks. Good news for our viewers*". As such [✂], which formed the basis for the 2010 Pay TV Statement.[81]

BT's rugby rights

2.32. BT has made [✂] improvements in terms of its acquisition of rugby rights, as it has now acquired exclusive live rights to Aviva Premiership Rugby (***APR***), whereas these rights were previously shared between ESPN (BT) and Sky. In 2010, ESPN had the majority of these games (43 versus Sky's 27 games), and ESPN also had the rights to the better games since it had first and third picks, with Sky having second picks. BT understands that APR approached Sky to discuss renewal of the existing rights deal but Sky decided not to renegotiate these rights when they came up for renewal.[82] As such, when the rights-holders approached BT, BT agreed an exclusive deal for all of the rights, meaning it now has 27 additional (second pick) games over those held by ESPN in 2010.

2.33. As part of the APR deal, BT and APR agreed a parallel deal for a future European club rugby tournament for English clubs. This was possible due to the fact that English and French clubs involved in the existing Heineken Cup (for which Sky held the exclusive rights) had the option

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[80] BT will have 42 matches (25%) compared with Sky's 126 matches (75%). BT will therefore have less than the one-third (33.3%) of live Premier League matches Setanta/ESPN broadcast in the 2007/08 to 2009/10 Premier League seasons.

[81] In turn, those rights were largely the same as the rights that Setanta held in the 2008-09 football season, which formed the basis for Ofcom's work in the First and Second Pay TV Consultations

[82] Barney Francis, Sky Sports' Managing Director, said "*We had to make some tough choices and one of those was around Premiership Rugby…We have extended our Heineken Cup deal and have the Lions, the autumn internationals, so we are pretty well covered from rugby fans. Premiership Rugby made a decision to go with BT, it wasn't particularly working for us and we were the junior partners*" (Advanced Television "*Sky Sports wasn't working*", 11 October 2012, http://advanced-television.com/2012/10/11/sky-sports-rugby-wasnt-working/.)

to withdraw from that competition after the 2013/14 season. However, on the same day that BT's APR deal was announced (including provisions for a future European club tournament), Sky announced a 3-year extension to its existing Heineken Cup deal covering the same matches i.e. it became apparent that two separate rights bodies had purported to sell the rights to the same underlying rugby games. [✂], BT and Sky agreed to share the rights to the new European Rugby Champions Cup (ERCC) with each broadcasting half of the games.

2.34. Despite BT's [✂] improvements in acquiring APR rights and half of the ERCC rights (which arose as a result of the APR deal), Sky has continued to retain the vast majority of its previous rugby content (including major international rights), and has also improved its position materially with new acquisitions:[83]

(i) Since 2010, Sky has renewed its exclusive Rugby Football Union rights for live England Autumn international team matches (with its latest renewal running until 2020), its British and Irish Lions rights, its RaboDirect Pro 12 rights, and its Super League rights (with its latest renewal deal running until 2021). It is important to note that in terms of attractiveness, and hence ability to drive subscribers, England international games are typically the most important.

(ii) Sky has also newly acquired the exclusive rights to live French, Italian and Ireland Autumn international team matches under a four year deal until 2018. These matches are against the Australian, New Zealand, South African and Argentinian national teams. Moreover, since Sky already had the live England Autumn international matches, this means Sky has a complete, and hence very strong line up in the autumn;

(iii) In 2011, Sky acquired exclusive live rights to the South African, New Zealand and Australian Rugby rights ("SANZAR"), and has since extended its exclusive rights until 2021, spending eight times more in its latest contract. These rights guarantee over 100 top-flight matches of southern hemisphere rugby including the summer internationals featuring England and Wales which attract strong viewing figures as explained below; and

(iv) Sky has acquired the Top 14 (French rugby) rights that were previously held by ESPN/BT, with Sky bidding 5 times the amount that BT had previously spent on these rights. Sky now holds these rights until 2019.

[83] It is also notable in some cases the extent to which Sky increased its payments for a number of these rights in order to secure them for a long period. BT discusses this further in Section 4 below.

2.35. In summary then, in terms of the most high profile rugby matches, which are most likely to have the broadest appeal (and hence are most likely to drive subscriptions), Sky has retained all of the key international (i.e. national teams) rights, and has extended this international coverage. Sky has also expanded its international club rugby coverage since 2010. [✂]:

(i) For example the summer internationals in 2012 and 2014 featuring England had average audiences of 410,900 and 401,600,[84] and the autumn internationals in 2013 and 2014 featuring England had average audiences of 525,100 and 540,140 respectively. Each of the seven matches featuring England had a total reach of over 1 million viewers, with one match (England v South Africa, 15 November 2014) reaching over 1.5 million viewers.[85]

(ii) In comparison to international rugby, other rugby events deliver much lower audiences. For example:

(a) in the 2014/15 season, [✂];[86] and

(b) average audiences for the 2014/15 European Champions Cup on Sky Sports 1-3 and BT Sport 1-2 (which has replaced the Heineken Cup) have averaged 96,000 viewers with an average total reach per match of 251,000 viewers. These figures are weaker than the predecessor Heineken Cup. The final Heineken Cup tournament achieved average audiences on Sky Sports 1-3 of 155,000 viewers with an average total reach per match of 387,400 viewers.

2.36. Therefore, as the data above shows, despite BT's [✂] gains at the margin, Sky's position in rugby remains materially stronger.

BT's Champions League rights

2.37. In August 2015, live Champions League rights will move from Sky Sports and ITV to BT Sport.

2.38. As discussed in detail in Section 3, below, Ofcom's analysis overstates the relative importance of these rights. BT's acquisition of these rights will not lead to a material weakening in Sky's market position when compared with its position in 2010, a position that Sky itself has confirmed. Jeremy Darroch was widely reported to have commented that Champions League programming accounted for less than 3% of viewing on Sky Sports and said there was a limit to how much people would pay for it, and that Sky could satisfy its

[84] The 2014 internationals were played on Saturday morning in the UK, whereas the 2012 internationals were played on Saturday mid-afternoon. The constant audience level notwithstanding the timing of the matches is a strong indication of the dedicated fan base for England rugby internationals.
[85] Source BARB data and analysis undertaken for BT by Digital-i.
[86] BT also notes that in 2013, Sky's average audience for APR was 154,000 viewers i.e. [✂]

subscribers using alternative content such as "Ashes cricket, F1 and top-flight golf".[87] For the reasons set out above, in view of the strengthening of Sky's position in relation to live Premier League rights, and the range of important, additional sports rights it continues to hold and has acquired, Sky has bolstered its position considerably since 2010. As such, [✂] BT elaborates on this point in detail in Section 3 at paragraphs 3.76 to 3.89.

2.39. Moreover, BT observes an inconsistency in Ofcom's analytical approach. Whereas Ofcom appears to assess BT's market position through the dual lens of live Premier League rights and Champions League rights (and as a result BT Sport's position appears to take on greater significance in Ofcom's assessment), Ofcom has not had adequate regard to the impact of the aggregation of Sky's superior Premier League offering with the broad range of other sporting events it holds, highlighted above. Again, BT elaborates on this point in detail in Section 3, at paragraphs 3.15 to 3.18.

2.40. Finally, following the outcome of the 2013 UEFA Auction, Enders Analysis noted that the loss of Champions League would have limited impact on Sky: "*…the main issue is that the vast majority of those keen on football are already with Sky, and these customers are not keen to move (back) to BT. **We cannot see how offering more of the same will make any difference at all to these dynamics***".[88]

Ofcom's focus on the cost of sports rights is misplaced

2.41. In the Consultation Document, Ofcom makes three key observations in relation to the cost of sports rights:

(i) that the cost of sports rights has increased, with which BT is in agreement;[89]

(ii) that a significant proportion of revenue is spent on football, in particular Premier League and Champions League, which is factually correct;[90] and

(iii) less money is spent on other rights, where Ofcom states that "*Rugby Union and Cricket had the second highest broadcaster spend, but each only accounted for 5% of the total expenditure on sports rights for the year*".[91] .

[87] Interview with Jeremy Darroch in The Scotsman, 25 November 2013, available at http://www.scotsman.com/business/management/interview-jeremy-darroch-bskyb-chief-1-3201427: "*Sky shrugged off the decision, claiming BT had overpaid and **noting that the Champions League accounted for just 3% of Sky's total sports coverage. Darroch says he is happy to offer subscribers alternatives such as Ashes cricket, F1 and top-class golf. "We are a broad-based sports service and the Champions League is just a small part of that**.**"*** (emphasis added). See also, *BT limbering up for next big TV football auction says CEO* (Reuters), 5 December 2013, http://uk.reuters.com/article/2013/11/20/uk-britain-tv-sports-idUKBRE9AJ0YY20131120.

[88] Enders Analysis, BT Sport Euro football winner what a price, November 2013, page 4.

[89] Consultation Document, paragraphs 3.33 to 3.37.

[90] Consultation Document, paragraph 3.36 to 3.37.

2.42. BT is concerned that Ofcom presents the amount paid for individual sports rights, without regard to the market context, as evidence of the importance or lack of importance of a particular set of sports rights. While there is no doubt that there is a linkage between the amount that a pay TV retailer is willing to pay for rights and the extent to which those rights might be expected to drive subscriber take-up, Ofcom's analysis does not take into account that there are also other factors driving rights costs not least of which is the existence of an entrenched dominant incumbent with material bidding advantages, that effectively forces up the cost of entry (even assuming Sky's material bidding advantages discussed in detail in Section 4 could be overcome). Therefore, sports rights inflation is evidently driven by competition for rights against an incumbent determined to hold onto as much as they can, not by a new reality in terms of competitive conditions in pay TV.

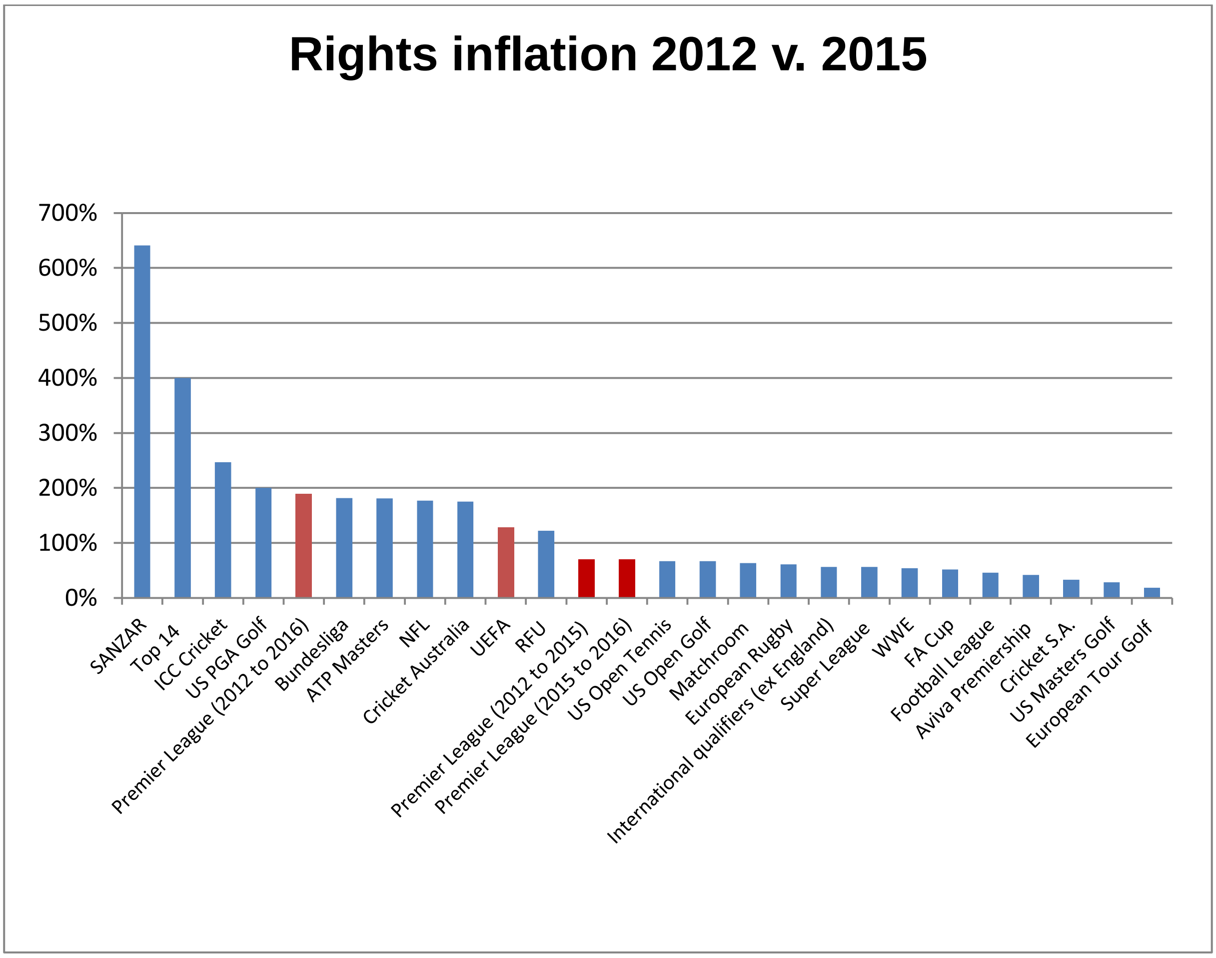
2.43. In addition, while Ofcom focuses on the sums spent on Premier League and UEFA rights, it appears to discount the material sums paid for other rights. The fact that there is a disproportionate amount of money spent on live football rights does not mean that it is not essential to have access to other high quality live sports rights, and, in fact the sums spent on other rights shows that they are also important. For example, BT estimates that Sky's annual expenditure on rugby, cricket and golf is likely to be at least £308 million per annum (at least £115 million on rugby union and league, at least £121 million on cricket and at least £72 million on golf). BT also notes that Sky's expenditure on these sports fluctuates due to events that only occur every two or four years, such as the Ryder Cup (golf), the Ashes (cricket), and the British & Irish Lions (rugby). Thus, in some years, Sky's expenditure on these sports could increase by more than £20 to £30 million.

2.44. BT's primary concern is that Ofcom appears to focus on the fact that the cost of football rights, particularly Premier League and Champions League rights, has increased materially in order to substantiate Ofcom's view that these rights are the most important rights to the exclusion of others. This ignores: (i) the fact that the cost of other rights have also increased, and in some cases by a relatively greater amount; and (ii) the context underpinning recent bidding for Premier League and Champions League rights. Below BT sets out its views on both of these issues. Ofcom's analysis also ignores the fact that in light of Sky's relationship with certain rights holders, some rights do not even go out to tender, as discussed in more detail in Section 4.

[91] Consultation Document, paragraph 3.35.

<u>Ofcom's analysis ignores the fact that the cost of other rights has increased at least as much as football rights since 2010.</u>

2.45. If Ofcom had examined a wider range of sports content, it would have noted that there has been a general trend towards rights inflation, which is not limited merely to football. Indeed, as the chart below shows, the reality is that the increased rights inflation for Premier League and UEFA rights is not out of line with rights inflation across other sports more generally.[92]



2.46. This demonstrates that the importance of other second-tier sports rights which Ofcom considered in its analysis in 2010, has now increased in relative terms, further underlining BT's detailed submissions in Section 3, that Ofcom is incorrect to focus solely on the importance of Premier League and Champions League content.

[92] For reference, BT also sets out in this chart the inflation for Premier League 2012 to 2016 (190%) in addition to 2012 to 2015 and 2015 to 2016 (in each case 70%).

Ofcom's analysis does not take into account the relevant market context

2.47. BT is concerned that Ofcom has considered the amount bid in the 2012 Premier League Auction and the 2013 UEFA Auction without having appropriate regard to the relevant market context in which those bids took place. Below, BT sets out the context within which its bids for these rights must be considered.

(i) In relation to the 2012 Premier League Auction, the amount BT paid reflects the 'penalty' incurred by BT due to Sky's entrenched bidding advantages (discussed in detail in Section 4). [✂]. Due to [✂][93] and its bidding advantages Sky was [✂][94]

(ii) [✂]

Ofcom overstates the increase in the availability of Sky Sports since 2010

2.48. Ofcom's research in its pay TV investigation identified a significant unmet demand for premium sports content. Indeed, driven by the WMO intervention and wider availability of Sky Sports, Ofcom anticipated that it "*expected to see around 1.6 million additional consumers of premium [sport] channels after five years*", and that *"[n]ew platforms will be able to compete effectively, and will be able to develop innovative new services*".[95] In practice, as set out above, this has not come to pass. It is through this lens that developments in relation to the availability of sports content should be assessed. In doing so, it becomes clear that the Consultation Document overstates the increase in the availability of sports content today, and Ofcom's expectations of the impact of the WMO regulation have manifestly not been met.

Availability of Sky Sports

2.49. BT believes that Ofcom's Consultation Document materially overstates the increase in the availability of Sky Sports since 2010, particularly when considered in the context of Ofcom's concerns about limited distribution. Since 2010, there has been only a very limited increase in the availability of the Sky Sports channels to other rival retailers, and as far as BT is aware, what little changes in wholesale supply have occurred has been either: (i) on the basis of

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[93] In particular due to a lack of permitted contingent bidding and limited transparency within the auction process.
[94] Even in the 2015 Premier League Auction, [✂] meant that even securing the minority rights resulted in further rights inflation (of 18% for BT). Sky on the other hand demonstrated the unrivalled bidding advantages it enjoys by being able to tolerate rights inflation of 83%, to £1,392 million per annum.
[95] 2010 Pay TV Statement, paragraph 1.51.

wholesale prices or terms that have not allowed the emergence of fair and effective competition;[96] or (ii) due to enforced supply under the WMO Remedy.[97]

2.50. In terms of wholesale supply of the Sky Sports channels to **BT**:

(i) Sky supplies Sky Sports 1, 2, and 5 in SD to BT's legacy Cardinal platform, [✂].[98][✂][99][✂] (as evidenced in greater detail in Section 3 below).

(ii) Following the amendment to the Interim Relief Order issued by the CAT in November 2014, Sky now supplies Sky Sports 1 and 2 in SD to BT's YouView platform, and BT is currently in the process of requesting HD supply of these channels under that Order. Prior to the CAT ruling updating the Interim Relief Order (which Sky resisted before the Tribunal)[100], Sky had prevented BT from having wholesale access to any Sky Sports channels on BT's YouView platform by seeking to impose the anti-competitive Grant-Back Condition as a pre-requisite for wholesale supply. The Grant-Back Condition is a term that seeks to undermine BT's incentive and ability to compete in channel development and distribution, by appropriating BT's investment,[101] and which the CAT agreed was an inappropriate condition for Sky to seek to impose.[102]

(iii) As was the case with BT's Cardinal platform, [✂].

(iv) As a result of the fact that BT is only able to offer a subset of the full Sky Sports proposition to retail subscribers, BT has [✂] Sky Sports 1 and 2 subscribers.[103] BT elaborates on this issue in detail in Section 3 below.

2.51. In terms of wholesale supply of the Sky Sports channels to **TalkTalk,** Sky's wholesale agreement with TalkTalk is the only new wholesale supply agreement reached outside of

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[96] As far as BT is aware, rate-card pricing and the imposition of a Grant-Back Condition are Sky standard terms for all retailers, and any incentives for retailers with wholesale supply of Sky Sports to extensively market and sell Sky Sports are clearly muted given the apparent limited penetration rates on other platforms.

[97] BT notes that even when required to provide its channels on regulated terms, Sky still imposes terms that impede fair and effective competition [✂]

[98] In this respect it is worth noting that Mike Darcey stated in an email to Marc Watson as early as 2 November 2012 that "*I have said several times that my governing principle is that I am* [✂]" (emphasis added)

[99] As Ofcom found in the 2010 Pay TV Statement, Sky's rate-card prices are set at a level which is too high to ensure fair and effective competition.

[100] 1152/8/3/10 (IR) British Sky Broadcasting Limited v Office of Communications (Interim relief) [2014] CAT 17 (the ***IRO***).

[101] In this regard it fits squarely in Ofcom's definition of limited distribution as set out at paragraph 7.3 of the Consultation Document.

[102] The IRO paragraph 67: *"BT has spent some £1.5 billion acquiring football broadcasting rights in order to improve its position on the market and I do not see that BT should be required, in effect, to deprive itself of the competitive gain from that investment in order to achieve the benefit of the WMO remedy ordered by Ofcom"*.

[103] As at the week ending 13 February 2015.

Sky's regulatory obligations. Although TalkTalk has access to the full set of Sky Sports channels in SD, it does not have access to the channels in HD. In addition, to the extent that TalkTalk's supply is on the basis of rate-card prices, these are too high to allow fair and effective competition. Thus, TalkTalk has wholesale supply of SD channels only and on terms that will not allow it to be an effective competitor. It is notable that TalkTalk's "Sky Sports Boost" is more than 20% more expensive than Sky's headline price for its "Sky Sports Pack" (£30 per month compared to £24.50 per month). As a result, it is unsurprising that the package is not broadly marketed by TalkTalk, nor is it innovatively packaged, which underpins BT's view that the terms of wholesale supply to TalkTalk means it has no incentive to seek premium sports subscribers and compete effectively against Sky. While BT does not have detailed figures on the take up of the Sky Sports channels on TalkTalk's platform, for these reasons, BT believes that it will be low.

2.52. Sky already wholesaled to **Virgin Media** in 2010, and as such availability via Virgin Media does not represent an increase in the availability of Sky Sports since 2010. Moreover, as noted above, there has been no growth in Virgin Media's overall subscriber base since 2010, suggesting that the terms on which it has wholesale supply of the Sky Sports channels has been insufficient to allow Virgin Media to compete more effectively with Sky for pay TV subscribers overall.

2.53. BT notes that other than a short footnote stating that "*Top-Up TV's retail pay TV service closed in October 2013,*"[104] the Consultation Document makes no reference to the fact that **Top-Up TV** has exited the market since 2010. BT understands that Top-Up TV's exit was largely linked to the CAT's 2012 judgment overturning the imposition of the WMO Remedy,[105] and, in particular, that this led to Sky prohibiting the distribution of the Sky Sports channels using Conditional Access Modules (CAMs) and to certain types of set-top boxes offering no additional services other than linear channels,[106] which was an essential component of Top-Up TV's business model.

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[104] Consultation Document, footnote 9.

[105] See footnote 468, on page 173.

[106] A practice which Ofcom had made clear was permitted under the WMO Remedy. In 2010, Sky attempted to exclude CAMs and certain types of set-top boxes offering no additional services other than linear channels from the ambit of the WMO Remedy, requiring additional, onerous security requirements beyond the minimum security requirements established. As a result Top-Up TV brought two disputes to Ofcom under the WMO reference offer dispute process, one addressing CAMs and the other set-top box limitations. In both cases, Ofcom ruled in Top-Up TVs favour, deciding that Sky had breached its WMO licence condition by preventing Top-Up TV from offering SS1 and SS2 for sale via CAMs and certain types of STBs. (http://stakeholders.ofcom.org.uk/binaries/enforcement/competition-bulletins/closed-cases/all-closed-cases/764676/TUTV_2nd_complaint_decision.pdf, and http://stakeholders.ofcom.org.uk/binaries/enforcement/competition-bulletins/closed-cases/all-closed-cases/764676/assessment.pdf)

2.54. Finally, BT notes that **Real Digital** has not yet launched its Sky Sports proposition, and there have been no other entrants in the retail provision of Sky Sports, notwithstanding the existence of the WMO Remedy.

2.55. All of the other market developments in terms of availability of the Sky Sports channels that Ofcom points to are, in fact, Sky self-retailing propositions (through NOW TV, Sky Go, Vodafone). As such, these developments, together with the increased number of subscribers on Sky's DSat platform, represent a strengthening of Sky's already strong market position since 2010 rather than providing evidence that concerns around the limited distribution of Sky Sports have reduced. As a result of these new ways to self-retail its channels, Sky has been able (i) to corner different market segments through effective price discrimination with NOW TV[107] (ii) to widen its addressable market via Vodafone and (iii) to increase its brand/consumer loyalty by offering add on services such as Sky Go. As a result these market developments do not represent increased competitive choice for pay TV consumers; Sky still controls the channels and packages of channels made available to consumers and the customer relationship, and as such is still the party determining retail prices, choice and innovation.[108]

2.56. BT agrees with Ofcom that existing wholesale agreements "*may be of limited value in determining the extent to which Sky would or would not supply its key sports channels in the absence of regulatory intervention*".[109] Regardless of the wholesale terms that Sky has ultimately agreed with TalkTalk or Virgin Media for wholesale supply, these agreements are conducted with the backstop of the WMO Remedy in place. Moreover, as BT's experience with respect to its YouView platform shows, in the absence of the WMO Remedy, it is clear that the distribution of Sky's sports channels would be further limited. BT sets out more detailed views on this issue in Section 6 below where it discusses Sky's incentives to limit the distribution of its channels.

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[107] Sky has publicly stated that it's NOW TV proposition is "*complementary*" to its pay TV business, suggesting, in line with the growth in subscribers on its DSat platform, that NOW TV has not led to its DSat customer base being cannibalised. Sky has also acknowledged that NOW TV is aimed at attracting additional revenues from subscribers who would be unwilling to take a monthly subscription for Sky Sports. Jeremy Darroch has stated "*It will enable us to target Now TV to new segments of the market we don't currently penetrate very highly…. We know there is a pool of customers who really like Sky's content, Freeview customers who like Sky's content but for a variety of reasons don't want an install, or pay through a regular monthly contract, want to pay more on the go. I wouldn't describe it as a YouView killer but it allows us to target that part of the market." (http://www.theguardian.com/media/2013/jul/26/bskyb-now-tv-targets-freeview).*

[108] *In this regard, BT notes Ofcom's previous statements in the Pay TV Statement regarding* self-retail. Ofcom concluded that "*Sky retailing widely on all platforms would not satisfactorily resolve our concerns about restricted distribution … Put most simply, it would not ensure fair and effective competition **between retailers on different platforms**, delivering choice, innovation and competitive prices to consumers, as there would only be one retailer of these important channels across platforms*" (paragraph 7.226).

[109] Consultation Document, paragraph 7.35.

Availability of BT Sport

2.57. As discussed above, the appropriate starting point in the WMO Review for Ofcom's analysis of the position of BT Sport is to consider the conclusions reached in respect of ESPN/Setanta in 2010, in particular that their offerings were not an effective constraint on the Sky Sports proposition, and to determine the extent to which BT Sport can be considered to be a materially stronger constraint on Sky today. From this starting point, it is apparent that there have been no relevant market developments in relation to the availability of BT Sport on pay TV retail platforms, as Setanta/ESPN were available on BT, Sky and Virgin Media's platforms in 2009/2010, and BT Sport is available on all of those platforms today – plus the BT App is available to internet users. Like Setanta, BT has chosen a model where it both wholesales and self-retails its pay TV sport channels.[110] Therefore, BT Sport is available across pay TV platforms on the same basis as Setanta was available in 2009/10.

2.58. Indeed, in light of the business model that BT has adopted, its sports channels are more widely available than either Setanta or ESPN's channels were, and BT continues to explore further opportunities for distribution of its channels on other platforms.

2.59. However, as Ofcom acknowledges, although BT Sport is available in five million homes, [✄] because "*the majority of BT Sport subscribers get the channels [for free] as part of bundle of other services, either as part of the XL package on Virgin Media or bundled with BT's broadband packages. Only [12% (excluding online subscribers)] of BT Sport subscribers pay a stand-alone charge for the channel in the way that Sky's customers do. In comparison, the vast majority of Sky Sports subscribers pay a monthly fee*".[111] [✄].[112]

Ofcom overstates the importance of new ways to access content in addressing competition concerns

2.60. BT considers that Ofcom's analysis in the Consultation Document overstates the importance of the emerging new ways for consumers to access content, specifically in relation to access to Sky Sports.

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[110] As Ofcom is aware, Setanta Sports was self-retailed on the DSat platform in the same way that BT Sport is self-retailed on this platform.

[111] Consultation Document, paragraph 3.45. As noted at footnote 176 (page 56) of the Consultation Document, "*[e]vidence from the October 2014 suggests that not all BT Sport subscribers are interested in sport. 49% of BT Sport subscribers on BT TV gave only non-sport reasons for taking BT Sport. 36% of BT Sport subscribers on BT TV gave only non-sport reasons, and 45% of BT Sport subscribers on Sky DSat and taking BT broadband gave only non-sport reasons*". As explained below at paragraph 4.23, and footnote 257, removing these subscribers from the calculation of market shares for BT Sport results in [✄]

[112] For completeness, BT notes its view that the availability of Eurosport and Premier Sport does not raise issues of relevance to the WMO Review.

2.61. BT agrees with Ofcom that new internet-enabled devices (including gaming consoles such as the Xbox) and new OTT players (such as Amazon Prime Instant Video and Netflix) have created many new and different ways for consumers to access content. This development is not particularly novel, as the emergence of such services was already discussed in the 2010 Pay TV Statement (in assessing potential substitutes to Sky Movies), though these services have now become more prevalent.

2.62. However, as set out above, the only new services that have emerged offering premium sports content that make use of these new routes to market are precisely the services offered by Sky – since Sky controls the underlying premium sports channels that drive consumer take-up of such sports offerings. It is notable that since 2010, Sky has not entered into wholesale deals for the supply of the Sky Sports channels with any of these new service providers, but has instead only agreed to self-retail its channels on their services. NOW TV may be innovative in terms of packaging and pricing/subscription models, but it remains a Sky retailed service across multiple platforms, which therefore does not contribute to increased competition between pay TV retailers. As a result, Sky is in a position to protect itself against potential competition from these new means of content distribution in the same way it has entrenched its position in the more "traditional" pay TV sector. By limiting wholesale distribution of its channels on these new and emerging services, Sky prevents competitors from gaining a purchase in the retailing of premium sports channels, ensuring no cannibalisation of its core retail business.

2.63. Moreover, it is not the case that an OTT operator would be in a position to displace Sky in bidding for premium sports rights any more than a traditional pay TV retailer can. OTT operators face the same structural barriers when bidding for sports rights as traditional pay TV retailers in terms of the "time to build" a large enough base of paying sports subscribers when acquiring perishable rights. As such, consistent with the "vicious circle", Sky will on average and in general be able to outbid them for sports rights. [113]

2.64. Thus, while the proliferation of new types of internet-enabled devices and the emergence of new providers of OTT content may widen the range of options for consumers seeking to access content generally, absent wholesale access to the key premium sports channels on fair, reasonable and non-discriminatory terms, this development does nothing to improve the lack of fair and effective competition associated with the limited distribution of Sky's premium sports channels.

[113] This issue is discussed later in Section 4 in more detail.

3. OFCOM'S NARROW FOCUS ON PREMIER LEAGUE AND CHAMPIONS LEAGUE CONTENT WILL NOT CORRECTLY IDENTIFY UNDERLYING COMPETITION PROBLEMS

3.1. This section of BT's Response explains why:

(i) BT agrees with Ofcom that live sport is important for driving pay TV subscriptions (paragraphs 3.2 to 3.3);

(ii) Ofcom's narrow focus on specific individual sporting events instead of channels and packages of channels comprising such content will not identify the sports channels and packages of sports channels to which wholesale access is necessary to ensure fair and effective competition (paragraphs 3.4 to 3.39);

(iii) Ofcom should identify which sport channels and packages of sports channels are necessary to ensure fair and effective competition. In doing so, Ofcom will find that:

(a) access to the full Sky Sports proposition is required to enable rival pay TV retailers to compete effectively with Sky for those subscribers with an interest in and willingness to purchase premium sports content (paragraphs 3.40 to 3.59);

(b) access to BT Sport is not required by BT's competitors in order to ensure fair and effective competition in pay TV markets (as Ofcom has provisionally concluded) (paragraphs 3.60 to 3.68);

(iv) Ofcom's focus on Premier League rights in the abstract overlooks the importance of the distinction between the majority and minority Premier League rights (paragraphs 3.70 to 3.75); and

(v) Ofcom has overstated the importance of live Champions League rights in absolute and relative terms (paragraphs 3.76 to 3.89).

Live sport is important for driving pay TV subscriptions

3.2. BT agrees with Ofcom's conclusion that live sport continues to be important for driving pay TV subscriptions.[114] The importance of sports to pay TV subscribers is evident from the considerable number of customers (not least the reported 59% of Sky's own pay TV subscribers who subscribe to Sky Sports)[115] who are willing to pay a significant premium in order to access this content in addition to their spending on other pay TV services. As a

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[114] Consultation Document, paragraph 5.14; in line with Ofcom's earlier analysis in the Pay TV Statement, paragraphs 4.110 and 4.111.

[115] "Sky, How High's the Limit?", *Financial Times*, 5 February 2014, available at: http://www.ft.com/cms/s/3/7cc76200-ac85-11e4-9aaa-00144feab7de.html.

result, access to those channels and packages of channels which are necessary to attract premium sports subscribers is essential for a retail pay TV operator to be able to compete in the provision of pay TV services: in a business such as pay TV which is driven by high fixed costs, the wider addressable market and higher ARPU associated with premium sports channel subscribers is critical in terms of building a viable, competitive retail pay TV business.[116]

3.3. BT also agrees with Ofcom that the essential characteristics of live sports rights underpin the ability of sports channels to drive pay TV subscriptions.[117] Simply put, subscribers wish to view sports "live" and delayed or catch-up rights and highlights are not a substitute. Other than specific listed events, and various sports where rights holders value the prominence of FTA (as discussed in more detail in Section 4) the vast majority of live sports coverage is shown exclusively on pay TV channels meaning that the large number of consumers with an appetite for live sports and a willingness to pay must subscribe to such channels. BT also notes that sport continues to lie at the heart of Sky's business, accounting for "*around half … of Sky's total programming costs (across all genres)*" in 2013/14.[118] BT agrees with Ofcom that Sky's willingness to spend "*so much more on sports programming than on other genres of content provides an indication of the aggregate value that Sky anticipates it can recover as a result of offering its sports channels*".[119] Indeed, it is self-evident that a key aspect of this cost recovery lies in the higher ARPU Sky derives from its Sky Sports subscribers when selling its sports channels.[120]

[116] For the reasons previously highlighted in Section 2 of this submission, new developments in the pay TV sector in terms of different ways to access content will not change this assessment.

[117] Consultation Document, paragraph 5.10 and footnote 109. It has been consistently shown that consumers have a strong preference for live sports content over pre-recorded content or highlights. This is evidenced by the price differential in live sports rights over near-live rights or highlights. For example, in 2012, live Premier League rights sold for over £3 billion whereas the highlights coverage was sold for just £180 million. (Source: Screen Digest research for BT). In 2015, the live rights sold for £5.14 billion, and highlights for £204 million (Source: "BBC pays £204m to keep Match of the Day as ITV declines to bid", *The Guardian*, 29 January 2015, available at: http://www.theguardian.com/football/2015/jan/29/bbc-match-of-the-day-premier-league-highlights)

[118] Consultation Document, paragraph 5.12. BT also notes that, according to Enders analysis, the annual amount that Sky recently spent on Premier League rights (£1,392 million) which generates about 16 days of televised
coverage "*is more or less 40% higher than the current total annual programming budget of ITV.*" (See Enders Analysis report "Football auction to end all auctions", 11 February 2015, page 3.

[119] Ibid.

[120] Whilst BT agrees that the *aggregate* amount spent on sports rights may be instructive in understanding the relative importance of live sports, BT cautions against overstating the importance of *individual* content rights from the amount paid for the rights to a specific event. As BT explained in Section 2 above looking at the absolute cost of individual sets of rights, particularly without considering the market context when those rights were bought/sold, will not be instructive.

Ofcom's focus on specific content instead of channels does not reflect the reality of consumers' purchasing decisions and will not identify the sports channels and packages of sports channels that are necessary for fair and effective competition

3.4. In BT's view, the overarching question that Ofcom should be asking in the WMO Review is 'what, products, if any, is it necessary to have access to in order to ensure fair and effective competition in the provision of pay TV services?'

3.5. As shown by the analysis in Section 2, at paragraphs 2.11 to 2.25 (and discussed further in Section 4, at paragraphs 4.3 to 4.48), notwithstanding the WMO Remedy, Sky has strengthened its dominant market position at the wholesale and retail level in pay TV, while Virgin Media has plateaued and BT and TalkTalk have been unable to develop retail pay TV businesses with significant numbers of premium sports subscribers, despite, [✂]. As such, it is clear that Ofcom's regulatory interventions to date have been insufficient to ensure fair and effective competition in retail pay TV markets, to the benefit of consumers. Equally, as elaborated on in detail in Section 4 below (at paragraphs 4.49 to 4.66), Sky's structural advantages when bidding for live sports rights remain, and, as such, the market is incapable of delivering genuine competition itself absent effective regulatory intervention.[121]

3.6. It is critical in this review that, in the absence of commercial wholesale arrangements on terms that ensure fair and effective competition, Ofcom focuses on the regulation that is required to enable Sky's rivals to compete effectively for pay TV subscribers both generally and, in particular, for those subscribers with a proven willingness to pay for premium sports content (given the importance of this content, as described above). Put simply, Ofcom needs to consider which products rivals require access to in order to allow them to compete fairly and effectively for retail pay TV subscribers with a high willingness to pay for live sports content, and what regulation is necessary in the absence of commercial wholesale supply that delivers fair and effective competition.

[121] As BT sets out in more detail in Section 4 below (see in particular, paragraphs 4.58 to 4.66), these structural barriers constitute a vicious circle. As a result of a lack of wholesale access to the Sky Sports proposition (or lack of access on terms that allows for fair and effective competition), other pay TV retailers are prevented from growing their own subscriber base with an established, positive, willingness to pay for premium sports content over time, thereby limiting their ability to challenge for key sports rights in the future. Given Sky's structural advantage in already having a large installed pay TV subscriber base with an established, substantial, willingness to pay for sports (and other premium movies and basics) content, it will be able systematically and on average to outbid any challengers for premium sports rights. Other broadcasters, such as BT, will only be able to acquire major rights against Sky in exceptional circumstances. Sky, therefore, is able to reinforce its position at the wholesale and retail levels, allowing it to maintain and grow its subscriber base, which in turn enables it to continue to bid successfully in upstream content auctions and further entrench its market position across the pay TV value chain.

3.7. With this in mind, it is insufficient for Ofcom merely to identify which individual sporting events consumers may or may not consider to be "important". Ultimately, Ofcom must ask itself whether regulating access to an individual sporting event in isolation would be sufficient to allow Sky's rivals to compete fairly and effectively for retail subscribers. Clearly, in a world where Sky can offer a subscriber an important sporting event in conjunction with the vast breadth and depth of second-tier sporting events that Sky also holds, and a rival can only offer the one "important" event, and a much sparser number of second-tier events, the potential premium sports subscriber is highly unlikely to choose to subscribe to (or to switch to) Sky's rival,[122] notwithstanding the strength of an individual "important" event, particularly in a world where the second-tier content is also available from Sky at no, or very low incremental cost.[123]

3.8. As such, Ofcom's theoretical exercise identifying the importance of individual sporting events in isolation, which is divorced from the reality that live sporting events are sold collectively in premium sports channels and packages of premium sports channels, will not address the core issue as to the scope of the regulation necessary to ensure fair and effective competition in pay TV going forward. Instead, the correct starting point for Ofcom's review of the WMO Remedy should be to focus on the sports *channels* and packages of channels which are available to pay TV subscribers and to consider which of these drive subscribers to subscribe to a particular pay TV service, rather than considering the impact of individual sports rights in isolation.[124]

3.9. This approach is also consistent with the standard orthodoxy of assessing competition issues around focal products. This requires an economic assessment of the competitive conditions that relate to the actual products that are bought and sold, not an artificial sub-segment of that product such as individual sporting events. In order for Ofcom's findings to be robust, and consistent with their regulatory duties, it is important that Ofcom adopts a robust economic framework consistent with general economic practice for assessing competitive constraints. That requires Ofcom to assess the actual sports channels and packages of channels which are available to pay TV subscribers, not individual sporting events that cannot be acquired separately.

3.10. BT elaborates on these issues in detail below.

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[122] Unless the potential subscriber places no value on access to the second-tier content, or the rival retailer is able to discount prices for the "important" event to such an extent as to offset the full value of this second-tier content in aggregate.

[123] There is abundant evidence of this on a more macro scale in terms of the operation of the WMO Remedy to date. As a result of the fact that the current WMO only provides for wholesale access to Sky Sports 1 and Sky Sports 2, [✂].

[124] See Annex 1, paragraphs 3 to 7.

Ofcom's analysis is theoretical and divorced from the reality of the products available in the market

3.11. Ofcom's approach does not reflect the way in which sports content is actually sold, and as such is divorced from the reality of the products that consumers purchase, and the licensed product that Ofcom will ultimately be required to regulate.

3.12. Individual sporting events are made available to pay TV subscribers in a limited number of propositions that have been deliberately structured around a mixture of similar content from the same sport (e.g. Premier League and Football League on SS1) and different content across multiple sports (e.g. Premier League and Super League Rugby on SS1 and the Heineken Cup and the Ashes on SS2).[125] These combinations of individual sporting events on sports channels and packages of sports channels maximise the appeal of the sports proposition to the broadest possible range of subscribers. Bundling different sporting events across a channel or within a package of channels also reflects the fact that individual sporting events do not run continuously for every week throughout the year, and a sports broadcaster needs to aggregate content in order to have an overall proposition that appeals to subscribers over the entirety of their subscription period.[126]

3.13. Since an individual cannot and does not decide to subscribe to an individual sporting event, but rather decides to subscribe to a sports channel or package of sports channels, Ofcom's approach of considering individual sporting events in isolation will not capture subscribers' true purchasing decisions. For the avoidance of doubt (and as discussed in more detail below), BT does not dispute that some sporting events will play more of a role in a subscriber's decision to subscribe to a particular sports channel or package of channels than others. BT's concern is that Ofcom's simplistic approach does not capture subscribers' purchasing decision for the product that is actually being bought and sold, and so will not properly identify all of the factors that have led a consumer to choose one sports channel or package of channels from a given retailer over another. The consequence of this is that any analysis that Ofcom undertakes based only on a partial understanding of consumers'

[125] BT notes that, while in theory, a "mixed genres" channel is possible (i.e. mixing sports with other content), in practice existing and historic holders of live sports rights (Sky, BT, ESPN, Setanta) have all opted to create strong thematic based sports channels (as this is the most likely strategy for profit maximisation). More importantly, this is the basis on which the current sports channels relevant to Ofcom's review are made available.

[126] In this respect it is worth noting that having a broad range of content is likely to be particularly important to Sky's business model, given that many of Sky's subscribers are likely to be out of contract. Sky therefore has a critical need to ensure that Sky Sports shows a range of high quality sport throughout the year, in order to nurture and protect brand loyalty, and avoid subscriber churn as seasons of sports end. By focusing on individual content rights, Ofcom risks overlooking the complementary role played by different sporting events in sustaining demand in pay TV sports channels and packages of channels throughout the year. BT believes that, other than subscribers that have opted into a discounted offer, the majority of Sky's sports subscribers are subject to a rolling 30 day notice period and could downgrade from Sky Sports on a month's notice.

decision making in acquiring the retail products actually bought and sold cannot be expected to identify the causes of consumers' decision making at the retail level and hence cannot be expected to address adequately the identified concerns with fair and effective competition.

3.14. Specifically, Ofcom's focus on content in isolation from the way(s) in which it is commercialised will understate: (i) the importance of Sky's aggregation of sports rights as a way of further strengthening its proposition overall; and (ii) the role providing a broad range of sports content plays in driving subscription revenues and subscriber retention.

<u>Ofcom's own research shows that the aggregation of individual sporting events on sports channels is important in driving consumers' subscription decisions</u>

3.15. The first point that BT notes is that Ofcom's own research[127] demonstrates the importance of channels (and packages of channels) in consumers' subscription decisions. Ofcom's research found that:

(i) the most popular reason for taking a pay TV service is "*to access <u>more channels</u>*" (71% unprompted; 78% prompted) (emphasis added);

(ii) "*access to <u>sport channel</u>*s *(either generally or by reference to specific sports channels) ranked highest as a reason for subscribing to a pay TV service [among*

[127] BT has a number of concerns with Ofcom's research approach, in terms of its survey design and approach, in particular as to the quality of the information put to respondents, and thus the value of the responses received by Ofcom on the issues that it has chosen to address:

(i) BT considers that the information and explanations provided to respondents about the sports propositions of relevant providers was incomplete or inadequate. Equally, in its assessment Ofcom was not clear when it was asking about differences in content availability across channels versus retailers/platforms (either in its questions, or in terms of the responses it sought from respondents). As such, BT doubts whether respondents could reach fully informed views in order to respond to many of the questions.

(ii) This was reinforced by the fact that Ofcom failed to take account of the different sports products (in terms of channels or bundles of channels) available to respondents across different platform operators, nor did it control for the differences in terms of other content available across platforms. (See Figure A6.1. Consultation Document, Annex 6, paragraph A6.10).

(iii) Ofcom did not consistently tie its analysis to specific rights and competitions, with an observable inconsistency in the treatment across sports. This is particularly acute in Questions 10-12 of Ofcom's 2014 research regarding why subscribers chose Sky Sports, where Ofcom does not distinguish between non-football competitions at all: when respondents mentioned football they were prompted to name particular football competitions, whereas when respondents mentioned other sports they were not. Moreover, in the 2014 survey respondents were given a list of different sports to choose from, yet football was broken down into different competitions, and other sports were not. Such an approach would no doubt have artificially increased the prominence of specific football competitions like Champions League. Taken collectively, BT considers these concerns undermine the robustness of the conclusions that Ofcom can draw from its research.

different programme genres] – the percentages were 11% unprompted and 18% including prompted responses" (emphasis added);[128]

3.16. Moreover, Ofcom's own research expressly identified the fact that the vast majority of respondents view more than one sporting event as essential. Specifically:

(i) Ofcom's November 2013 survey found that "*69% of respondents considered two or more individual competitions or sports to be essential.*[129] Since 69% of respondents consider two or more individual competitions or sports to be essential, an analytical framework based solely around one sporting event (regardless of its importance) will fail to capture a proper, comprehensive picture of the key drivers to subscription decisions to sports channels and packages of channels. Equally, ensuring access to only one sporting event, such as Premier League, will not address the underlying competition problem in retail pay TV markets: as this statistic indicates, the vast majority of subscribers would not switch to a rival retailer that was only capable of offering Premier League content, when they also consider access to other sports (F1, cricket, golf, etc) to be essential.

(ii) This is underscored further by the research finding that "*Overall, 77% of respondents considered at least one sport or sporting event* ***other than*** *Premier League coverage to be essential."*[130] Again, this shows that any analysis that is built solely around access to Premier League content will not identify the cause of the underlying competition problem. While 70% of these respondents (or 54% of all respondents) **also** said Premier League coverage was essential, it is clear that Premier League in isolation is not the basis on which subscribers choose their premium sports channels or packages of channels.

(iii) Even more broadly, Ofcom's research found that *"[a]t the level of the sports, 51% considered two or more different sports to be essential*"[131] This shows again, that despite Ofcom's disproportionate focus on football in its Consultation Document, over half of subscribers require access to a broader range of sport than simply football. This also means that even though fewer respondents in Ofcom's survey may have cited "second-tier" sports (such as cricket, rugby, motorsports, golf and

[128] Consultation Document, paragraph 5.7.
[129] Consultation Document, footnote 123.
[130] Consultation Document, footnote 125.
[131] Consultation Document, footnote 123.

tennis) as being essential, ensuring access to this content will nonetheless be essential in delivering fair and effective competition.[132]

(iv) Further reinforcing the fact that Ofcom has overstated the importance of football relative to other sports in its Consultation Document, just "*23% of respondents only identified football competitions as essential*". This means that 44% of respondents identified a football based competition (or competitions) **and** a non-football based competition (or competitions) as essential,[133] and 16% of respondents identified a non-football based competition or competition as essential.[134]

(v) Moreover, Ofcom claims that "*few respondents identify sports other than football or other specific football competitions as their main reason*" for subscribing to Sky Sports and as a result concludes that "*for most of these respondents [non-football content] was not their main reason [for subscribing]*".[135] However, this conclusion is inconsistent with Ofcom's October 2014 research which found that 50% of respondents to the 2014 survey made no mention of football as their main reason for subscribing to Sky Sports.[136] This number increased to 62% for BT Sport.[137]

(vi) Moreover, Ofcom's October 2014 research assessed a hypothetical scenario in which BT Sport showed the same number (or a greater number) of live Premier League games per week as Sky Sports. It found that even if the number of Premier League games on BT Sport doubled, and the number of games on Sky Sports halved, the majority of subscribers who currently have Sky Sports but not BT Sport would

[132] To take a hypothetical example of a subscriber who considers Premier League and test cricket (i.e. generally, rather than a specific event such as The Ashes) to be essential, Sky's strong portfolio of domestic and test cricket rights provides a compelling incentive to ensure that the subscriber chooses the full Sky Sports package of channels rather than a channel that can offer Premier League alone. Similarly, if a rival retailer to Sky can only offer the Sky Sports channel or channels containing Premier League, but not those containing cricket, they cannot hope to attract that subscriber. It is precisely because of these complex trade-offs with respect to individual sporting events that Ofcom needs to consider the impact at a channel level in order to ensure it designs an effective remedy.

[133] According to the results of question C7A of Ofcom's November 2013 survey (as summarised in Figure 5.2 of the Consultation Document), 67% of respondents identify "any football" (summary code) event as essential; excluding the 23% of respondents who only identify football event(s) as essential indicates that 44% of respondents must consider a non-football competition or competitions to be essential, in addition to a football competition or competitions.

[134] According to the results of question C7A of Ofcom's November 2013 survey (as summarised in Figure 5.2 of the Consultation Document), 83% of respondents identify "any sport" (summary code) as essential. Subtracting the 67% of respondents who identify any football event(s) as essential indicates that 16% of respondents must only consider a non-football competition or competitions essential.

[135] Consultation Document, paragraph 5.24

[136] "*Q11 (unprompted) and which is your main reason for getting Sky Sports*?" (table 15, October 2014 research)

[137] "*Q13 (unprompted) and which is your main reason for getting BT Sport*?" (table 17, October 2014 research)

not change their subscription (54%). In fact, only 16% of respondents said they would switch to taking both BT Sport and Sky Sports and only 3% would switch to BT Sport only.[138] Furthermore, even if BT Sport could show the majority of Premier League games, 49% of Sky Sports-only subscribers would continue to remain Sky Sports only subscribers, whilst only 17% would additionally acquire BT Sport and 9% would switch to BT Sport only.[139]

(vii) Therefore, Ofcom's own research data categorically demonstrates that Sky Sports subscribers subscribe to it for more than just Premier League: it reveals that even a complete rebalancing of Premier League content would be insufficient to change the majority of subscribers' decisions to subscribe to Sky Sports. As such, other factors, such as the other sports that subscribers have identified as essential, clearly play a critical role in subscribers' subscription decisions.

3.17. BT recognises that not every sporting event is "essential" (either individually or when aggregated with other sporting events) to a large enough pool of subscribers to warrant regulation; i.e. there may be a "long tail" of sports which have little impact or which are essential to so few subscribers that their absence will not impact on the scale of a rival retailer's addressable market. Equally, however, Ofcom must recognise that there are second-tier rights that are essential, both individually and collectively, to sufficiently large numbers of subscribers[140] that these rights must form part of Ofcom's assessment, in light of the evidence emerging from Ofcom's own research data, as outlined above. It is incumbent upon Ofcom to recognise that a consumers' decision making is more sophisticated than simply being driven by the individual sporting event that is perceived to be "most" important, and the consequence of such an approach is that Ofcom will not identify correctly the necessary scope of regulation. If Ofcom is to address the serious underlying competition problems in pay TV, it needs to consider the impact of these sporting events in aggregate, and hence it must identify the sports channels and packages of channels that are sufficient to change consumer subscription behaviour at the retail level. Ofcom's own

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[138] "Q*24 (prompted) Currently Sky Sports shows about 3 live Premier League games per week, and BT Sport shows about 1 live Premier League game per week. If this changed to a scenario where both Sky Sports and BT Sport each showed 2live Premier League games per week, but everything else stayed the same, what sports channels would you get?* (table 41, 2014 research)

[139] "*Q.26 (prompted) Currently Sky Sports shows about 3 Premier League games per week, and BT Sport shows about 1 Premier League game per week. If this changed to a scenario where Sky Sports showed 1 Premier League game per week and BT Sport showed 3 Premier League games per week, but everything else stayed the same, what sports channels would you get?*" (table 51, 2014 research)

[140] In this regard, it is important to note that large portions of respondents in Ofcom's survey identified other sports as essential, such as cricket (22%), rugby (20%), motorsports (19%), golf (17%) and tennis (16%). Additionally, 29% of subscribers identified "other" sports as essential, in response to question C7A of Ofcom's November 2013 survey (as summarised in Figure 5.2 of the Consultation Document).

research data shows conclusively that access to Premier League alone will not lead to consumer switching.

3.18. This is particularly the case when, as set out above, subscribers are required to subscribe to sporting events aggregated into channels and packages of channels, and where access to additional content on those channels or packages of channels is made available at no extra cost. Under this structure, sporting events that may not be perceived as "essential" may nonetheless play an important role in consumers' decisions, particularly where that content may be available from Sky at no extra cost, but is not available from a rival pay TV retailer at all. Complementarity effects within sports channels and, in particular, across packages of sports channels, are likely to be high (for the reasons set out in more detail below), and will not be captured by looking at individual sporting events in a piecemeal way.

<u>Ofcom's analysis does not examine the importance of overlapping preferences versus unique preferences when attracting subscribers</u>

3.19. Ofcom appears to assume that the stated preferences of respondents to its two surveys provide an adequate basis for determining which content is likely to drive incremental subscription decisions.[141] However, Ofcom's analysis ignores the fact that the wide range of second-tier sports content available on Sky Sports is likely to be critical in driving subscriber take-up, as second-tier content (individually and when aggregated) can attract different subscribers, and may, therefore, be more effective at driving take-up overall.

3.20. As Ofcom's own research shows:

> *"95% of those who said Champions League was essential also said Premier League was essential. 96% of those who said FA Cup was essential also said Premier League was essential. 94% of those who said international football matches were essential also said Premier League was essential."*[142]

3.21. It is a reasonable assumption, then, that there is a high degree of overlap between those subscribers who view various football events as essential. Given this high degree of overlap, in order to maximise the number of subscribers to a sports channel, at a certain point second-tier sports content which attracts <u>different</u> subscribers (either on its own, or due to the fact that a subscriber views the channel proposition with this second-tier content in aggregate) becomes essential. Ofcom's research is unable to capture this effect.

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[141] BT understands that there are certain questions that can only be addressed through consumer surveys, but since Ofcom places considerable weight on these surveys, it is also incumbent on Ofcom to attempt to test the extent to which survey responses correlate to actual behaviour wherever possible, and to undertake as detailed an analysis as possible as to the drivers of subscription decisions.

[142] Consultation Document, footnote 122.

3.22. Instead, BT believes that Ofcom must examine different cohorts of subscribers in order to identify where different sporting events deliver different subscribers unique to that sport. Assessing the relative contribution of different sports (individually and in aggregate) is essential to identify subscription behaviour in practice.

<u>Ofcom's approach to content aggregation is inconsistent even within its Consultation Document</u>

3.23. In Section 2 above BT highlighted a material inconsistency in Ofcom's analytical approach, which relates to the issue of Ofcom's approach to content aggregation. When considering the importance of BT Sport's market position, BT notes that Ofcom undertakes its assessment from the perspective of assessing content aggregation on BT Sport with regards to BT's Premier League and (forthcoming) Champions League content.[143] Specifically, paragraph 5.34 of the Consultation Document states that:

> *"Survey evidence on the stated importance of different sporting events also suggests that live coverage of the Champions League is important to a high proportion of consumers, albeit to a lesser extent than Premier League football. Champions League coverage also contains a relatively high volume of attractive matches, albeit not as many as Premier League coverage.* ***Although our survey evidence suggests that Champions League coverage alone is unlikely to drive pay TV provider choice for a material group of customers, it seems very likely that it could increase the degree to which a sports proposition which included Premier League coverage could influence consumers' choice of pay TV provider.****" [Emphasis added]*

3.24. Ofcom then goes on to set out the evidence that it claims supports this proposition. Yet, this is at odds with Ofcom's approach more generally of considering individual sporting events in isolation. In particular, it is notable that in the next paragraph Ofcom states that:

> *"In relation to other sports and sporting events,* ***these do not appear to be sufficiently important to subscribers such that, on their own, the availability of this content could influence a significant number of consumers' choice of pay TV***

[143] BT notes that there is a particular problem with Ofcom's research data relating to Champions League. Ofcom fails adequately to acknowledge, and control for, the fact that the timing of the surveys are likely to have influenced the responses of the participants as regards Champions League. The surveys were conducted in November 2013 and October 2014 in the midst of the group stage of the Champions League games, where the highest number of Premier League teams participate in the tournament, and games featuring these teams would be at their most frequent. This would inevitably have increased levels of subscriber interest and awareness in the competition at this time. As such the snapshot provided by Ofcom's survey evidence at a particular time cannot be taken to be illustrative of the average importance placed on this tournament as a whole, and, ultimately, its ability to influence subscriber behaviour. Similar effects would be observable had, Ofcom, for example, gauged the level of interest in other sports whilst other high-profile tournaments were in progress, for example cricket would likely rate much more highly during a home Ashes tournament.

provider *and consequently impact upon competition. In addition, given the majority of consumers for whom these other sports are important also consider Premier League content to be important, any influence will be limited by the availability of this content.* ***We recognise that the agglomeration of other sports content has the potential to influence a greater proportion of consumers' choice of pay TV provider. However, for this to affect a significant number of subscribers the content would need to be very highly concentrated and it is not clear that this is currently the case****. For present purposes our focus is on Premier League and Champions League content." [Emphasis added]*

3.25. Thus, Ofcom dismisses the importance of other sports on the basis that, on their own, they are not sufficiently important, but yet determines it should focus on Champions League rights not because it believes they are important in isolation, but rather because it believes they may be important when aggregated with Premier League. Ofcom provides no explanation for why it has singled out Champions League content in this way, particularly when, as the data below shows, its impact on subscription decisions is likely to be minimal.

3.26. Further, Ofcom's rationale for dismissing the issue of "agglomeration" (or aggregation) of other sports content is flawed in several respects:

(i) Firstly, for the reasons set out above, even if not considered important when assessed individually as compared to Premier League, given consumer preferences for more than one sport it is clear that the availability of this content could influence a significant number of consumers' choice of pay TV provider;

(ii) In addition, Ofcom is not correct that "*any influence will be limited by the availability of this [Premier League] content*". Given the analysis above showing large portions of subscribers with preferences for more than one sport, clearly these subscribers require more than Premier League content. Equally, Ofcom's hypothetical assessment set out at paragraph 3.16(vi) above categorically shows that the influence of second-tier rights is not limited to the availability of Premier League content.

(iii) Moreover, even if Ofcom was correct and any influence *was* captured via Premier League, then that would equally be the case for Champions League content, yet Ofcom has chosen to single out Champions League in its assessment in paragraph 5.34; and

(iv) Ofcom merely asserts that for the agglomeration of other sports to have an effect, a significant number of subscribers of the content would need to be very highly concentrated and also asserts that this is not currently the case. However, as the evidence in Section 2 of this Submission shows, second-tier content is highly concentrated within the Sky Sports proposition, and the degree of concentration is now greater than in 2010. Just because some content from an individual sport is available FTA or from BT Sport, does not mean that the vast majority is not concentrated on Sky Sports.[144] Nor does it mean that the limited, partial offering available FTA or from BT Sport will be viewed by premium sports subscribers as a substitute for the Sky Sports proposition.

3.27. As such, Ofcom puts forward no justifiable rationale why it accepts that content aggregation is a relevant factor when considering BT's position with respect to Premier League and Champions League rights in aggregate, but aggregation is not a relevant factor when other sports are assessed. This issue is further underscored by the data in Figure 5.3 of the Consultation Document. When respondents were asked what the main reason for taking Sky Sports was, cricket, F1, rugby union, golf and 'other sports' all scored more highly than Champions League (most more than twice as high). As such, Ofcom's approach is fundamentally inconsistent:

(i) If, contrary to BT's arguments at paragraphs 3.4 to 3.23 above, Ofcom persists with basing its analysis on the stand-alone impact that individual sporting events have on consumer subscription decisions, then there is no basis for its analysis singling out Champions League for consideration due to its effects when aggregated with Premier League in order to assess the strength of BT Sport's market position. This is particularly true in light of the fact that Ofcom's research data shows Champions League to be less important than other sports when it comes to subscribers' main reason for subscribing to Sky Sports; or

(ii) Alternatively, and BT believes correctly, Ofcom must accept the principle that content aggregation is an important part of its assessment, and therefore must now properly examine the impact of content aggregation when assessing Sky's rights position, in the same way that it has done when examining BT's position. This is particularly true in light of the fact that Ofcom's own research data shows that each of the "second-tier" sports on Sky Sports is individually more important than the Champions League in terms of subscribers' main reason for subscribing to Sky Sports.

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[144] BT notes in particular, as highlighted in Section 2, the disparity of Ofcom's assessment of the rights that BT holds, versus the rights that Sky holds. In the case of Sky, Ofcom recognises that it holds the rights to **all** F1 races, **all** live cricket, **all** golf coverage, rugby union rights and "*a range of other sport including rugby league, darts, and the NFL*", yet for BT Ofcom cites minor, individual rights across sports (e.g. Caribbean Premier League cricket or Women's Tennis Association Tour). It is clear that despite Ofcom's presentation [✂]

Ofcom's focus on individual sporting events will not capture other important effects such as cross promotion and branding

3.28. Although BT does not dispute that content is critical to the take-up of sports channels and packages of channels, consumers' perception of this content will also be driven by other important, though more intangible factors such as channel branding, marketing and cross promotion. In particular, the ability to cross promote other sporting events within channels and across packages of channels provides a broadcaster with a strong opportunity to increase the prominence and hence appeal and importance of second-tier content.

3.29. BT notes in this regard that in 2011 Sky invested heavily in and rebranded its Sky Sports News HQ channel (including moving the channel to the top of the sports genre in the Sky EPG in 2014, ahead of Sky Sports 1 HD), which now acts as a 'store front' for the rest of the Sky Sports proposition by cross promoting events across the rest of the Sky Sports proposition. Equally, Sky is able to use prominent events on one Sky Sports channel to raise awareness of less prominent sporting events on other Sky Sports channels. BT also discusses Sky's strong marketing advantages as a result of its strong retail incumbency advantages in detail at paragraph 4.46 below.

3.30. Further, BT notes that programme production and ancillary programming around live sporting events can also be used to increase the prominence of individual sporting events.[145] This issue was identified by Stuart Murphy, the Director of Sky Entertainment Channels, on the BBC Radio 4's The Media Show podcast recently.[146] In it he stated that producing an effective sports proposition is not just about the rights, and that Sky tries to "*creatively revive*" the sports rights that it invests in by spending more on production in order to boost the rights' appeal.

[145] The fact that such matters have an impact can be seen by, for example (i) a comparison of viewing figures for the World Cup final, which is broadcast live simultaneously on both BBC1 and ITV1. In 2014, the Germany v Argentina final was watched by an average 12.09 million viewers on BBC1 compared with an average 2.86 million viewers on ITV1. Clearly, factors other than the underlying sporting event, which was identical on both channels, were at play in driving consumers' behaviour; and (ii) the commercial failure of "*The Premiership*", during the 2001/02 to 2003/04 Premier League seasons, when ITV held the highlights rights, in comparison to the success of Match of the Day on BBC1. Despite both programmes containing the same underlying content in terms of the exclusive rights to Premier League highlights, The Premiership was unable to attract the same levels of audience as Match of the Day (Sources: (a) "ITV Premiership rating plunge, BBC News, 27 August 2001, available at: http://news.bbc.co.uk/1/hi/entertainment/tv_and_radio/1511568.stm, and (b) "ITV relegates The Premiership", Daily Mail, November 2001, available at:, http://www.dailymail.co.uk/tvshowbiz/article-79965/ITV-relegates-The-Premiership.html).

[146] Broadcast on 4 February 2015, http://downloads.bbc.co.uk/podcasts/radio4/media/media_20150204-1704a.mp3

3.31. Ofcom's focus on individual sporting events rather than channels and packages of channels in aggregate will not get a true picture of these important, intangible, factors which will have an effect on subscribers' choice of sports channel.

<u>A focus on channels and packages of channels is consistent with Ofcom's analysis of market positions</u>

3.32. In contrast to the (over)-prominence given to individual sporting events in the Consultation Document generally, BT observes that the data and analysis relied upon by Ofcom in Section 6 of the Consultation Document, in fact, evaluates Sky and BT's market positions by reference to the sports <u>channels</u> (and packages of channels) that each sells. Specifically:

(i) Ofcom notes that its "*analysis … focuses on Sky Sports …* ***rather than the standalone channels on which this content is shown as much of the evidence available to use reflects the way in which the channels are typically made available (i.e. as part of a wider bundle)***". [Emphasis added]

(ii) Ofcom also acknowledges that its "*assessment also takes into account the influence of other content shown on these channels (in addition to the key content we have identified*)".[147]

3.33. BT considers that this approach is appropriate, and in line with the analytical approach that Ofcom should have adopted throughout, as outlined above (and as noted in Annex 1, at paragraphs 3 to 7). However, this does not vitiate the analytical flaws that arise through Ofcom's failure to consider the relevant product actually bought and sold and the issue of content aggregation at the outset of its assessment – in particular, that it is lack of access to channels and packages of channels that drives the impediment to fair and effective competition.

<u>Ofcom has set out no reasons for deviating from its position in 2010, where it assessed content aggregation and the importance of sports channels and packages of channels</u>

3.34. Despite being a review of the WMO Remedy, Ofcom's approach in the Consultation Document is at odds with its analysis in the 2010 Pay TV Statement, where it expressly acknowledged the importance of aggregation of individual sporting events across sports channels and packages of sports channels. Specifically:

(i) Ofcom agreed with BT's analysis that: "*[a] range of other sports are also valued by pay TV subscribers. In particular, rugby union, cricket, motorsports, tennis, boxing*

[147] Consultation Document, paragraph 6.3, footnote 141.

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" [148]

(ii) Ofcom also stated that: "*the importance of offering both highly attractive content as well as a range of moderately attractive content is shown by Sky's conduct. Rather than just acquiring the most attractive sports content, Sky has also acquired a range of rights which it has used to assemble not one but four sports channels.*" [149]

(iii) Ofcom acknowledged the importance of Sky's broader aggregation of rights content, noting "*a risk that the aggregation of content can result in the creation of market power*".[150]

3.35. Indeed, in the 2010 Pay TV Statement, Ofcom considered in depth a range of sports, and combinations of sports, in order to understand their impact on consumer subscription decisions. Ofcom has put forward no evidence in the Consultation Document as to why it now believes that these second-tier rights, and in particular aggregation across these second-tier rights, are not important factors that warrant consideration in determining the nature and scope of the competition problem identified. As the evidence that BT has set out in Section 2 (at paragraphs 2.11 to 2.25) clearly demonstrates, with the acquisition of *inter alia* F1, the US Masters, the British Open, and additional international rugby, the importance of Sky's "second-tier" content in aggregate has vastly increased since 2010. There have been no underlying changes to the market, or competitive conditions within the market which would justify such a fundamental change in approach by Ofcom.

<u>Conclusions on Ofcom's approach in focusing on individual sporting events rather than channels</u>

3.36. In summary, Ofcom has so far failed to test the relevant product that is sold by pay TV retailers and bought by pay TV subscribers (i.e. sports channels and packages of sports channels), and has instead only considered a subset of the content available on a given channel. By failing to consider at the <u>first</u> stage of its analysis the actual products that are bought and sold in the market, Ofcom has divorced its assessment from the market reality.

3.37. Ofcom's own research shows the important role that content aggregation plays in consumers' decisions to subscribe to a particular sports channel or package of channels. Ofcom's approach in considering individual sporting events is inconsistently applied

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[148] Pay TV Statement, paragraph 5.93. Footnotes omitted.
[149] Pay TV Statement, paragraph 5.93, footnote 179.
[150] Pay TV Statement, paragraph 4.81.

throughout the Consultation Document and is at odds with the approach taken by Ofcom in 2010, with no reasons for this material deviation in approach supplied.

3.38. The consequence of Ofcom's analytical exercise identifying the importance of individual sporting events in isolation, is that it will not address the core issue in this review as to the scope of the regulation necessary to ensure fair and effective competition in pay TV markets going forward.

Access to the full Sky Sports proposition is necessary to ensure fair and effective competition

3.39. For the reasons set out above, in order to identify correctly which products are necessary in order to ensure fair and effective competition in pay TV markets, Ofcom must consider the nature of the products that are actually bought by consumers. This means determining those sports channels and packages of channels where access is necessary for a pay TV retailer to be able to compete effectively in the provision of sports channels, and hence retail pay TV more widely. Equally, in order to properly address the enduring structural competition problems in pay TV, Ofcom must also be concerned about ensuring access to those sports channels and packages of channels that are necessary to unwind Sky's bidding advantages (discussed in more detail in Section 4 below), such that over the longer term, genuine competition for live sports rights can emerge. More specifically:

(i) At the retail level, Ofcom must ensure that rivals to Sky are able to develop a sufficiently strong retail proposition in order to be able to attract and retain the material number of retail subscribers with a high willingness to pay for sports content. In a fixed cost business, such as pay TV, the size of the addressable market and ARPU matter. Therefore, rival pay TV retailers are unlikely to be able to compete fairly and effectively without access to the sports channels and packages of channels that are capable of attracting premium sports subscribers.

(ii) Given Sky's entrenched bidding advantages (discussed in detail in Section 4 below), Ofcom must create the conditions for these to be unwound. Since Sky's bidding advantages stem, in particular, from the relative scale of its installed sports subscriber base (which allows it systematically and on average to outbid rivals), ensuring conditions where rivals can attract and retain those subscribers with a high willingness to pay for premium sports content is essential. Again, in light of the limited distribution of Sky Sports, this necessitates Ofcom ensuring access to those sports channels and packages of channels that are capable of attracting premium sports subscribers, providing rival bidders with the opportunity to compete fairly and close the gap on Sky's existing installed base and hence reduce its systematic advantages when bidding for rights.

3.40. Below BT explains that to ensure fair and effective competition, given the nature of Sky's sports proposition and the evidence of consumer preferences, this means that access to all Sky Sports channels (currently comprising SS1, SS2, SS3, SS4, SS5, F1 and SS News HQ in SD and HD) is necessary.[151] Equally, BT demonstrates that access to the BT Sport channels is unnecessary to ensure fair and effective competition.

Access to all of the Sky Sports channels is necessary to ensure fair and effective competition

3.41. It is not disputed that SS1 is Sky's flagship sports channel, given that it is the channel on which most live Premier League content and other attractive "top-flight" live sports are broadcast.[152] In light of the strength of the SS1 channel (particularly when, as argued above, the content on that channel is correctly analysed in aggregate), there can be no dispute that access to SS1 is necessary to ensure fair and effective competition.

3.42. In its 2010 Pay TV Statement, Ofcom went on to analyse the rest of the Sky Sports channels (as existed then)[153] individually, identifying whether each channel could be considered to be a substitute for SS1 in order to determine whether it should be regulated. BT strongly believes that this analysis of each channel individually did not properly assess the necessity of the remaining Sky Sports channels to ensuring fair and effective competition and is, therefore, one of the primary reasons why the WMO Remedy has failed to be effective to date.[154] Similar to the analysis set out above, although at a more macro level, Ofcom needs to consider which sports channels and packages of channels rivals require access to in order to allow them to compete fairly and effectively for retail pay TV subscribers with a high willingness to pay for live sports content. Specifically, Ofcom must ask itself whether ensuring access to a single Sky Sports channel (or two channels as has been the case to date) would be sufficient to enable Sky's rivals to compete fairly and effectively for retail subscribers. In light of the way in which the Sky Sports channels are bundled, marketed, cross-promoted and sold by Sky, plainly access to a subset of these channels has not been and would not be sufficient. BT sets out the evidence to support this below.

[151] BT also believes that the wholesale pricing of those channels is a critical issue, for the reasons it previously highlighted in its pay TV appeal, *BT v Ofcom* [2012] CAT 20.

[152] As Ofcom is aware, Sky is contractually bound to show certain sporting events – most notably its live Premier League content – on SS1. The attractiveness of SS1 is therefore linked to its status as Sky's primary sport channel.

[153] At the time this was SS2, SS3 and SS4 as SS5 and SSF1 had not yet been launched.

[154] The scope of the WMO Remedy was one of BT's primary points on appeal as, from the outset of the WMO Remedy, BT believed that failing to regulate the Sky Sports proposition would mean that fair and effective competition would not be ensured. As the evidence in Section 2 demonstrates, this has clearly been the case, and as the data below shows, the problem is now even more acute than in 2010.

3.43. Although in theory SS1 and SS2 are offered for sale by Sky separately, in practice the bundled pricing for these channels means that very few subscribers take only one of the channels. BT understands that over 90% of Sky's retail subscribers on DSat opt to take both channels.[155] Moreover, once subscribers opt to take SS1 and SS2, they are provided with SS3, SS4, SS5 and F1 for free. All other things being equal, a subscriber with a strong willingness to pay for sports content, who has the option of taking SS1 and SS2 from BT, but receives SS3, SS4, SS5 and F1 in addition for free from Sky is highly unlikely to choose to subscribe to (or to switch to) BT in circumstances where BT only offers SS1 and SS2.[156] This simple fact has been one of the primary reasons why the WMO Remedy has failed to be effective in addressing competition issues to date.

3.44. Sky has effectively developed a single sports proposition built around seven live sports channels,[157] thereby ensuring that it caters to consumers' varied demands for a broad range of live sports across the full sporting calendar.[158] In aggregate, the depth and breadth of Sky's offering across its Sky Sports proposition is now even stronger than in 2010, as supported by the evidence set out in Section 2 of this Submission. Equally, Ofcom cannot dismiss the importance of the content that is available on the SS2, SS3, SS4, SS5, and SSF1 channels since the content on these channels frequently performs better than content available on SS1, which has an average audience of approximately 96,500 for the channel as a whole.[159] For example, across a host of sports, the content available on SS2-SSF1 delivers high viewing audiences and wide reach. For example:

(i) The 2014 **Ryder Cup** was shown on **SS4** (which was temporarily rebadged Sky Sports Ryder Cup). The final day of play had a total reach of 2.84 million viewers (which is higher than the average reach per match for Premier League matches on SS1) and a

[155] Ofcom's research (data table 10) suggests that 91% of all Sky Sports subscribers take Sky Sports 1 and 2. This is a similar to Ofcom's finding in 2010 that 95% of Sky Sports subscribers subscribed to both Sky Sports 1 and 2. (Annex 8 to Ofcom's pay TV market investigation consultation from 18 December 2007, paragraph 3.63 on p.34) http://stakeholders.ofcom.org.uk/binaries/consultations/market_invest_paytv/annexes/a8.pdf. [✂]
[156] Unless the potential subscriber places no value on access to all of this additional content, [✂]
[157] Although it does not broadcast full live sporting events, SS News HQ is still a very important part of the Sky Sports proposition overall. It plays a key role in terms of branding and marketing, as well as cross promotion from the basic tier subscription and across the Sky Sports proposition as a whole. It effectively acts as a "store front" for the channels containing live sporting event, making extensive usage of clips of sporting events appearing on the rest of the Sky Sports proposition, driving consumer interest and prominence.
[158] In this regard, BT notes that Sky's cricket, golf, tennis and rugby coverage are especially important as they provide Sky with top-flight live sports content outside of the football season.
[159] Even if content on SS3-F1 does not always attract the same audience levels as some content on SS1-2, in particular Premier League content, it is also important to recognise that consumers may value the option of viewing SS3-F1 content and/or subscribing to the channels at a point in the future. Ofcom itself acknowledges that consumers place an option value on the possibility of acquiring Sky Sports (Consultation Document, paragraph 6.11).

peak audience of 1.81 million viewers. Across 32 hours of coverage on three days, Ryder Cup achieved an average audience of 632,000.

(ii) The 2014 **William Hill Darts Championship** was primarily shown on **SS3** (which was temporarily rebadged Sky Sports Darts). The 89 hours of content on SS3 achieved an average audience of 343,000, with total reach of over 935,000 viewers. The semi-final had a total reach of 1.64 million viewers with a peak audience of 940,500 viewers. The final had a peak audience of 1.07 million viewers and a total reach of 1.43 million viewers. In 2013, when more than half of the coverage was on Sky Sports, the average audience across 87.5 hours of content was 295,000 viewers, demonstrating that Sky is able to shift content from the regulated to non-regulated Sky Sports channels without suffering a drop in audiences.

(iii) The 21 **European Qualifiers** shown on **SS5** since August 2014 have achieved an average audience of 157,000 and an average peak audience of 285,200, only slightly lower than the four European Qualifiers on SS1 which have achieved an average audience of 172,000, and an average peak audience of 285,500.

(iv) **F1** races shown exclusively on **SSF1** attracted an average audience of 910,400 in 2014, and an average peak audience of 1.39 million viewers. The most watched exclusive event of the season, the Monaco F1 Grand Prix on 25 May 2014, had an average audience 1.17 million viewers and a peak audience of 1.60 million viewers as well as a total reach of 2.1 million viewers.

(v) The **US Open Golf**, shown exclusively on **SS4**, achieved an average audience of 112,000 throughout 2014, with an average total reach per programme of 801,000.

(vi) The 2014 **Super League** games shown on **SS3** achieved an average audience of 113,000 and an average total reach per match of 244,000.

(vii) In 2014 the **Heineken Cup**, now the ERCC, achieved an average audience of 93,000 and an average total reach of 321,000 on **SS3**.

(viii) In the 2014/2015 season of the **Scottish Premier Football League** to date Sky Sports has shown 18 games and achieved an average audience of 133,000 [✂]. **SS4** achieved an average audience of 159,000, [✂]. Further, games shown on **SS3** and **SS4** achieved a greater average total reach (271,000 and 316,000 respectively) than [✂].

3.45. More importantly, since 2010 Sky's strategic approach in branding, marketing and cross promoting its channels has focussed on promoting the essential existence of a single "Sky Sports" proposition, rather than actively distinguishing between the seven individual sports channels and the content that each channel provides. As a result, consumers are less likely to be able to determine what content is available on each channel, and hence it is highly unlikely that they will determine their subscription decisions based on individual sports channels. Instead, it is much more likely that they will want access to the Sky Sports proposition as a whole. This merging of the distinct channels in Sky's marketing has become increasingly prevalent over time, such that it is now entirely artificial for Ofcom to distinguish between SS1-2 and SS3-F1.[160] For example:

(i) It is very difficult to locate the option to subscribe to SS1 or SS2 on a stand-alone basis on Sky's website, as the website is focused on selling the full Sky Sports proposition ("the Sky Sports pack") as the default Sky Sports product. Throughout Sky's Sky Sports product page, it emphasises the "*complete line-up of seven Sky Sports channels*", and additional features such as HD and sports on the go with Sky Go.[161] The product page does not, in general, provide individual information for each channel (except in relation to SSF1, which BT understands Sky is contractually obliged to do). This contrasts markedly with the equivalent page for Sky Movies, where each channel has a distinct identity and information for each is presented separately.[162]

(ii) Sky generally advertises its sporting events as being available on 'Sky Sports' rather than specific Sky Sports channels, unless contractually required to specify a particular channel (as with SSF1) or directly incentivised to do so.[163] This marketing underlines the importance of the full Sky Sports proposition by reference to all seven channels collectively and the Sky Sports brand.[164] Moreover, even where a sporting event may generally be associated with a particular channel (e.g. Premier League on SS1), Sky's marketing materials frequently show it alongside the generic 'Sky Sports' brand name, rather than with reference to the specific channel on which the sporting event can be found.[165] In this way, Sky's imagery is directed towards advertising the Sky Sports proposition as a whole, rather than the individual channels, and this has serious implications in terms of uncertainty for subscribers (or

[160] BT observes that SS News HQ also plays an important role in Sky's marketing and promotion of its sports proposition, and is positioned as an important part of the Sky Sports proposition as a whole.
[161] See Annex 4-1 (screenshot from http://www.sky.com/products/sky-tv/sports/)
[162] See Annex 4-2 (screenshots from http://www.sky.com/products/sky-tv/movies/)
[163] For example, SS5 was introduced for the beginning of the 2014/15 football season. In BT's view, the creation and channel-specific marketing of this new 'European Football' channel was: (i) a direct response to BT's acquisition of Champions League rights, and was intended to maximise Sky's value in this content by linking the channel's launch to two year broadband contracts, with a view to locking in subscribers who were out of contract [✂]; and (ii) to assist Sky in migrating sports content away from its regulated channels onto unregulated channels that it was not required to wholesale to rivals.
[164] See advertisements at Annex 4-3.
[165] See Annex 4-4 which provides a wide range of Sky promotional material, across multiple sports all referencing "Sky Sports".

potential subscribers) without access to the full proposition (as discussed in detail at paragraph 3.49).

(iii) Sky's own promotions also prominently feature sporting events from across all of the Sky Sports channels collectively, and with considerable emphasis on sporting events from SS3, SS4, SS5 and SSF1. For instance Sky's 'Ultimate Weekend' advertising for the weekend 22 to 25 May 2014 advertised a wide range of content from across the full Sky Sports proposition and, in particular, included multiple events that were not available on the current regulated channels, such as The Monaco Grand Prix on SSF1, The PGA Championship Golf on SS4, Rugby League on SS3 and The Heineken Cup Final on SS3.[166] More recently Sky ran two more advertising campaigns on their website under the banner "*Another Big Weekend*", for 7 to 9 November 2014 and 21 to 23 November 2014.[167] Again, Sky highlighted the range of content available across the Sky Sports proposition, including events not available on the current regulated channels, such as Formula 1 (available on SSF1) and ATP World Tour Finals (on SS3).

(iv) This kind of advertising is in no way unique, and the importance of having all of the Sky Sports channels has been a recurring feature of Sky's marketing. For instance, a promotional video for the Sky Sports channels on Sky's website from May 2014 stressed the importance of having the full Sky Sports proposition, as the annexed screenshots show.[168]

(v) Sky's own on-screen cross promotions, even when promoting a particular event on a particular channel, still underscore the more general "Sky Sports" message, and Sky Sports subscribers are subject to a steady stream of within programme and cross-promotion time promotions. BT attaches cross-promotional data from a period of less than two hours (6.16pm to 7.51pm on 25 February 2015 i.e. a Wednesday evening), demonstrating that Sky's cross-promotional material extensively promotes the Sky Sports proposition. In this respect, SS News HQ plays a crucial role indicating to subscribers what is available on other channels (and what subscribers are missing out on if they do not have the full Sky Sports proposition).[169]

(vi) Sky also reinforces the nature of the full Sky Sports proposition in its external communications. An analysis of 74 Sky Sports press releases between 31 January

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[166] See web page print-out at Annex 4-5
[167] See web page print-out at Annex 4-6
[168] See screenshots at Annex 4-7. At the time this was six channels (SS1-SSF1, and SS News HQ), as SS5 had not yet been launched.
[169] See screenshots at Annex 4-8.

2012 and 31 January 2015 found that fewer than half (32) referred specifically to any of SS1-SSF1. Of the remainder, 35 press releases only refer to "Sky Sports" in general terms,[170] rather than making reference to the individual channels, with a further 6 referring only to SS News HQ.[171]

(vii) Moreover, Sky has proven very protective of its 'full Sky Sports package' as representing the Sky Sports proposition. [✂][172][✂]

3.46. In addition, Sky's increased use of themed channels also serves to increase the prominence, and hence subscribers' perceptions of the primacy of the core Sky Sports brand (that being the common theme amongst all rebranded channels: eg Sky Sports World Cup, Sky Sports Ryder Cup, Sky Sports Ashes, Sky Sports Darts, etc). In addition it further highlights the importance of second-tier content that is available from time to time across the Sky Sports channel portfolio (and conversely to underscore what subscribers are missing in the event they do not have access to the full Sky Sports proposition, either from Sky or from a rival pay TV retailer). It allows Sky to reinforce the common core theme that subscribers need to subscribe to Sky Sports as a whole in order to have access to these time-limited, but high profile events. Sky's substantial marketing advantages (discussed in detail at 4.46 below), and cross-promotion advantages means it is well placed to raise the profile of second-tier events, assist subscribers in content discovery and therefore persuade more subscribers to see the value across the full Sky Sports proposition. As an example, the re-badging of SS4 as 'Sky Sports Ryder Cup' for two weeks in September-October 2014 materially increased the prominence of that event and that channel.[173]

3.47. As a result of the fact that Sky's branding and marketing focuses so extensively on the full Sky Sports proposition, rivals who are unable to offer the full proposition are placed at a material disadvantage, without Sky even having to draw express parallels between the sports content that is available from Sky and the more limited sports content that is available from other retailers. That said, Sky has also undertaken marketing campaigns precisely to underline the inadequacy of other retailers' offerings where they only have

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[170] See examples at Annex 4-9.

[171] One press release referred only to Eurosport, and made no reference to Sky Sports. Press releases can be found at: https://corporate.sky.com/media-centre/news-page

[172] [✂]

[173] The average audience for the 2014 Ryder Cup – shown on SS4 – was 632,400 viewers, which is more than 5% higher than the audience for the 2012 Ryder Cup, which was shown on SS1. (http://www1.skysports.com/ryder-cup/news/26732/9387614/sky-sports-ryder-cup-only-place-to-see-exclusive-live-coverage-of-golfs-biggest-event) Similarly, SS3 became 'Sky Sports Darts' to broadcast the William Hill World Darts Championship from 18 December 2014 to 4 January 4 2015, and SS2 became Sky Sports World Cup for the 2015 ICC Cricket World Cup from 14 February 2015 to 29 March 2015.

access to SS1 and 2. In particular, in summer 2010 Sky produced a series of advertisements depicting a “half pizza” or “half football”, captioned with (for example):[174]

(i) *“You’ll only get all of Sky Sports with Sky, including all 5 channels in high definition”;*

(ii) *“The full HD serving. Only with Sky. Unlike with BT Vision or Virgin Media, you’ll only get all 5 Sky Sports channels in high definition with Sky”*; and

(iii) *“As BT don’t have any Sky Sports HD channels. Sky’s the only place to watch a whole season of high definition football, including the Barclays Premier League, Uefa Champions League and npower Football league – plus the FA Cup and Serie A with ESPN”*[175]

3.48. This strategy taps into consumers’ fear of missing out on particular sporting events if they only have access to a subset of the channels that make up the Sky Sports proposition from one of Sky’s rivals. Sky’s deliberate use of this marketing strategy is supported by:

(i) Its sales tactics in Sky call centres and on ‘web chats’ on Sky’s website.[176] [✂][177] [✂].

(ii) Sky’s scheduling of sporting events. Sky can use the scheduling of major sporting events as a tool to create uncertainty, and limit rivals’ ability to attract subscribers if they only have a subset of the Sky Sports proposition. For example, as can be seen from Sky’s website, with respect to Rugby League matches, Sky provides limited information as to what content will be available on each channel on a forward looking basis.[178] From May 2015 onwards, it merely refers to the games as being available on “Sky Sports”, underscoring to subscribers that they may miss out on matches without access to the full Sky Sports proposition. BT has no information

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[174] See press clippings at Annex 4-10.

[175] The extent of Sky’s marketing highlighting this issue was also notable. As set out in more detail in Section 4, Sky’s UK marketing expenditure specifically in relation to Sky Sports increased dramatically in July to August 2010 compared with the same period in 2009. Sky's July marketing spend in relation to Sky Sports increased by 374% and its August spend by 90%. Sky itself confirmed that for the quarter ending 30 September 2010 it spent £58 million more on marketing the Sky brands in the UK as a whole, compared to the same quarter in 2009.

[176] In July 2010, shortly after BT was granted regulated wholesale supply of SS1 and SS2, BT engaged a research agency to conduct a mystery shopping exercise by calling Sky’s call centres or undertaking ‘web chats’ on Sky’s website 10 times every week for 5 weeks. In each case the research agency stated that it intended to leave Sky for a rival, and asked for clarity as to what content would be available from rivals on SS1 and SS2 (second witness statement of Marc Watson, 7 September 2010, paragraphs 41-46).

[177] [✂]

[178] http://m.skysports.com/liveonsky/rugbyleague.

other than that which is provided publicly as to what content will be scheduled on which Sky Sports channels, and [✂].[179] [✂].

3.49. BT endeavoured to measure the impact that such uncertainty will have on subscribers' subscription decisions in 2010 as part of the Pay TV Proceedings.[180] BT engaged a market research agency to survey a representative sample of 1000 Sky customers (on Sky's DSat platform) who subscribed to a Sky package including at least one Sky Sports channel. [✂].[181] [✂]:

(i) [✂]

(ii) [✂].

3.50. The marketing of Sky Sports as a single unified proposition, where access to all of the channels is required by the consumer has been further accentuated by Sky's strategy of shifting content from the regulated SS1-2 channels to the non-regulated SS3-F1 channels. In addition to devaluing the regulated proposition available from rivals, by moving individual sporting events across channels, the uncertainty effects outlined above are exacerbated.

3.51. Notwithstanding the WMO Remedy, Sky has shifted content on a very large scale from the regulated channels onto its unregulated sports channels. Most notably, Sky's launch of SS5 on 12 August 2014 was largely created from sporting events previously broadcast on the regulated sports channels. On a conservative basis, BT estimates that in the twelve-month period from 12 August 2014, Sky will broadcast at least 162 live football matches (over 360 hours of content) on SS5 that, but for the launch of SS5, would have been broadcast on SS1 and SS2. In fact, BT estimates that 37% of the content that goes to make up the SS5 channel was previously on SS1 and 29% on SS2.[182] The launch of SS5 shows Sky's ability to create a stronger proposition to emphasise its range of second-tier content as a marketing tool.

3.52. Sky has also shifted content from its regulated channels for short periods, with focused re-branding. As described above, the re-badging of SS4 as 'Sky Sports Ryder Cup' led to the relevant content moving from SS1 (where the Ryder Cup was shown in 2012) to SS4. There are also further instances of a general shift in content away from the regulated channels to

[179] BT contrasts this with the situation with respect to Sky Movies, [✂].

[180] Second witness statement of Marc Watson dated 7 September 2010, paragraphs 37 to 38.

[181] This exercise is discussed in more detail at paragraph 3.55 below. It is important to note that at the time the exercise was undertaken there were only four Sky Sports channels SS1 and SS2 (regulated) and SS3 and SS4 (unregulated).

[182] It is important to note that these estimates are based on live match data recorded by BARB. As such they do not take account of the substantial additional content shown behind the red button for these football tournaments and thus under-estimates the total amount of content that will move in practice. The content shown behind the red button is likely to be substantial in the case of the Champions League where up to 8 matches are shown live simultaneously in the initial group stages.

Sky's unregulated channels, as exemplified by the scheduling of the following tennis and golf tournaments:[183]

(i) from 2007 to 2013, US Open tennis was shown across SS1-4 (for instance in 2013 85:40 hours were shown on SS1, 50:07 hours on SS3 and 9:06 hours on SS4). However, in 2014 all 160:47 hours of Sky Sports coverage was shown on SS3;

(ii) from 2007 to 2013, Sky's coverage of ATP Tour tennis was shown relatively evenly across SS1-4. In 2013 255:30 hours of content was shown on SS1 and 2, with 480:03 hours of content on SS3 and 4. In 2014, only 1:55 hours were shown on SS1 or 2, with 830:12 hours shown on SS3 and 4;

(iii) the 4-day US Open golf tournament was shown entirely on SS1 and SS2 in 2007 and 2010-2012, with no more than 5 hours of coverage on SS3 or SS4 in any other year between 2007 and 2014. However, in 2014, all 35:48 hours of US Open coverage on Sky Sports was shown on SS4;

(iv) from 2007-2013, European Tour golf was shown across SS1-4, with 359:43 hours of coverage on SS1 and SS2 and 223:29 hours of coverage on SS3 and 4 in 2013. In 2014, all 626:38 hours of Sky Sports coverage was shown on SS4;

(v) from 2007-2013, US PGA Tour golf was shown across SS1-4, with 113:54 hours of content on SS1 and SS2 and 383:35 hours of content on SS3 and SS4 in 2013. However, in 2014 all 548:14 hours of Sky Sports coverage was shown on SS4;

(vi) from 2010 to 2013, all Players Championship golf coverage was shown on SS1 or SS2. In 2014, all 26:33 hours of Sky Sports coverage of the 4-day tournament was shown on SS4; and

(vii) in 2012 and 2013, Sky Sports coverage of the World Golf Championships was spread across SS1-4, with 38:32 hours of coverage on SS1 and 2 and 51:15 hours of coverage on SS3 and 4 in 2013. In 2014, all 103:27 hours of Sky Sports coverage was shown on SS4.[184]

3.53. The consequential impact of Sky's increased branding, marketing and cross-promotion of a single Sky Sports proposition, combined with the uncertainty effects around the threat and

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[183] BT recognised that there can be good editorial reasons for more systematic, dedicated scheduling of a particular event on a particular channel, eg to aid content discovery for subscribers, and to improve the overall presentation of a particular event. On the basis that such editorial/scheduling decisions are undertaken to improve the overall attractiveness of the Sky Sports proposition, this further demonstrates the importance of having access to the full Sky Sports proposition.

[184] Source: Digital-i BARB data

reality of content shifting off the regulated channels is that the importance of the full Sky Sports proposition has vastly increased, and it is impossible for a rival pay TV retailer to compete effectively without the full Sky Sports proposition.

3.54. In the course of previous investigations since 2010, BT has produced ample evidence on the complementarity effects arising from the full range of Sky's sports channels. As part of the Pay TV Proceedings, BT provided evidence on how important the non-regulated Sky Sports channels were to existing Sky Sports subscribers.[185] BT engaged a market research agency to survey a representative sample of 1000 Sky customers (on Sky's DSat platform) who subscribed to a Sky package including at least one Sky Sports channel:[186]

(i) [✂]

(ii) [✂]

(iii) [✂].[187][✂]

3.55. Four years later, in the course of its Competition Act Complaint against Sky's anti-competitive imposition of the Grant-Back Condition, BT commissioned Compass Lexecon to undertake a detailed choice modelling exercise underpinned by a survey on consumer preferences. [✂][188][✂].

3.56. Therefore, despite being undertaken four years apart, both pieces of research proved the same point: [✂].

3.57. This is also borne out by operational experience of the WMO Remedy in practice. As the data in Section 2 of this Submission shows, fair and effective competition has not emerged. [✂][189][✂][190][✂]:

(i) Due to the high proportion of Sky Sports subscribers who choose to take the full Sky Sports proposition, there is clearly a high demand for these channels from existing subscribers and thus it is very difficult for a competitor to persuade such consumers to switch to a platform without these channels, even if it were possible to offer

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[185] Second witness statement of Marc Watson dated 7 September 2010, paragraphs 19-24. At the time the non-regulated channels were SS3 and SS4 as SS5 and SSF1 had not yet launched.

[186] [✂]

[187] In each scenario, option (a) stayed the same, whilst option (b) was altered to offer a different level of compensation.

[188] When this research was carried out, the non-regulated Sky Sports channels were SS3, SS4 and SSF1, as SS5 had yet to launch.

[189] Ofcom correctly references documentary evidence from BT that its inability to offer Sky Sports has hampered its ability to acquire subscribers (Consultation Document, paragraph 6.7)

[190] In contrast to Sky's estimated 5 to 6 million Sky Sports subscribers on the Sky DSat platform, BT currently has [✂] Sky Sports customers on BT TV.

significantly lower retail prices (which it is not, in light of the high wholesale prices that Sky charges).

(ii) As noted above by reference to Ofcom's own findings, Sky Sports subscribers have a higher willingness to pay than average subscribers (as evidenced by their higher ARPU), because they value having access to premium sports content. Given their higher willingness to pay to secure the full range of channels, these subscribers are likely to be less price sensitive and, as such, price discounting is unlikely to compensate these subscribers for the loss of the additional channels.

(iii) This is fully supported by the research referred to above in paragraph 3.55 to 3.57: [✂]. This is unsurprising in light of the evidence BT has set out in this section.[191]

3.58. In summary then, developments since 2010 indicate that the aggregate importance of SS3-F1 has increased, and Sky's approach to the marketing and scheduling of content across Sky Sports has resulted in there being, in effect, a single Sky Sports proposition. Due to the fact that the Sky Sports channels are now bundled, marketed, cross-promoted and sold effectively only as a single proposition, access to only a portion of the full Sky Sports proposition would not be sufficient to ensure fair and effective competition as rivals' offerings based around a sub-set of Sky's proposition will be insufficient to attract material numbers of subscribers with a willingness to pay for premium sports channels. This is fully supported by operational experience of the impact of the WMO Remedy to date. Therefore, in order to be effective, any remedy going forward must be based on providing access to the full Sky Sports proposition.

<u>None of the BT Sport channels are necessary to ensure fair and effective competition</u>

3.59. By contrast, none of the BT Sport channels individually, nor when considered as a single package of sports channels, are necessary to ensure fair and effective competition. The presence or absence of BT Sport is not a sufficient driver of pay TV subscribers' decisions to have an impact on the competitive process.

3.60. In fact, given the nature of the competition concerns in pay TV, which stem from Sky's entrenched incumbency advantages, it is unclear why Ofcom believes it is necessary to examine the market position of BT Sport at the level it has done in the Consultation Document. For the purpose of this review, the only question of relevance that relates to BT Sport is whether BT Sport is a materially stronger constraint on Sky than ESPN/Setanta

[191] Moreover, the relatively low incremental cost of producing the SS3-F1 channels means that the marginal value of these channels far exceeds their marginal cost. This is why Ofcom's previous WMO adjustments were manifestly insufficient.

were in 2010, in order to determine whether the regulation of Sky continues to be warranted. As the data in Section 2 (and Section 4 below) on Sky's strengthened retail market position, its increased profitability, and its strengthened position in terms of rights acquisitions since 2010 shows, it is manifestly clear that Sky is not competitively constrained by BT either at the retail level or when bidding for rights upstream, and that regulation of Sky Sports remains necessary and, in fact, should be strengthened to ensure fair and effective competition.[192]

3.61. Indeed, as explained in Section 2, a proper analysis of market developments demonstrates that [✂], while in many respects Sky's position has grown stronger since that time. As explained in detail below at paragraphs 3.67 and 3.76 to 3.89, BT's acquisition of the Champions League rights does not alter this analysis. As such, there is no basis to conclude that the regulation of BT Sport – in contrast to ESPN – has somehow become necessary or desirable to ensure fair and effective competition in pay TV markets.

3.62. Although BT believes it is unnecessary to go further and consider the specific issue of the importance of the content on BT Sport, other than in the context above, for completeness BT addresses Ofcom's analysis on this point below.

3.63. Ofcom's analysis supports BT's view that [✂] sports proposition than Sky Sports. Specifically Ofcom's own survey evidence[193] demonstrates that:

(i) In comparison to Sky where its Sky Sports subscribers pay a large monthly sum to access its premium sports channels, [✂][194]) of BT Sport subscribers actually pay to access the BT Sport channels [✂].

(ii) Indeed, in Ofcom's surveys when BT Sport subscribers were asked why they subscribe to BT Sport, the most common reason cited for taking BT Sport was that it '*comes with broadband package*', cited by 34% of respondents in Ofcom's October 2014 survey and 39% in the 2013 survey.[195]

(iii) Only 4% of subscribers claim that they would either switch pay TV provider or drop their service altogether if BT Sport was no longer available. This compares to

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[192] In the context of BT's Competition Act complaint to Ofcom, the data underpinning the Choice Modelling analysis described at paragraph 3.56 above [✂].

[193] Summarised at paragraphs 6.12 to 6.19 of the Consultation Document.

[194] BT has a total of [✂] BT Sport channel only Sky customers, against a total BT Sport base of [✂] (figures correct as at week ending 13 February 2015).

[195] *"E3A. Why does your household subscribe to BT Sport channels? PROBE: Any other reasons? / E3B. Looking at the following list, are any of the following reasons why your household subscribes to BT Sport? Please include any you already mentioned previously, as well as any others that may apply. PROBE: Anything else?"* (table 78, 2013 survey).

Ofcom's finding that between 12% and 24% (around 20%) of pay TV subscribers view access to Sky Sports as a critical element of their pay TV package.

(iv) Similarly, Ofcom notes in Annex 6 to the Consultation Document that its 2014 survey found that 23% of Sky Sports subscribers would switch Pay TV provider to an alternative that provided the Sky Sports channels if their current provider ceased to do so.[196] Ofcom's 2013 survey found that 30% would do so.[197] In contrast, only 10% of existing BT Sport subscribers say they would switch to a service providing BT Sport if their current provider ceased to provide it.[198]

(v) As noted at 3.16 above, even if BT Sport had the same or more Premier League rights as Sky Sports, [✂]. Even if BT had the majority of Premier League rights, only 17% of Sky Sports subscribers would additionally acquire BT Sport and only 9% would switch away from Sky Sports to BT Sport only.[199] This strongly suggests that [✂].

3.64. Moreover, all available empirical evidence suggests that BT Sport is [✂]:

(i) despite being available for free, [✂] in contrast BT notes that the vast majority of Sky Sports subscribers on the DSat platform are paying an incremental sum of £16.50 to £24.50 per month for access to Sky Sports. This is in addition to other services purchased from Sky;[200]

(ii) BT Sport is provided bundled as part of Virgin Media's XL TV package. In contrast, Virgin Media charges £17 per month for either SS1 or SS2, and £27.25 for all the Sky Sports channels;[201] and

(iii) survey evidence submitted by TalkTalk in the course of the VULA margin consultation demonstrated the low value that subscribers place on BT Sport in

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[196] Figure A6.1.

[197] "*D7. If <A2 SERVICE> stopped offering Sky Sports channels would your household continue to get your TV service with them? / D8. If you cancelled your TV service with <A2 SERVICE> do you think your household would....?*" (table 65, 2013 research).

[198] Consultation Document, Figure A6.1.

[199] "*Q.26 (prompted) Currently Sky Sports shows about 3 Premier League games per week, and BT Sport shows about 1 Premier League game per week. If this changed to a scenario where Sky Sports showed 1 Premier League game per week and BT Sport showed 3 Premier League games per week, but everything else stayed the same, what sports channels would you get?*" (Table 51, 2014 research).

[200] Moreover, as Ofcom notes in the Consultation Document, customers who subscribe to Sky Sports typically have a higher ARPU than Sky's other customers, and as set out above Sky TV customers must 'buy through' a pack of basic channels in order to access the Sky Sports channels, which also contributes significantly to Sky's overall pay TV revenues and profitability.

[201] http://store.virginmedia.com/digital-tv/channels/sky-sports.html.

aggregate: the total mean price that TalkTalk customers with access to BT Sport were willing to pay each month was £2.95.[202]

3.65. In view of this, BT challenges the reliance placed, and conclusions drawn, by Ofcom on survey findings as to the importance of BT Sport, specifically Ofcom's assertion that "*around 5% of pay TV subscribers may not consider a platform that did not offer BT Sport at all*".[203] BT strongly challenges this assertion:

(i) Ofcom has no basis for drawing the conclusion that it draws from its research data. Ofcom did not ask subscribers whether or not they would consider subscribing to a platform that did not offer BT Sport (even though it could have), so this figure is merely inferred from other responses. BT does not agree with the inference that Ofcom has drawn.

(ii) In fact, in light of the evidence in paragraph A6.20, it appears that the vast majority of subscribers who consider that it is important to have BT Sport also consider it is important to have Sky Sports. Given this overlap and the far greater importance of Sky Sports to subscription decisions, the availability of Sky Sports is the key determinant of consumers' choice of platform. As such, the 5% figure identified by Ofcom must be considered to be an absolute upper bound, materially over-stating the actual likely effect (which Ofcom itself appears to recognises in footnote 158 of the Consultation Document). In any event, for Ofcom to reach a conclusion on this matter it would need to determine respondents' behaviour in light of a clear counter-factual, namely whether or not a rival's platform could or could not offer Sky Sports (or indeed any of the other Sky basic channels that are also important to a subscriber's switching decision). It has not done so.

(iii) Equally, Ofcom's analysis does not specify any level of pricing in its questions to allow it to properly evaluate consumer trade-offs. For example, Ofcom has not made clear how BT Sport might be priced on a rival's platform, or what would happen to existing market prices, in order to make a sound determination of subscription choices and switching behaviour.

(iv) BT notes that Ofcom has also overstated its conclusions even on the data by including respondents who "*don't know*" how they would respond to the loss of BT Sport. A don't know response typically indicates ambivalence, and therefore it is inappropriate to consider that this group **might** consider that BT Sport is 'essential or very important'.

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[202] Fixed Access Market Reviews: Approach to the VULA margin (Consultation published 19 June 2014).
[203] Consultation Document, paragraph 6.18.

(v) Finally, there is no evidence presented by Ofcom that [✂] In fact, the only available statistic on consumer switching behaviour in pay TV markets, discussed in more detail below, suggests that switching remains extremely low.[204] [✂]

3.66. Ofcom suggests that the number of subscribers who are unlikely to consider a platform that cannot offer BT Sport rises to "up to 8%"[205] with the acquisition of live Champions League rights, though Ofcom does acknowledge that this effect is uncertain and may be greater or smaller. However, for similar reasons to those outlined in paragraph 3.65 there is no basis for Ofcom's assertion that BT Sport will have this level of effect on subscribers' platform choice, even once BT can offer Champions League:

(i) As set out above, Ofcom did not ask subscribers about their propensity to switch platform. The only questions that Ofcom asked about the impact of Champions League were about channel switching.[206] Moreover, even the effect on channel switching was low. Only 17% of current Sky Sports subscribers who do not subscribe to BT Sport would additionally subscribe to BT Sport as a result of BT's acquisition of Champions League content. The majority would continue to subscribe to Sky Sports only (51%).[207]

(ii) BT has previously explained in detail above the inconsistency in Ofcom's approach to considering BT's market position by reference to the aggregation of Champions League and Premier League content, while simultaneously ignoring the aggregation of content on Sky Sports. Ofcom's analysis in this case is equally problematic.

(iii) Further, as explained at paragraphs 3.76 to 3.89 below, Ofcom has in general overstated the importance of Champions League in subscriber decisions. Whilst some subscribers consider it important, Ofcom's analysis does not adequately take into account the importance of other sports content (and the aggregation of such content) in subscriber decisions.

3.67. Ofcom also claims that some customers place a "high" value on BT Sport, highlighting that 12% of BT Sport customers are willing to pay £5 or more for the channels.[208] It is unclear

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[204] See paragraph 4.42 below.
http://stakeholders.ofcom.org.uk/binaries/research/consumer-experience/tce-13/TCE_Research_final.pdf

[205] Consultation Document paragraph 6.27.

[206] *"Q.28 Currently ITV and Sky Sports both show Champions League football matches. This will change in 2015. From August next year Champions League matches will only be available on BT Sport. When that happens, if everything else stayed the same, what sports channels would you get?"* (table 61, 2014 research).

[207] *"Q.28 Currently ITV and Sky Sports both show Champions League football matches. This will change in 2015. From August next year Champions League matches will only be available on BT Sport. When that happens, if everything else stayed the same, what sports channels would you get?"* (table 61, 2014 research)

[208] Consultation Document, paragraph 6.15.

whether Ofcom is implying that £5 is a high value to pay for a premium sports channel, but for the avoidance of doubt it is not – for instance, a pay-per-view (PPV) movie rented from the Sky Store can range from £4.49 to £9.99.[209] More importantly, Ofcom's own analysis shows that [✂] Consequently, as Ofcom appears to concede at footnote 158, for these subscribers, the availability of BT Sport on a given platform would be expected to be second order to the availability of Sky Sports in terms of their platform subscription and switching decisions.

Ofcom's analysis regarding the individual sporting events that it examines is incorrect even on its own terms

3.68. For the reasons set out in detail above, BT submits that Ofcom's focus on individual sporting events is incorrect. The correct approach is to assess those sports channels and packages of channels necessary to be able to compete effectively: this extends to all of SS1-F1 and SS News HQ. On this basis Ofcom should regulate SS1-F1 and SS News HQ. However, even on its own terms, Ofcom's analysis of individual sporting events is defective due to errors of assessment and focus, which fundamentally undermine the conclusions reached. BT outlines why this is the case below.

<u>The Consultation Document does not distinguish between the effects of the majority and minority Premier League rights</u>

3.69. BT accepts that the live Premier League rights are uniquely placed given their strength in driving consumer decision-making, though for the reasons set out above, it is wrong for Ofcom to focus only on individual pieces of content. However, this unique ability to drive pay TV subscription decisions, and an associated high willingness to pay for the channels that contain these rights [✂][210]

3.70. Nonetheless, all of Ofcom's survey evidence treats "Premier League" as if it is a single proposition with a single set of characteristics. At the first stage of Ofcom's analysis, it determines that *"live Premier League content…. were capable of influencing the choices of a*

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[209] http://www.sky.com/products/ways-to-watch/sky-store/ .

[210] In the Pay TV Statement, Ofcom stated that "*Sky is likely to maintain its wholesale position if it wins the majority of the Live Premier League Rights. By "majority" we mean: either any five [of the six] packages of Live Premier League Rights; or four packages including package A (which contains 23 first pick games and is the most attractive package)*" (paragraph 5.493). Ofcom acknowledged that "*it could be argued that Sky would still maintain its position if it holds just three packages of Live Premier League Rights*". Since 2010, the packages of live Premier League Rights made available in the 2012 and 2015 PL Auctions have differed slightly from those made available in the 2006 and 2009 PL Auctions. Regardless, it is clear that in each PL Auction Sky retained the "majority" Premier League Rights. By implication, in the 2012 and 2015 PL Auctions, BT has been awarded the minority Premier League Rights, similar to Setanta and ESPN in the 2006 and 2009 PL Auctions

significant proportion of pay TV consumers and could therefore be considered key content."[211]

3.71. As a consequence of this conclusion Ofcom determines that "*[k]ey sports content is currently shown on Sky Sports and BT Sports*", and hence continues on to consider the question of limited distribution for both Sky Sports and BT Sport. Ofcom should have taken an intermediate step to consider the separate impact of the majority and minority Premier League rights. If it had, it would have been clear that BT's minority Premier League rights should not have been identified as "key content" at all,[212] and hence that there could be no issue with the limited distribution of BT Sport.[213] Although Ofcom goes on to consider the market position of BT Sport in its subsequent analysis ([✂]), the fact is that had Ofcom properly tested the two Premier League offerings, it would have been abundantly clear at the first stage of its analysis that BT's market position is irrelevant.

3.72. Ofcom's approach in this regard has also led to further errors. For example, at paragraph A6.6, Ofcom states that:

> *"Among respondents who subscribed to Sky Sports, 64% considered access to Premier League coverage to be essential to have as part of their pay TV service. For some of these respondents,* ***Sky Sports may not be that important in their choice of pay TV provider given the availability of Premier League matches on BT Sport….****"*

3.73. BT considers that there is no basis for the assertion that Sky Sports subscribers who consider Premier League coverage to be essential would be satisfied by the availability of Premier League on BT Sport:[214]

(i) Firstly, Ofcom has not empirically tested this proposition,[215] which is simply an assertion without any survey data to support it. As Ofcom did not differentiate

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[211] Consultation Document, paragraph 6.2.

[212] In particular, for the reasons discussed below, because they are not capable of influencing the choices of a significant proportion of pay TV subscribers.

[213] BT notes that Ofcom also cites the fact that BT Sport will have Champions League rights in the future. However for the reasons already set out at paragraphs 3.24 to 3.28 the basis of Ofcom's inclusion of Champions League rights in conjunction with Premier League rights is itself inconsistent with Ofcom's purported analytical approach.

[214] BT notes that this assertion is also inconsistent with Ofcom's statement at footnote 158 that "*We note that a number of respondents considered both BT Sport and Sky Sports as important. Given the preponderance of evidence that Sky Sports is substantially more important to customers than BT Sport, it is likely that this group of customers are likely to regard access to BT Sport as a key element of their platform choice only if Sky Sports is additionally available on the platforms that the customers are choosing between."*

[215] Ofcom did address the issue of majority / minority Premier League rights in questions 24-26 of the 2014 survey: *"Q24 (prompted) Currently Sky Sports shows about 3 live Premier League games per week, and BT Sport shows about 1 live Premier League game per week. If this changed to a scenario where both Sky Sports and BT Sport each showed 2live Premier League games per week, but everything else stayed the same,*

between the majority and minority Premier League rights when conducting this aspect of its survey it has no evidential basis for this conclusion.

(ii) More importantly, in considering the "Premier League" generically, Ofcom's research obscures the likely value that Sky Sports subscribers will place on having the depth of content that the majority Premier League rights implies, and as such are unlikely to be satisfied by the level of Premier League available on BT Sport.

(iii) Indeed, it is logical to assume that those subscribers who consider Premier League coverage to be essential would place **greater** importance on the ability to watch the majority of Premier League fixtures – conversely, the ability to watch a minority of fixtures would only satisfy those who do not see it essential to begin with.

(iv) Finally actual behavioural evidence suggests that the minority of fixtures on BT Sport is not sufficient given that [✂]

3.74. Ofcom's conclusion is, therefore, entirely speculative and unlikely to be correct. Moreover, it was clear when Ofcom was designing its surveys that the minority Premier League rights are not comparable to the majority Premier League rights [✂] This has also been demonstrated previously by the experience of Setanta, ESPN and BT:

(i) Setanta entered into administration in June 2009, due primarily to the shortfall between the amount it had paid for content rights (of which the minority Premier League rights accounted for the majority of its costs) and the amount it was able to earn from channel subscriptions. It is important to note that in relative terms, Setanta had a higher proportion of the Premier League rights than BT has today: Setanta held the rights to show 33% of the televised Premier League matches per season (46 matches out of 138) compared to BT's current 25% rights holding (38 matches out of 154).[216] [✂] It struggled, because its proposition overall was still significantly inferior to the Sky Sports proposition, and due to Sky's material incumbency advantages discussed in detail in Section 4 below.

(ii) Prior to being acquired by BT in 2013, in the 2011 financial year ESPN UK [✂], again largely due to a shortfall between content costs and channel subscription revenues

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what sports channels would you get? […] *"Q.26 (prompted) Currently Sky Sports shows about 3 Premier League games per week, and BT Sport shows about 1 Premier League game per week. If this changed to a scenario where Sky Sports showed 1 Premier League game per week and BT Sport showed 3 Premier League games per week, but everything else stayed the same, what sports channels would you get?".* However, these questions only address the issue in relation to channel choices, not whether both minority and majority rights are separately seen as 'essential'.

[216] Following the 2015 Premier League rights auction, BT's proportional share of live Premier League games will remain at 25% (42 matches out of 168) for the 2016/17 to 2018/19 seasons.

(and in circumstances where, compared to Setanta, it had managed to reach an accommodation with Sky on wholesale carriage terms to be included in Sky DSat retail package).

(iii) BT's strategy was to bundle BT Sport for free with BT broadband, [✂][217]

<u>There is a disproportionate and unwarranted focus on Champions League in the Consultation Document</u>

3.75. Ofcom also has a disproportionate focus on Champions League content throughout the Consultation Document. Ofcom conducts an extensive analysis of Champions League content, whilst simultaneously expressing reservations about its importance. Indeed, all of the points that Ofcom makes about Champions League content apply equally to other second-tier sports rights which Ofcom has chosen not to examine. Specifically:

(i) Champions League rights are said to influence consumer choice "*to a lesser extent*" than FAPL rights;[218]

(ii) it is "*unlikely that Champions League football alone could drive Pay TV retailer choice for a material group of customers*";[219]

(iii) "*Champions League coverage alone is unlikely to drive pay TV provider choice for a material group of customers*";[220]

(iv) under the heading, "*The impact of BT's acquisition of Champions League rights may be modest",* Ofcom states: "*we do not consider it is likely that the loss of live Champions League content* [by Sky] *will have a significant impact on the number of subscribers for whom the availability of Sky Sports is likely to be an important or determinative factor in their choice of Pay TV provider*";[221]

(v) Ofcom's ultimate conclusions on the importance of Champions League are cautiously expressed, for example "*Champions League coverage is also important to a large number of consumers, albeit to a lesser extent than live Premier League coverage, and <u>may</u> influence consumers' choice of pay TV retailer*"; and

[217] See section 6 of BT's submission to Ofcom in respect of CW/01103/03/13, Complaint from TalkTalk Telecom Group plc against BT Group plc about alleged margin squeeze in superfast broadband pricing (22 November 2013)
[218] Consultation Document, paragraph 1.12
[219] Consultation Document, paragraph 5.28
[220] Consultation Document, paragraph 5.34
[221] Consultation Document, paragraph 6.28

(vi) in every case these statements could be applied to the vast range of second-tier sports content currently on Sky Sports.

3.76. BT agrees with the sentiments underlying these reservations. However, in light of the tentative nature of Ofcom's assessment, it is misplaced for Ofcom to single out Champions League as 'key sports content', to the exclusion of other second-tier events. The primary reason for Ofcom drawing this conclusion is set out in paragraph 5.34 of the Consultation Document, namely that:

> *"Although our survey evidence suggests that Champions League coverage alone is unlikely to drive pay TV provider choice for a material group of customers, it seems very likely **that it could increase the degree to which a sports proposition which included Premier League coverage could influence consumers' choice of pay TV provider."** [Emphasis added]*

3.77. BT has already highlighted in detail at paragraphs 3.24 to 3.28, why this approach to Champions League is inappropriate and inconsistent with Ofcom's treatment of the issue of sports content aggregation more generally, and is also not compatible with Ofcom's own research.

3.78. Ofcom goes on to claim that its analysis in paragraph 5.34 is supported by the following evidence, which is also flawed:

(i) **The increase in the amount BT committed to spend to acquire the Champions League rights from 2015/16.** It is misleading to look at this single cost figure in isolation as an indicator of the "key" nature of content, and improper to draw inferences as a result that this content is more important than others in terms of its competitive effect. As discussed in Section 2 above, [✂].

(ii) **Statements made by Sky and BT in relation to the attractiveness of Champions League content.** BT notes, that, despite relying on them, Ofcom has not cited these statements in its Consultation Document. Moreover, BT notes that Sky's public statements have been unequivocal as to the lack of importance of Champions League. For example, Jeremy Darroch, Chief Executive of Sky, was widely reported to have commented that Champions League programming accounted for less than 3% of viewing on Sky Sports and said there was a limit to how much people would pay for this content.[222] This is consistent with Ofcom's own survey findings which found

[222] *BT limbering up for next big TV football auction says CEO* (Reuters), 5 December 2013, http://uk.reuters.com/article/2013/11/20/uk-britain-tv-sports-idUKBRE9AJ0YY20131120.

that live Champions League was cited as the main reason for taking Sky Sports by just 2% of subscribers.[223]

3.79. The reality, as the evidence set out below demonstrates, is that: (a) Champions League content remains in a second-tier of events with a variety of other sports (which, as established in Section 2, Sky still largely controls); and (b) when content aggregation is considered more rigorously, it is evident that BT's acquisition of Champions League has no bearing upon Sky's market position in light of Sky's continued control of the majority Premier League rights, together with its agglomeration of rugby, football league, cricket, tennis, golf and other attractive second-tier content.

The Champions League rights remain in the second-tier in terms of attractiveness

3.80. The second-tier nature of the Champions League rights is confirmed by an analysis of what the rights comprise, and average audiences and unique reach data, as well as Ofcom's own research data.[224]

(i) In relation to the rights themselves:

(a) Whereas Sky's majority Premier League rights offer all fans the opportunity to see their team on multiple occasions over the season, Champions League coverage is usually limited to just four Premier League clubs, and unless those teams progress, there will be limited opportunities to watch them. The total number of Champions League matches featuring Premier League clubs will typically be around 35-40, very substantially less than the 116 (set to increase to 126 from 2016) live Premier League matches that Sky is able to offer.[225] This fact was underscored recently in a tweet by Graham McWilliam Sky's Group Director of Corporate Affairs, in which he stated "*Right decision for us not to chase Champ League. £300m only guarantees 26 matches with British teams. #premierleague matters more to fans*".

(b) Ofcom also recognised this in the Pay TV Statement, where it concluded that whilst certain Champions League matches are attractive to subscribers, "*The Champions League also features a large number of matches that are*

[223] See Figure 5.3 of the Consultation Document.

[224] The source for the viewing data used throughout is: BARB data as analysed by Digital-I for BT.

[225] In 2007/08 (the season considered by Ofcom in the Pay TV Statement, when two Premier League clubs reached the Champions League final for the first time), there were exceptionally 47 Champions League matches featuring FAPL clubs.

relatively less attractive to UK viewers (because they do not feature Premier League teams)".[226]

(c) All Champions League group stage matches are broadcast simultaneously, generally with eight matches being broadcast at the same times on Wednesday and Thursday evenings. This means that the headline number of matches acquired by BT (145 Champions League matches per season) is not, in practice, directly comparable to the number of live Premier League matches. In 2012, Sky and ITV were only able to broadcast 75 of the 145 Champions League matches on linear TV channels (with the remaining matches available via interactive services behind the red button).

(d) [✂][227]

(ii) In relation to audiences:

(a) In 2013/14, the average audience for a Champions League match broadcast on Sky Sports was 362,000 viewers.[228] This is considerably lower than the average audience for a Premier League match in the 2013/2014 season or F1 races in 2014 on Sky Sports, which are (respectively) 1.2 million and 910,400 subscribers (for F1 races broadcast exclusively on SSF1). Indeed, it is even lower than the average audience on SSF1 for F1 races in 2014 broadcast by both Sky and the BBC (672,000 viewers).

(b) Audiences for Champions League matches are considerably lower than average when a Premier League team is not playing. Out of 67 Champions League matches broadcast by Sky on its linear channels (i.e. not behind the red button) in the 2013/2014 season, more than half (37 matches) did not feature a Premier League team. The average audience of these matches (211,600) was considerably lower than the average for those matches featuring Premier League teams (722,600). Further, only one Premier League match shown on Sky Sports in the 2013/2014 season achieved a

[226] Pay TV Statement, Annex 4, paragraph 2.17.
[227] [✂]; in 2014/15, ITV broadcast 15 Champions League matches.
[228] Note that BT has calculated this figure using the Digital-i produced average audience for each match, rather than the minute-by-minute match data.

lower average audience.[229] The lowest average audience for a Champions League match in the 2013/2014 season was just 9,200 viewers.[230]

(c) Indeed, even when a Premier League team **is** playing in a Champions League match shown on Sky Sports, the average audience is lower than that for a Premier League match on Sky Sports. For example, the average audience for Champions League matches in the 2013/14 season featuring Chelsea broadcast on Sky Sports was 696,300 (8 games in total). Comparatively, the average audience of the 20 Premier League games featuring Chelsea in 2013/2014 that were broadcast on Sky Sports was almost twice as large (1,372,000).[231]

(iii) In relation to unique reach:

(a) BARB unique reach data for Champions League demonstrates that it is a second-tier right, and is not comparable to Premier League. Based on pay TV only viewing in 2012 (i.e. excluding FTA audiences that can be delivered by ITV), Premier League delivers a unique reach of 874,000 viewers. In comparison, the unique reach of Champions League was only 158,000.

(b) The unique reach figure for Champions League is much closer to that of other second-tier rights. Indeed the unique reach of F1 on pay TV (for F1 events broadcast exclusively on SSF1) in 2012 was 544,000[232] – almost three and a half times the unique reach delivered by Champions League, and still scores more highly even for races broadcast by both the BBC and Sky (161,000). Similarly England test match cricket (even excluding the Ashes as there was no Ashes tournament in 2012) delivers 1.75 times the unique reach of Champions League (282,000 viewers).

(iv) In relation to incremental unique reach:

(a) When compared with Premier League, Champions League content has virtually no unique reach among Pay TV viewers (i.e. excluding FTA audiences that can be delivered by ITV). This means that all Sky Sports subscribers who watch Champions League on Sky Sports are also likely to

[229] The Premier League match with the lowest average audience broadcast by Sky Sports in the 2013/14 season was Tottenham Hotspur v Aston Villa (Kick-Off 16:00, 11 May 2014, Sky Sports 3), average audience 97,000.
[230] Live Champions League - PSG v Bayer Leverkusen (Kick-off 7.45pm), 12 March 2014, Sky Sports 4.
[231] Source: Digital-i BARB data
[232] BT notes that F1 featured in a Sky Sports free weekend, which may have increased this figure.

watch Premier League, whereas over 4.1 million Sky Sports subscribers watch Premier League on Sky Sports but do not watch Champions League on Sky Sports. Thus, it is inaccurate to single out Champions League content alongside Premier League from other second-tier content. Subscribers who have an interest in Champions League content will largely already have been attained by Premier League content alone.

(v) In relation to Ofcom's own research data:

(a) In its 2013 survey, Ofcom asked Sky Sports subscribers to provide reasons for their subscription. Only 23% cited the Champions League, far less than live sport in general (43%) or the Premier League (35%) and comparable to cricket and F1 (both 18%) or rugby union (16%). Moreover, only 9% of respondents cited Champions League as one of their 'three main reasons' for subscribing to Sky Sports, the same proportion as cited test cricket and F1, and considerably less than Premier League (20%).

(b) In its 2014 survey, Ofcom found that 28% of Sky Sports subscribers' reasons for subscription included Champions League, again comparable to cricket (20%) and considerably less than Premier League (43%). Crucially, in this survey only 2% cited the Champions League as their main reason for subscribing to Sky Sports, compared to Premier League (27%), cricket (4%), rugby union (4%), F1 (4%) and "*to watch a wide range of live sports coverage*" (10%).

(c) Ofcom's 2013 and 2014 survey results paint a broadly similar picture to the research undertaken in relation to the 2010 Pay TV Statement, which found that the Champions League was a motivation for only 14% of subscribers, comparable to test cricket and rugby union (both 11%) and considerably behind Premier League (28%).

(d) It is also illustrative that only 17% of current Sky Sports subscribers who do not subscribe to BT Sport would additionally subscribe to BT Sport as a result of BT's Champions League content. The majority would continue to subscribe to Sky Sports only (51%).

(e) As previously highlighted above, BT also notes that the timing of the survey is likely to have influenced the responses of participants. The surveys were conducted in November 2013 and October 2014, in the midst of the group stage of the Champions League games. This is the part of the season when the highest number of English Premier League teams are taking part in the competition and games featuring these teams would be at their most frequent. As such interest in the Champions League would have been higher than average. Conversely many other sports would not have been in the spotlight at this time, if taking place at all, such as tennis or cricket and so respondents' interests in them would have been lowered at the time of the survey.

(f) This means that, at best, Ofcom's survey evidence provides a snapshot of the importance of the Champions League at the relevant points in time, but isn't necessarily reflective of its average importance or ability to influence behaviour. For example had Ofcom conducted the survey during the Ashes, BT would expect that respondents would have placed much more emphasis on cricket as a reason for subscribing to their sports proposition.

3.81. Moreover, BT notes that Ofcom states that "*[s]urvey evidence relevant to the forthcoming move of live Champions League coverage to BT Sport in August 2015 is limited*,"[233] and then goes on to state "*However, evidence on the proportion of Sky Sports subscribers that took Sky Sports in order to access Champions League coverage suggests that the availability of Champions League content is likely to strongly influence the choice of pay TV provider of around 3% of pay TV subscribers.*"[234] The evidence Ofcom relies upon to reach this 3% figure is based on the proportion of Sky Sports subscribers who (unprompted) identified Champions League as a reason for their subscription (10%).[235]

3.82. However, BT notes that Ofcom omits reference to two survey questions that directly address the impact of the importance of Champions League content on BT Sport, specifically:

(i) *"Q.28 Currently ITV and Sky Sports both show Champions League football matches. This will change in 2015. From August next year Champions League matches will only be available on BT Sport. When that happens, if everything else stayed the same, what sports channels would you get?*;*"* and

(ii) *"Q.29 You said that your household would get [INSERT ANSWER FROM Q.28], how certain are you that your household would make this choice in practice?"*.

3.83. The responses to these questions show that only very few subscribers plan to switch **channels** as a result of Champions League moving to BT Sport. 4% say they would take both BT Sport and Sky Sports, and 5% say they would switch away from Sky and take BT Sport only.[236] The number of subscribers who might be willing to switch **platforms/pay TV**

[233] Consultation Document, paragraph 6.21.
[234] Consultation Document, paragraph 6.21.
[235] See Consultation Document, paragraph A6.30.
[236] Table 61, 2014 research.

providers will be far lower than the number who might be willing to switch channels, and as such Ofcom's claim that the availability of Champions League content on BT Sport is likely to strongly influence the choice of pay TV provider for around 3% of pay TV subscribers simply cannot be supported by Ofcom's own research findings.

3.84. Moreover, BT notes that Ofcom's omission of critical information in asking Q28 means that respondents are likely to have significantly over-stated the impact of the change on their channel switching behaviour. The Champions League will not "*only be available on BT Sport*" (i.e. only available on pay TV) as Ofcom's question implies. [✂] (see footnote 217).

3.85. BT notes that Ofcom chooses not to take account of responses to this survey question, stating that: "*…we do not have confidence that this particular hypothetical question was well understood or is sufficiently robust for this purpose.*" Ofcom states that one of the reasons for discounting responses was that the scenario posed may not reflect the reality of the BT Sport offering with Champions League in terms of prices. However, that is the case for all of the switching questions that Ofcom has asked (where no assumptions are made in terms of pricing impact), yet it chooses to place weight on those. Ofcom also cites the high proportion of respondents saying "don't know" (21%) in response to the question as another reason for discounting this data. But a large proportion of 'don't knows' does not necessarily imply confusion at the question. It may equally show ambivalence as to the availability of Champions League content, suggesting it is not important in subscriber decision making, which BT believes is the more correct interpretation. Finally, Ofcom also cites the fact that 66 respondents provided potentially counter-intuitive responses to these questions. However, this is the nature of research surveys and a 3% error rate is not an appropriate basis for placing no weight on responses that go to an important issue. [237]

3.86. It is not open to Ofcom to pick and choose which survey data it will rely upon. Ofcom has clear survey data which shows that the availability of Champions League content on BT Sport is **not** likely to strongly influence the choice of pay TV provider for around 3% of pay TV subscribers, and Ofcom must properly reflect this finding in its conclusions.

3.87. In summary, in light of the factors outlined above, a more rigorous examination of the role of second-tier content is required. BT considers that this would show that Champions League rights remain in a second-tier of attractiveness, alongside various cricket, rugby, golf, tennis events and now F1, similar to the position in 2010.[238] As such, Ofcom is misplaced in selectively focussing on the impact of BT's acquisition of Champions League rights, whilst

[237] Consultation Document, footnote 253
[238] See figure 35 of the Pay TV Statement.

overlooking the enormous breadth of other second-tier sports rights aggregated on the Sky Sports proposition, which has materially strengthened Sky's position since 2010.

3.88. Equally, there can be no case that BT's acquisition of the Champions League rights will lead to a diminution of the strength of the Sky Sports proposition. As the data above and in Section 2 shows, since 2010 Sky has maintained its advantages both in terms of first-tier rights (by holding and strengthening its position with respect to the majority of FAPL rights) and second-tier rights by maintaining a wide range of important second-tier rights such as test cricket, international rugby, tennis and key golf events, and materially strengthening that position with the addition of F1, the US Masters and the British Open golf.

4. SKY ENJOYS A STRONG MARKET POSITION ACROSS ALL PARTS OF THE VALUE CHAIN

4.1. This section of BT's Response addresses five overarching issues in Ofcom's Consultation Document.

(i) First, BT explains why it agrees with Ofcom's finding that Sky has had, and continues to hold, a very strong market position (with a market share that clearly equates to dominance[239]) in the wholesale supply of sports channels (paragraphs 4.3 to 4.15);

(ii) Second, BT agrees with Ofcom that Sky has a very strong retail position overall (with a market share usually associated with dominance) and particularly in respect of those retail subscribers who are willing to pay for premium sports channels (paragraphs 4.16 to 4.30) Neither BT's market position with BT Sport nor its acquisition of Champions League rights will undermine Sky's strong retail market position (paragraph 4.30);

(iii) Third, BT explains why Sky has – and will continue to hold – material incumbency advantages at the retail level. In particular, BT explains why each of the three barriers to entry and expansion identified by Ofcom in the Pay TV Statement (and restated by the CC in the Movies Investigation) continues to remain relevant today – and will continue to remain relevant going forward. (paragraphs 4.31 to 4.48); and

(iv) Fourth, BT endorses Ofcom's finding that Sky continues to have material advantages when bidding for live sports rights. In particular, as identified in 2010, Sky's bidding advantages perpetuate a 'vicious circle': Sky's systematic ability to win perishable sports rights at the upstream level, combined with the limited wholesale distribution of its Sky Sports proposition, bolsters its position at the wholesale and retail levels, further entrenching its strong market position across the value chain. BT also explains why BT's ability to monetise its investment in sports rights indirectly by providing BT Sport to its broadband subscribers does not overcome Sky's bidding advantages (paragraphs 4.49 to 4.89).

4.2. Taken collectively, this analysis confirms that Sky enjoys a strong market position across all parts of the value chain, as supported by all the available evidence, and hence is in a position to undermine fair and effective competition through limited distribution of its Sky Sports proposition.

[239] As set out in Annex 1, BT recognises that under s.316 Ofcom is not required to establish dominance before intervening. Nonetheless, BT believes that it is instructive to note that Sky's strong market position is such that it would equate to dominance under ex post competition law.

Sky's market position in the wholesale supply of sports channels

4.3. BT agrees with Ofcom's finding that Sky has had, and continues to hold, a very strong market position (with a market share equivalent to dominance) in the wholesale supply of sports channels. In the Consultation Document, Ofcom uses two metrics to consider wholesale market shares:

(i) wholesale revenues (representing a demand-side assessment of market shares); and

(ii) sports rights expenditure (as a supply-side assessment of market shares).

4.4. BT sets out its comments on each of these in turn below.

Wholesale revenues (demand-side assessment)

4.5. BT believes that the most robust and appropriate basis for calculating wholesale market shares is on the basis of wholesale revenues. On the basis of that calculation, BT agrees with Ofcom's finding that Sky "*has significant shares of revenue in the supply of key sports channels which are consistently in excess of 80%*".[240] It is clear from Ofcom's analysis that Sky's wholesale market share has barely declined since Ofcom's regulatory intervention in pay TV markets in 2010.

4.6. Ofcom states that Sky's share of wholesale revenues has declined by approximately 6% since the entry of BT Sport.[241] This figure is likely to over-estimate the decline in Sky's wholesale market share for the following reasons:

(i) Due to the wider availability of BT Sport (as a result of BT's business model) and hence a higher volume of imputed charges for wholesale self-supply,[242] Ofcom's calculation is likely to overstate BT Sport wholesale revenues.

(ii) It does not appear that Ofcom has included an imputed charge for wholesale self-supply by Sky for its self-retailing activities on NOW TV or Vodafone. These revenues should be included in Ofcom's assessment since (a) Ofcom includes an imputed

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[240] Consultation Document, paragraph 6.33.

[241] Consultation Document, paragraph 6.34.

[242] Specifically, as a result of the fact that BT Sport is given away for free to BT's broadband and TV subscribers, the volume of subscribers who are self-supplied is very large compared with that of Setanta (and ESPN had no self-supply). This materially increased volume, when multiplied by Ofcom's (high) imputed wholesale charges for those subscribers who are receiving BT Sport for free will lead to an erroneously large determination of BT's wholesale self-supply revenues. BT also notes that these "imputed self-supply" charges are an estimate of the wholesale value that BT receives by dint of its broadband customers, yet Ofcom does not appear to include an equivalent imputed benefit to Sky from bundling broadband (either in its wholesale or in its retail calculations).

charge for wholesale self-supply by BT to BT Sport app only customers;[243] and (b) as noted at paragraph2.3(vi), the sale of daily and weekly Sky Sports passes by Sky via NOW TV, and Sky's self-retailing of its Sky Sports proposition on Vodafone represent additional revenue streams which serves to strengthen Sky's market position further. If wholesale proxies for these revenues were included as they should be, Sky's imputed wholesale revenues would be higher than Ofcom's calculations suggests.

4.7. These omissions both overstate BT's wholesale revenues from BT Sport, and under-estimate Sky's wholesale revenues. When corrected these are likely to account for a considerable portion of the 6% decline in Sky's market share identified by Ofcom,[244] rather than any actual increased competitive constraint on Sky's revenues resulting from BT's entry. In any event, the fact that Sky's market share has declined by a maximum of 6%, [✂] and the existence of the WMO regulatory intervention, demonstrates that BT Sport is not an effective constraint on Sky.[245]

4.8. For the same reasons, while BT agrees with Ofcom's finding that its wholesale market position can be described as, at best, "*relatively modest*",[246] [✂].[247] However, it is not necessary for Ofcom to reach a final view on BT's market share given that, on any plausible approach, Sky's market share is clearly in excess of 80% (which is certainly at a level representative of market power where fair and effective competition can be impacted, and thus within the scope of s.316) and BT's market share is clearly at a level where its actions cannot be expected to have any impact on competition.

Sports rights expenditure (supply-side assessment)

4.9. In terms of Ofcom's supply-side assessment of wholesale market shares, BT notes that, again, Sky's market share is high, consistent with a strong market position (and in the range of market shares normally associated with dominance). This is despite the fact that Ofcom's adopted approach in its supply-side estimate of market shares is likely to lead to Sky's market share being materially understated.

[243] Consultation Document, paragraph A7.5.
[244] BT estimates that Ofcom has overstated its wholesale revenues by [✂].
[245] BT supports Ofcom's approach of expressly including HD revenues in the calculation of Sky Sports' wholesale market share, given that Sky charges an additional wholesale fee for HD supply, and, as noted in Section 3 at 3.48, Sky has sought to use HD wholesale supply of the Sky Sports channels as a source of differentiation from its competitors. As such, there can be no doubt that HD makes a material contribution to Sky's strong market position, both in terms of the additional revenues Sky is able to generate, and its ability to provide an enhanced viewing experience that subscribers now expect as standard.
[246] Consultation Document, paragraph 6.35.
[247] BT estimates that [✂]

4.10. Firstly, a methodology based around a simple comparison of expenditure on sports rights by Sky and BT provides only a limited insight into market positions. As Ofcom recognises, as the entrenched incumbent operator Sky has a number of material bidding advantages (discussed in detail below at paragraphs 4.49 to 4.89), as well as a number of other advantages that result from its longstanding commercial relationships with rights-holders, [✂].[248] In light of Sky's bidding advantages, [✂].[249] As such, Ofcom's simple assessment of shares of rights expenditure is likely systematically to overstate BT's market position and consequently understate Sky's in the wholesale supply of premium sports channels.

4.11. This methodological flaw is further compounded by the fact that Ofcom also includes expenditure on sports rights held by FTA broadcasters in its market shares assessment. There are a number of reasons why it is incorrect to include this expenditure in the calculation:

(i) The purpose of Ofcom's WMO Review is to determine the on-going necessity of the WMO Remedy in delivering fair and effective competition in pay TV markets. Sports rights that are currently held FTA have no bearing on competition as between retail pay TV providers – by definition, this content is available on all retail pay TV platforms and so cannot influence retail pay TV subscription decisions.

(ii) Many of the sports rights that are available FTA are not permitted to be acquired by pay TV broadcasters, as they are Category A Listed Events.[250] This includes many of the major sporting events that are most important to consumers[251] and hence that are most likely to drive FTA broadcasters' expenditure on sports rights. At a minimum expenditure on these events must be excluded from Ofcom's wholesale market share calculations.

(iii) Many of the major sporting events available FTA are available FTA as the rights holders have deliberately chosen the strategy of ensuring their rights are available FTA in order to maximise exposure for their sporting event rather than maximising potential revenues via pay TV.[252] Since those rights holders have made the choice

[248] [✂].

[249] In this regard, BT refers Ofcom to Section 2 paragraph 2.46 above explaining why it is necessary to consider the context of bids for rights, rather than simply examine rights expenditure alone.

[250] http://stakeholders.ofcom.org.uk/broadcasting/broadcast-codes/code-sports-events/

[251] The current list is: The Olympic Games, The FIFA World Cup Finals Tournament, The European Football Championship Finals Tournament, The FA Cup Final, The Scottish FA Cup Final (in Scotland), The Grand National, The Derby, The Wimbledon Tennis Finals, The Rugby League Challenge Cup Final, and The Rugby World Cup Final.

[252] For example: "*Fees paid by international broadcasters are vital… As important to the All England Club is to carry Wimbledon to as large an audience as possible, which is why, in most parts of the world, the Club aims to*

not to offer the rights via pay TV, again, it is clear that these rights cannot influence competition at the wholesale level in pay TV.[253]

(iv) Many of the major events available FTA tend to be time limited, stand-alone competitions (such as Wimbledon which is shown for only two weeks per annum) and are also infrequent (such as the football World Cup which is shown for four weeks every four years). Clearly, such isolated events on FTA differ in terms of product characteristics from the wholesale provision of premium sports channels which are composed of a constant schedule of sporting events in order to drive subscriptions.

(v) Therefore, by including FTA expenditure, Ofcom understates Sky's relative share of expenditure on sports rights, and consequently risks understating its strong wholesale market position.

4.12. In the Consultation Document, Ofcom includes FTA rights expenditure, and estimates that Sky's share of expenditure on sports rights in 2013/14 accounted for more than 60% of all sports rights expenditure, and BT's expenditure accounted for around 15%.[254] In the tables below, BT has estimated expenditure on sports rights and market shares in 2015/16 and 2016/17, both including and excluding FTA expenditure on rights.[255] As can be seen, including FTA expenditure masks the true extent of Sky's market share. Indeed, when the distortive effect of FTA revenues is removed, Sky's wholesale market shares based on expenditure are very similar to its market shares discussed above based on wholesale revenues.

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place at least part of The Championships on national, free-to-air television." (Source: Wimbledon website, "Television", available at: http://www.wimbledon.com/en_GB/about_aeltc/201205091336585368259.html.

[253] BT notes, as set out in Section 3 above, to the extent such rights holders have chosen to move from FTA to pay TV, the rights have all moved to Sky (F1, US Masters, British Open).

[254] Consultation Document, paragraph 6.34.

[255] Ofcom's Consultation Document states that expenditure on sports rights in 2013 was £1,808m (based on August 2013 forecasts).

Market shares on a rights expenditure basis including FTA

Broadcaster	2015/16	2016/17[256](m)
Sky (estimated)	[✂]	[✂]
BT	[✂]	[✂]
BBC (estimated)	[✂]	[✂]
ITV (estimated)	[✂]	[✂]
Others (estimated)	[✂]	[✂]
Total	[✂]	[✂]

Market shares on a rights expenditure basis excluding FTA

Broadcaster	2015/16	2016/17[257]
Sky	[✂]	[✂]
BT	[✂]	[✂]
Total	[✂]	[✂]

4.13. Ofcom also highlights in its Consultation Document that BT's wholesale market share calculated on the basis of rights expenditure will increase in August 2015 to 30% (**including** FTA) as a result of BT's acquisition of the Champions League rights.[258] However, as a result of the fact that Ofcom only adjusts its share calculation to take account of the change in ownership of Champions League rights,[259] rather than considering the changes in rights expenditure as a whole in 2015, it over-estimates the increase in BT's market share on this basis. In particular, in August 2015, BT estimates that Sky's expenditure on rights that it has renewed will have led to an increase in expenditure of at least £80m since August 2013 (i.e. an amount comparable to its annual expenditure on Champions League rights, such that in August 2015, Sky's expenditure on sporting rights will still be higher than it was in August

[256] BT has, conservatively, estimated that in addition to the increased expenditure on Premier League rights, other rights costs will increase by [✂]
[257] Adjusted to reflect increase in Premier League costs only. Sky will be paying an additional £631 million per annum; BT will be paying an additional £83m per annum.
[258] Consultation Document, paragraph 6.35.
[259] Consultation Document, footnote 167.

2013).[260] As a result of these two errors, BT's market share on a rights expenditure basis will only increase to a maximum of [✂]% (including FTA i.e. on the basis of Ofcom's calculation) and [✂]% excluding FTA.

4.14. Moreover, BT believes it is inappropriate to consider BT's forward looking share of expenditure, without also factoring in Sky's forward looking share of expenditure as a result of the latest Premier League auction. From August 2016, Sky's annual expenditure on the Premier League rights alone will increase by £632 million. As the tables above show, BT estimates that in 2016, total expenditure on sports rights (including FTA) will be around £[✂] billion per annum, or almost £[✂] billion excluding FTA. Sky's wholesale market share on the basis of rights expenditure will remain at almost [✂] excluding FTA, and BT's market share [✂] estimated by Ofcom.[261]

<u>Conclusion on Sky's wholesale market position</u>

4.15. As shown by Ofcom's Consultation Document, Sky has held, and continues to hold, a strong wholesale market position with market shares in the range normally associated with dominance. On the basis of wholesale revenue market shares, it is clear that Sky's wholesale market share has barely declined since Ofcom's regulatory intervention in pay TV markets in 2010. Even following adjustments for changes in rights expenditure with the movement of the Champions League rights from Sky to BT, a supply-side analysis of share of rights expenditure also shows Sky's strong market position persists going forward.

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[260] This increase is due to increased expenditure on the following rights in 2014 and 2015. In 2014, Sky commenced broadcasting events under renewed rights agreements. BT estimates that Sky incurred an additional £30 to £31m in annual rights costs compared to the previous rights agreements for these events, as follows: (i) ATP World Tour Masters (additional £5.8m per annum), (ii) Matchroom (additional £7m per annum), (iii) European Rugby (additional £9.5m per annum), (iv) Cricket Sri Lanka (additional £1m per annum), (v) Cricket New Zealand (additional £1.5m per annum), (vi) Wrestling (WWE) (additional £4.67m per annum), and (vii) other rights (e.g. Speedway, LPGA) (£1m per annum). In 2015, BT understands that Sky will commence broadcasting the following events under renewed rights agreements. BT estimates that Sky has/will incur an additional £52.6m in annual rights compared to the previous rights agreements for these events: (i) ICC (additional £11.1m per annum), (ii) USGA (US Open Golf) (additional £4m per annum), (iii) US PGA Tour (additional £13.3m per annum), (iv) US Masters (additional £1.67m per annum), (v) NFL (additional £7.67m per annum), (vi) Indian Premier League (additional £1.5m per annum), (vii) US PGA Tour (additional £13.3m per annum).

[261] BT notes that these figures are likely to understate Sky's position, given that BT has adopted a conservative approach to estimating the amount Sky is paying for its live content rights, as the amount Sky pays for most content rights is not in the public domain.

Sky has a strong retail position overall and particularly in respect of those retail subscribers who are willing to pay for premium sports content

4.16. BT agrees with Ofcom's findings that Sky maintains a very strong market position in the retail supply of pay TV, as evidenced by an assessment of retail market shares. Sky's retail pay TV market share is in excess of 60% on whichever metric Ofcom uses.

4.17. For the reasons set out in detail in Section 3 above, in order to ensure fair and effective competition in pay TV markets, the correct analytical approach to considering the retail market position of BT Sport and Sky Sports is to look at the retail products made available to consumers, namely retail products including pay TV sports channels and packages of channels. This means assessing retail market shares on this basis.[262] Nevertheless, BT acknowledges that Ofcom's analysis of Sky's position in retail supply to all pay TV subscribers (including those that do not take Sky Sports or BT Sport) is also relevant as it provides corroborative evidence that Sky's market position at the retail level is exceptionally strong.

4.18. However, BT disagrees with extending the analysis of Sky's retail market shares to include other communications services beyond pay TV. The purpose of the WMO Review is to address the manifest competition problems in pay TV markets stemming from Sky's entrenched dominant position and limited distribution of its Sky Sports proposition. While these issues are now spilling over into wider communications bundles (as highlighted in Section 2 above), that does not mean that the correct approach analytically is for Ofcom to assess Sky's retail market position in pay TV by reference to other communications products such as broadband and telephony where Sky is subject to a considerably greater degree of competition (as a result of stringent regulation of the relevant wholesale inputs). Such an

[262] BT notes that for the purposes of the WMO Review, Ofcom explicitly excluded OTT operators from its analysis of both wholesale and retail competition, (Consultation Document paragraph 2.11). BT agrees with Ofcom's assessment that (i) stand-alone OTT providers have not entered into the provision of sports content, (ii) a comparatively small share of consumers appear to subscribe to OTT services as opposed to traditional pay TV services, and (iii) the majority of OTT subscribers also appear to subscribe to a traditional pay TV subscription, suggesting these services are complements rather than substitutes (Consultation Document, paragraphs 6.41-6.42). However, even if Ofcom were to include OTT operators in its analysis, it would make no difference to the outcome since those operators face the same constraints as existing pay TV retailers in the provision of premium sports channels, as discussed above in Section 2, paragraphs 2.59 to 2.63. BT also notes that despite the CC's expectation in the Movies Investigation that OTT operators were likely to increase the constraints on Sky in acquiring movie rights in the first subscription window from the major US studios (Paragraph 6.119, CC Movies Decision), in practice, as BT stated at the time, this has not come to pass and Sky has retained the first subscription rights to all major US studios. It is clear that the potential constraint from emerging OTT operators that the CC identified has not had any effect in practice.

approach would merely serve to artificially dilute Sky's retail market share[263] and obfuscate the competition problems arising in pay TV.[264]

4.19. Below, BT comments on each of the three methodologies used by Ofcom to assess Sky's retail market shares.

Method 1: Retail market shares using retail revenues

4.20. Consistent with BT's position set out in detail in Section 3 that the relevant product for Ofcom's analysis is premium pay TV sports channels and packages of channels, BT considers that the most appropriate tool for measuring retail market shares is retail revenues associated with these channels and packages of channels. This measure most closely aligns with the assessment of Sky's ability to use its concentration of retail subscribers with a high demand and willingness to pay for premium sports channels, and limited distribution of those channels, to restrict the emergence of fair and effective competition. As such, the retail revenue shares-based methodology, focusing on those subscribers who subscribe to premium sports channels or packages of channels, provides the most appropriate analytical framework for Ofcom's analysis.

4.21. However, as Ofcom notes, its calculation of market shares under this methodology is likely to overstate BT's market share as a result of the fact that Ofcom has included revenues from customers who receive BT Sport for free on Virgin Media (as part of the XL package), on Sky DSat (as a BT Broadband customer) and on BT's YouView platform, and not all of these customers will be interested in the content shown on BT Sport.[265] BT believes that the extent of this over-statement is likely to be high as, even on the basis of Ofcom's own surveys, a large number of customers who receive BT Sport at no extra cost with their Virgin package or with their BT Broadband subscription are unlikely to value BT Sport very highly, or place

[263] BT notes for example in Table 6.2 in the Consultation Document, that when Sky's retail market shares are calculated for pay TV only its market shares are in the region of 60% to 80% under either metric, whereas when broadband and voice revenues are added, the estimate for Sky's retail market share drops to 40% to 60%.

[264] BT also notes that Ofcom has to date found across its telecoms and broadcasting market reviews that separate product markets continue to be the relevant focus of any economic analysis of market power (in the telecoms sectors) and of fair and effective competition (in the broadcasting sector). It would be entirely inappropriate for Ofcom to adopt an approach of assessing whether Sky's wholesale inputs require regulation by assessing Sky's market position by reference to a wider market, while simultaneously assessing the necessity of regulation of BT's wholesale inputs by reference to narrow, product-specific markets. It would also be inconsistent with the approach Ofcom took in the VULA investigation, where it consistently underlined its view that it wanted to consider the competition issues in pay TV and broadband separately. (See for example, Ofcom's Draft Statement on the Fixed Access Market Review: Approach to the VULA margin, 15 January 2015, e.g. paragraphs 7.60 to 7.62).

[265] Consultation Document, paragraph 6.49

any value on it at all (between 36% and 49% according to Ofcom's surveys[266])[267]. Moreover, even amongst those who have some level of interest in BT Sport, [✂].

4.22. In addition, BT notes Ofcom's comment that BT's share of supply "*is sensitive to whether or not we include revenues associated with the supply of BT Sport on Sky DSat and through the app and online player*".[268] As such, Ofcom appears to have included (and tested the sensitivities around) BT's revenues that are not derived directly from its pay TV platform. In contrast it does not appear that Ofcom has included equivalent additional retail revenues that Sky makes when selling its Sky Sports proposition outside its DSat platform. Specifically, it does not appear that Ofcom has included Sky's retail revenues (in aggregate or from Sky Sports sales) from NOW TV, Sky Go,[269] or Sky's self-retail revenues from Vodafone, despite the fact that these represent additional retail revenue streams which serve to strengthen Sky's market position further.[270] These additional revenues for Sky ought to be factored into Ofcom's calculation.

4.23. By addressing these methodological issues, BT's retail market share on a revenue basis would [✂]%.[271]

4.24. BT notes that Ofcom has also calculated revenue shares on the basis of all TV customers (i.e. not just those who subscribe to a premium sports channel). It is notable that even on this broader metric, Sky's retail market share remains at 60% to 80%. BT also believes that

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[266] Consultation Document, footnote 176. Namely: "*49% of BT Sport subscribers on Virgin Media … 36% of BT Sport subscribers on BT TV … and 45% of BT Sport subscribers on Sky DSat*".

[267] See also paragraphs 3.60 to 3.68.

[268] Consultation Document, paragraph 6.52.

[269] Sky has consistently highlighted the important role that Sky Go has played in its revenue and subscriber growth in recent years (Sources: (a) "Sky Go Extra helps profit jump 10%, Broadcast Now, 16 October 2014, available at: http://www.broadcastnow.co.uk/broadcasters/sky-go-extra-helps-profit-jump-10/5078701.article, and (b) Sky Q1 2014/15 press release of 30 September 2014, available at: https://corporate.sky.com/documents/investors/results/2015/q1-press-release.pdf)

[270] This is all the more inappropriate in light of Ofcom's proposed VULA margin regulation, where BT Sport is regarded as an acquisition and retention tool with respect to the associated broadband product. (Ofcom's Draft Statement on the Fixed Access Market Review: Approach to the VULA margin, 15 January 2015, e.g. paragraph 5.90). While BT has set out in detail in the course of the VULA consultation why Ofcom's approach of including BT Sport costs in the margin test is inappropriate, by also including revenues for BT broadband customers receiving BT Sport for free as pay TV revenues in this WMO review and simultaneously excluding revenues that Sky makes from NOW TV, Sky Go and Vodafone, it appears that BT is effectively punished on both fronts.

[271] Ofcom acknowledges at footnote 176 that: (a) 45% of BT Sport subscribers on Sky's DSat platform and taking BT broadband gave only non-sport reasons for taking BT Sport, and (b) 36% of BT Sport subscribers on BT TV also gave only non-sport reasons. Assuming that the percentage for app only subscribers is around [✂]%, would imply a reduction in BT's share of supply by around [✂]%, or a reduction of the [✂]% share of supply set out at Table 6.3 to [✂]%. Assuming even a modest increase in Sky's market share as a result of incorporating NOW TV customers would require BT's market share to be below [✂]%.

Ofcom's retail market share calculation in this case is likely to under-estimate Sky's share of revenue (and hence over-estimate BT's).

4.25. As observed by Ofcom there are difficulties with isolating TV-only revenues when TV channels are offered as part of wider bundles of communications services including voice and broadband services.[272] Ofcom described its methodology for doing so as follows:

> *"To estimate TV only revenues we subtract an estimate of the communication revenues for all customers that take pay TV from the total retail revenues provided by operators. This is based on the number of subscribers on different voice and broadband packages and the standalone price of the associated package, i.e. the price when broadband and voice is taken as part of a bundle excluding TV."*[273]

4.26. While this appears to be a reasonable approach for providers like BT and TalkTalk that offer pay TV only in combination with broadband and voice services (i.e. where there is no other choice to determine pay TV revenues on a stand-alone basis), there is no reason for using such an approach for operators such as Sky where a direct, stand-alone pay TV estimate is possible using pay TV prices at least for the non-triple-play portion of its subscribers. Ofcom's approach also ignores the fact that a subscriber's primary reason for subscribing to Sky is more likely to have been to access pay TV services,[274] but Ofcom's approach will under-estimate its importance and weight in the wider bundle thereby, again, under-estimating Sky's retail market share.

4.27. In any event, regardless of which measure is used by Ofcom to determine retail revenue, and retail market shares, it is clear that Sky's retail market share associated either (i) with premium sports subscribers or (ii) with all pay TV customers, is 60% to 80% and hence Sky continues to hold a strong retail market position with market shares at a level associated with dominance.

Method 2: Retail market shares using retail platform subscriber numbers

4.28. Whilst BT considers a revenue-based approach to be superior, it acknowledges that, total retail pay TV subscriber numbers provide a further, albeit crude, indicator of Sky's strong market position at the retail level.[275] Based on BT's own estimates, Sky's share of retail pay

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[272] Consultation Document, footnote 174.
[273] Consultation Document, footnote 174.
[274] See "Industry Panel – Creating a level playing field in competition in multi-play bundles" (WIK Conference on Bundling, 30-31 May 2011) Presentation by Wim De Rynck, page 2 "TV is the central component… TV turns 'a' bundle into a 'triple play' offer"
[275] In this case, BT notes that it would not be possible to undertake a similar analysis for sports subscriber numbers only, in light of the fact that "*so many BT Sport customers receive the channels for free means that*

TV subscribers as at February 2015 was approximately [✂]%, followed by Virgin Media with [✂]%, TalkTalk with [✂]% and BT with [✂]%.[276] Moreover, Sky's market share has remained high and persistent over time, notwithstanding new entry, and as detailed in Section 2, Sky has continued to grow its retail pay TV subscriber base in absolute terms. This strongly implies that Sky does not face an effective constraint from third parties.[277]

Method 3: Retail market shares including revenues associated with broadband and voice services

4.29. BT notes that Ofcom has also calculated retail revenue shares including revenues associated with broadband and voice services sold in bundles together with pay TV services, as a "*check of the sensitivity*"[278] of Ofcom's results based on TV only revenues. For the reasons set out above, BT does not believe that these numbers should be used in isolation to determine retail pay TV market shares, but accepts that they are instructive in terms of understanding the strength of Sky's position more broadly. In particular, it is notable that despite having a broadband market share of 23%,[279] Ofcom estimates that Sky's retail market share when TV, broadband and telephony revenues are included is in the region of 40% to 70%[280] i.e. above the market share level usually associated with a presumption of dominance. This underscores BT's concerns set out in Section 2 above that competition issues in pay TV markets are now spilling over into wider communication bundles.

BT's acquisition of the Champions League rights cannot be expected to materially alter Sky's retail market share

4.30. BT notes Ofcom's view that "*[o]verall, BT's acquisition of Champions League rights will mean that BT's retail revenues may increase*"[281], and that "*the acquisition of live Champions League content is likely to increase the number of subscribers who are unlikely to consider a platform that cannot offer BT Sport.*"[282] However, for the reasons set out in Section 2 above (at

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the number of subscribers to BT Sport is unlikely to be informative as to the number of subscribers who place a high value on the content shown on BT Sport" (Consultation Document, paragraph 6.15). [✂]

[276] BT Consumer, Competitor Insight Dashboard, issue 154, 19 February 2015, table Pay TV Market Stats.

[277] This is consistent with Ofcom's analysis in the Consultation Document which (correctly) notes that Virgin Media, TalkTalk and BT are all "*limited in some way*" as competitors to Sky. Consultation Document, paragraph 6.45.

[278] As intimated at paragraph 6.51 of the Consultation Document.

[279] As set out in Section 2, paragraph 2.3(ix).

[280] Depending on the assumptions made.

[281] Consultation Document, paragraph 6.53.

[282] Consultation Document, paragraph 6.27. BT notes that Ofcom expresses that the effect it has identified is "*uncertain*" and that the impact "*may be greater or smaller*". The lack of analysis underpinning this assessment and the extent of uncertainty around the impact means that the conclusion Ofcom has drawn is merely speculative. In light of the detailed evidence on the Champions League that BT has set out in Section 3, there will, in fact, be no impact at all.

paragraphs 2.11 to 2.25) regarding the strengthening of Sky's sports proposition overall, and for the reasons set out in Section 3 above regarding Ofcom's disproportionate focus on Champions League, ultimately, BT's acquisition of Champions League rights will not overcome the factors that sustain Sky's strong retail market share (on whatever basis it is calculated).

Sky has material incumbency advantages at the retail level

4.31. In the 2010 Pay TV Statement, Ofcom outlined various incumbency advantages that Sky enjoyed at the retail level. In the CC's Movies Investigation, the CC distilled Ofcom's analysis into three specific issues at the retail level, which Ofcom sets out in the Consultation Document.[283] However, other than setting out these advantages, and stating that Sky "*may enjoy a number of incumbency advantages at the retail level",* Ofcom does not set out its views on the specific advantages cited in any level of detail.[284]

4.32. In BT's view, it is manifestly the case that Sky's incumbency advantages at the retail level continue to persist to the present day and can be expected to persist (in light of the lack of significant developments in the pay TV sector, as outlined in Section 2 above and the importance of the Sky Sports proposition as outlined in Section 3 above). Moreover, all three of the barriers identified are relevant not just to a new entrant pay TV platform operator, but apply equally to existing smaller platforms that seek to compete with Sky. BT sets out its views on each of these retail incumbency advantages in turn below.

<u>High fixed costs with operating a pay TV platform</u>

4.33. The first retail incumbency advantage identified in Ofcom's Consultation Document is: "*the high fixed costs of setting up a pay TV platform. As new entrants face uncertainty about their future scale high fixed costs can act as a barrier to entry"*.[285] In the movies investigation, the CC elaborated on this point stating that this issue also encompassed platform developments, which would require the new entrant to "*subsidise the provision of receiving dishes and STBs as other entrants have done*".[286]

4.34. Sky's strong entrenched position at the retail level, combined with its incentive and ability to limit the distribution of its Sky Sports proposition (discussed further in Sections 5 and 6 below) give Sky an enduring advantage at the retail level. Other TV competitors, absent

[283] Consultation Document, paragraph 6.54.
[284] Ofcom merely notes that BT and TalkTalk "*still account for less than 15% of pay TV subscribers, and substantially less than that in terms of platform revenues*", and that "*switching remains low, and the time taken to acquire subscribers remains significant*". Consultation Document, paragraph 6.55.
[285] Consultation Document, paragraph 6.54(i).
[286] CC Movies Decision, paragraph 5.60.

access on fair and reasonable terms to the Sky Sports proposition, are unable to attract new subscribers that are interested in, and willing to pay for, premium sports channels. As a result of the limitations on the size of their addressable market, it is impossible for smaller competitors to reach the necessary scale to compete effectively in a market dominated by high fixed costs. This cements the smaller market shares of Sky's competitors.

4.35. The competition issues associated with high fixed costs are not merely limited to the costs of entry ex ante, but rather apply equally to an existing pay TV operator. Specifically, the high fixed costs associated with **operating and developing** a pay TV platform also means that Sky derives substantial advantages from its relative scale at the retail level, merely by being better able to recover its fixed costs on a considerably lower per subscriber basis, allowing it to either derive a higher margin or offer lower priced, more compelling offers to attract (even more) retail subscribers.

4.36. There is no doubt that there are many areas where Sky's scale will assist it in benefitting from a lower per unit cost than other pay TV operators as a result of its relative scale, such as:

(i) Sky can better spread the fixed costs of sports rights acquisitions and MRGs for other content. In addition, it is also likely to have lower variable costs for programming costs given Sky's advantageous arrangements with many channel suppliers as a result of its strong bargaining power given the strength of its platform;

(ii) Its per unit costs of content production are likely to be lower than other operators as its greater scale in content production allows it to better spread the costs of studios, pundits' salaries, etc and it will also enjoy lower content encoding costs. Again its variable costs are also likely to be lower due to its long-standing relationships with set-top box manufacturers and greater bargaining power; and

(iii) Moreover, Sky acquired Amstrad in 2007, allowing it to bring set top box production in-house. Over the last couple of years, Sky is reported to have been in the process of developing its next generation of STB itself,[287] taking advantage of its vertical integration in STB production. Moreover, as Sky develops its STBs for Sky UK, Sky Italia and Sky Deutschland, Sky will be in a position to recoup its STB development and investment costs across five countries (UK, Republic of Ireland, Italy, Germany and Austria), providing further scale advantages.

[287] http://invezz.com/news/equities/10581-bskyb-share-price-satellite-broadcaster-prepares-set-top-box-revamp

4.37. The combination of these factors creates a very material incumbency advantage for Sky directly resulting from its scale at the retail level.

4.38. Moreover, merely as a result of its relative scale, Sky is also better placed than its rivals to pay significantly more for content.[288] While Sky may pay more in absolute terms for a given piece of content, due to its scale, ultimately it will pay less on a per subscriber basis. This point was illustrated recently in the outcome of the 2015 Premier League, where it was noted by the FT that Sky could absorb over £130m of estimated over-expenditure per annum (above rights inflation that had already been factored in by analysts) by increasing the cost of its pay TV channel subscriptions by £1 per month. In comparison, with BT's pay TV retail subscriber base at less than a tenth of Sky's, BT would need to increase its prices by £[✂] per month to raise a comparable amount of revenue from its retail subscriber base.[289] Furthermore, this advantage is not merely limited to Sky's strength as a result of its Sky Sports proposition, but is reinforced by its relative scale in the provision of movies and basics too. Therefore, in terms of appealing to a household with differentiated preferences, Sky's relative scale allows it to strengthen its offering as a whole relative to its rivals, and better recoup the costs associated with doing so.

4.39. Sky's relative scale also means it is easier to recoup material fixed cost investments in the development of its technological infrastructure, including investment in better set top boxes and associated subscriber hardware and software. Sky has made a number of such investments in recent years, including:

(i) Material investment in **HD**. BT believes there is a strong correlation with sports subscribers and a willingness (and ability in light of higher ARPU) to pay for higher picture quality. Sky's scale with respect to premium sports subscribers has assisted it in underpinning a substantial investment in HD, which in turn has then facilitated its wider roll-out of HD across other genres. Indeed, in 2014 alone, Sky spent in the region of £70m[290] to increase the roll out of Sky+ HD STBs. By the end of 2014, 5.7 million customers had Sky+ HD STBs. This offering has led to more customers

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[288] BT's discusses Sky's bidding advantages in greater detail at paragraphs 4.49 to 4.89below.

[289] http://www.ft.com/cms/s/0/6e8d4f24-b167-11e4-a830-00144feab7de.html. The report notes Sky's stated aim to make £200m of cost savings in relation to its expenditure of "*around £330m more than analysts' forecasts*". The article continues, "*The company could recoup the remainder of its unanticipated spending [£130m] by increasing prices for its 11.8m retail customers by £1 a month. Alternatively, it could pass the cost on only to its 5m Sky Sports customers, or to the pubs and clubs that show its games*".

[290] http://www.telegraph.co.uk/finance/newsbysector/mediatechnologyandtelecoms/media/10789883/BSkyB-plans-major-overhaul-of-set-top-box-to-meet-Apple-threat.html

upgrading to HD and has seen "*the number of On Demand downloads more than [treble] to 257 million in the quarter*".[291]

(ii) In July 2011, Sky Player and Sky Mobile TV services were merged and rebranded as **Sky Go,** enabling subscribers to watch live channels in addition to their Sky TV subscription at no additional charge. An app for use on the iPhone was made available in July 2011, offering subscribers an optimised viewing experience on Apple iPhone and iPad devices.

(iii) More recently, in January 2014, Sky invested in and **relaunched its EPG** and expanded the number of channels made available on Sky Go. Sky's 2014 Annual Report explained: "*[o]ur new EPG is helping customers to get even more from their subscription*". It is noted on page 19 that: "*… there's more to come. Our next software update, later this year will enable us to dynamically change the home page to do things like promoting the launch of a new show or film. For the first time, we'll also be able to make recommendations on programmes that customers might like to watch based on what they are choosing to record on their planner*".[292]

(iv) Sky launched the **Now TV** internet service in July 2012 providing access to Sky Sports and, subsequently to Sky Movies and Sky Entertainment packs, available from internet-connect devices.[293] According to its 2014 annual report, NOW TV gives Sky "*the chance to unlock new pockets of demand in an emerging pay light sector and extend [Sky's] reach in Freeview homes – many of whom are looking for an easy and flexible way to enjoy a better TV experience*."[294] NOW TV has required significant upfront investment in the NOW TV box.[295]

(v) It has been reported that in 2015, Sky is planning to launch its next generation of set-top box which may include **4K or Ultra HD (UHD)** picture capability. As set out above with respect to HD, there is a strong correlation with sports subscribers and a willingness to pay for higher picture quality. As such, BT is unsurprised that following 4K trials carried out in 2013 and 2014, Sky concluded that "*live sport in UHD has real potential*".[296] Originally the STB was expected to launch in 2016, but BT understands that Sky has decided to accelerate its launch in order to maintain its reputation as

[291] https://corporate.sky.com/documents/investors/results/2015/q1-press-release.pdf
[292] Page 19. See also the following press release: https://corporate.sky.com/media-centre/our-blog/2014/a-new-look-for-skys-epg-as-on-demand-viewing-continues-to-rise.
[293] https://corporate.sky.com/media-centre/our-blog/2012/nows-the-time-for-now-tv
[294] https://corporate.sky.com/documents/annual-report-2014/annual-report-2014.pdf (page 9)
[295] http://www.digitaltveurope.net/83172/sky-launches-roku-based-now-tv-box/
[296] http://www.telegraph.co.uk/finance/newsbysector/mediatechnologyandtelecoms/media/11381115/Sky-accelerates-new-set-top-box-launch.html

the leader in technology – and go to market with a 4k offering ahead of its rivals.[297] In terms of investment, Sky is estimated to be spending up to £3.2 billion to improve its STB and convert to UHD. According to Berenberg Bank, this investment should achieve major efficiencies in Sky's satellite bandwidth costs of around £50 million annually in operating costs.[298]

(vi) BT also understands that Sky's new set-top box will incorporate improved streaming functionality for **OTT TV services**, for example from Amazon, Apple and Google, and will include a new system to make access to programmes on any device easier for customers. It has been reported that the new technology will include a central data centre where recorded television can be stored that would be accessible from smartphones and tablets; and will allow customers to pause recorded and on-demand video content on their main TV set and then continue watching from where they left off on another device, and vice versa. This multi-screen technology will reportedly also extend the reach of BSkyB's targeted advertising system AdSmart, which utilises the Sky set-top box to show tailored commercials to specific customers.[299]

4.40. In addition to these specific investments, Sky's Brand Director of TV Products, Luke Bradley-Jones confirmed that Sky *"...invest[s] pretty substantially in [its] broadcast platform every year".*[300] Sky is able to maintain high levels of investment and make these specific hardware and software investments with the benefit of its large existing subscriber base to underpin its investments. However, once Sky undertakes these investments, a rival pay TV retailer, despite its much smaller scale, is required to follow suit or risk its relative retail market share falling further behind (as discussed in more detail in Section 5 below).

<u>The high cost of acquiring new subscribers</u>

4.41. The second retail incumbency advantage identified in Ofcom's Consultation Document is "*the high cost of acquiring new subscribers. A new entrant would incur significant marketing costs in order to acquire new customers and for those that do switch the entrant would incur further costs providing new equipment. The incumbent operator already has an existing subscriber base and so does not have to incur marketing and only needs incur the costs of*

[297] https://corporate.sky.com/media-centre/our-blog/2013/sky-broadcasts-the-uks-first-live-event-in-ultra-hd
[298] http://advanced-television.com/2013/12/13/bskybs-ultra-hd-conversion-could-cost-3-2bn/
[299] http://www.telegraph.co.uk/finance/newsbysector/mediatechnologyandtelecoms/media/10789883/BSkyB-plans-major-overhaul-of-set-top-box-to-meet-Apple-threat.html
[300] www.stuff.tv/sky/project-ethan-revamp-will-transform-sky-s-set-top-box-service/news

maintaining existing equipment and infrastructure for these customers".[301] This barrier remains in place, and as such continues to confer a substantial benefit on Sky.

4.42. As Ofcom identified in its 2013 Consumer Experience Report, the levels of switching in digital TV generally are exceptionally low, with only 3% of non-pay TV consumers switching digital TV provider. This suggests that persuading non-pay TV households to switch to a pay TV service is likely to be extremely challenging.[302] Moreover, in 2013, only 4% of consumers with a pay TV service switched their main TV provider, as compared to around one in ten in each of the fixed-line (9%), mobile (11%) and fixed broadband (9%) markets. In addition, as set out in Section 2 above, Sky's churn rate remains extremely low. Given these low levels of switching it is extremely difficult for a small, existing pay TV retailer to attract customers away from Sky.

4.43. As discussed at paragraph 3.16(iv) Ofcom's October 2014 research assessed a hypothetical scenario in which BT was able to show the same number (or a greater number) of Premier League games than Sky per week. It found that even if the number of Premier League games on BT Sport doubled, and the number of games on Sky Sports halved, the majority of subscribers who currently have Sky Sports but not BT Sport would not change their subscription (54%). In fact only 16% of respondents said they would switch to taking both BT Sport and Sky Sports and only 3% would switch to BT Sport only.[303] In fact, even if BT Sport could show the majority of Premier League games, 49% of Sky Sports-only subscribers would continue to remain Sky Sports only subscribers, whilst only 17% would additionally acquire BT Sport and 9% would switch to BT Sport only.[304]

4.44. Furthermore, due to asymmetries in industry regulation around how companies can contact switching customers once they are out of contract, Sky is more likely to be able to retain its subscribers than BT. As Ofcom is aware, there are regulations inhibiting when companies are able to contact customers who wish to switch their voice and broadband services. No such rules apply to pay TV customers. As a result, Sky is afforded a greater ability to 'save' a

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[301] Consultation Document, paragraph 6.54(ii).

[302] This is most likely due to the market slowing down as it trends towards market saturation.

[303] "Q*24 (prompted) Currently Sky Sports shows about 3 live Premier League games per week, and BT Sport shows about 1 live Premier League game per week. If this changed to a scenario where both Sky Sports and BT Sport each showed 2live Premier League games per week, but everything else stayed the same, what sports channels would you get?* (Table 41, 2014 research)

[304] "*Q.26 (prompted) Currently Sky Sports shows about 3 Premier League games per week, and BT Sport shows about 1 Premier League game per week. If this changed to a scenario where Sky Sports showed 1 Premier League game per week and BT Sport showed 3 Premier League games per week, but everything else stayed the same, what sports channels would you get?*" (Table 51, 2014 research)

retail pay TV customer who is considering switching than BT,[305] including aggressive consumer retention offers.[306]

4.45. Moreover, Sky's scale also means that its available marketing budget dwarfs that of other pay TV retailers. As Ofcom is aware, even in 2010, Sky's marketing budget was approximately £1 billion, and this has now risen to 1.2billion.[307] As the largest marketing spender in the UK[308], Sky benefits from scale advantages in terms of its bargaining power with other media owners which further reinforces the benefits it derives from the relative scale of its budget.[309] The sheer scale of Sky's marketing budget increases the acquisition

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[305] Triple play customers wishing to leave BT for Sky inform Sky who applies a standardised, regulated industry processes to terminate the customer's voice and broadband services. (General Condition 22). As a broadband line is required to provide BT's TV services, terminating the broadband service automatically terminates all pay TV services from BT, and BT is prohibited from contacting the switching customer about potentially staying with BT. On the other hand if a Sky triple play customer wishes to switch to BT, only their voice and broadband services are automatically terminated, and the customer is required to contact Sky directly to cancel their TV service. This enables Sky to make a 'save' offer to retain the customer not just for its pay TV services, but for all three services.

[306] This issue is the subject of a series of reports in The Telegraph last year. Two articles published on 4 and 7 January 2014 identified widespread instances of Sky seeking to make it very difficult for a customer to cancel their contract other than by phone, and, when a customer did seek to cancel by phone they were offered substantial discounts in order to prevent them leaving. On 4 January 2014, *The Telegraph's* personal finance team reported on Sky's aggressive approach, for example: *"Neil Bottrill… tried to cancel his Sky package in June when moving home. He wrote on June 4 requesting cancellation of his contract.* ***Sky replied saying he would have to call. He wrote again, explaining that he would answer any security questions by letter. Sky again replied insisting that he ring. Then he noticed that his Sky package had been switched off, so he assumed it was cancelled. However, in August Sky sent him a bill for £47.14 and threatened to send debt collectors. Eventually Sky refunded him the money.*** *(*http://www.telegraph.co.uk/finance/personalfinance/money-saving-tips/10549570/Problems-with-cancelling-Sky-TV.html).
On 7 January 2014, a follow-up article was published by The Telegraph noting that: "*Unhappy Sky customers have inundated The Telegraph with personal experiences that appear to corroborate allegations that the television, phone and internet provider makes it difficult to leave at the end of a contract."* In particular it was noted that "*many readers had encountered difficulty in cancelling in writing or by email, despite Sky's terms and conditions suggesting this is allowed*". (http://www.telegraph.co.uk/finance/personalfinance/money-saving-tips/10555611/Sky-subscriptions-why-is-it-so-hard-to-cancel.html). Several months later, an article was written on 25 May 2014 confirming that Sky had amended the wording in its terms and conditions to preclude written terminations, thereby requiring customers to cancel their contract only by phone (http://www.telegraph.co.uk/finance/personalfinance/household-bills/10851095/Sky-agrees-to-make-it-clear-for-customers-on-how-to-cancel.html.)

[307] 2014 Annual Report, page 39, https://corporate.sky.com/documents/annual-report-2014/annual-report-2014

[308] "*Top 100 UK advertisers: BSkyB increases lead as P&G, BT and Unilever reduce adspend*", 11 April 2014: http://www.marketingmagazine.co.uk/article/1289560/top-100-uk-advertisers-bskyb-increases-lead-p-g-bt-unilever-reduce-adspend.

[309] Sky's scale also allows it to benefit as a seller of advertising as well, as Sky is the only option for advertisers seeking to deliver targeted ABC1 male impacts at scale. This means that rivals who are trying to attract premium sports subscribers need to acquire advertising from Sky. However, BT's experience has been that Sky will not carry advertisements for BT Sport on Sky Sports, thereby making it nearly impossible to target the BT Sport primary target market. For example, as Ofcom is aware, on 10 January 2013, Sky refused to grant

costs Sky's smaller rivals face in order to (a) gain recognition for their pay TV services, such that a consumer would even contemplate switching from Sky, and (b) actually convincing a Sky customer to switch. Their ability to compete is further undermined by Sky's ability to cross-promote its Sky Sports proposition (outside of regulated advertising time), which a competitor cannot do.[310] Clearly this problem is further exacerbated when Sky's rivals are unable to offer the full Sky Sports proposition that is necessary to attract a large portion of retail pay TV subscribers.

4.46. Ofcom suggests in the Consultation Document that entrants with an existing subscriber base in an adjacent industry such as broadband or mobile may face lower costs of acquiring new customers than a new entrant offering pay TV on a standalone basis. It is not clear why Ofcom has reached this speculative conclusion. To the extent those subscribers had an interest in, and willingness to pay for, TV services, then the likelihood is they would already be taking a pay TV service. If they were not, then persuading subscribers to take services in an adjacent market, who have already demonstrated by their actions that they have limited interest in, or willingness to pay for, pay TV services to subscribe to a pay TV service remains difficult. Moreover, as noted in Section 2 above, due to the stringent regulation at the wholesale level of broadband and telephony inputs, Sky has been in a position to offer triple-play products for many years. Thus, to the extent that subscribers had an interest in, and willingness to pay for, a triple-play bundle encompassing the full Sky Sports proposition, Sky (or Virgin Media) has been in a position to attract them already over the last number of years.[311] As such, the same barriers exist today, even where an existing operator has a subscriber base in an adjacent market.

<u>The likelihood of a competitive response by Sky</u>

4.47. The third retail incumbency advantage identified in Ofcom's Consultation Document is "*the likelihood of a competitive response by existing platforms. An entrant may expect incumbents to respond by strengthening their offering and by seeking to retain their existing subscribers (i.e. a normal competitive response). Anticipation of such a competitive response could deter entry or expansion*"[312]. Sky's relative size in the pay TV market enables it to defend its position robustly against any attempt by its competitors to attract customers away from Sky. This has been amply demonstrated over recent years through Sky's

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advertising space to a BT Sport campaign on its Sky Sports channels, as this was the subject of an undue discrimination case.

[310] BT also notes that Sky may benefit from the fact that on the largest platform with the highest concentration of premium sports subscribers, Sky Sports occupies the first page of the EPG.

[311] Indeed, as the evidence set out in paragraph 2.3 shows Sky has been doing just this in practice.

[312] Consultation Document, paragraph 6.54(iii).

aggressive marketing campaigns and reconfiguration of its Sky Sports proposition in response to rivals' attempts to compete:

(i) When BT Vision launched its Sky Sports 1 and 2 offering in July 2010, Nielsen figures for the period showed that Sky's UK marketing expenditure specifically in relation to Sky Sports increased dramatically in July to August 2010 compared with the same period in 2009 i.e. the period directly following BT (and Top-Up TV's) entry. The Nielsen figures show that Sky's July marketing spend in relation to Sky Sports increased by 374% and its August spend by 90%.[313]

(ii) Further, in 2010 Sky confirmed that for the quarter ending 30 September 2010 it spent £58 million more on marketing the Sky brands in the UK as a whole, compared to the same quarter in 2009.[314] Sky stated that this reflected "*increased investment in successful marketing campaigns in home communications and Sky Sports ahead of the Premier League season, both of which delivered record performance in the quarter*".

(iii) BT has previously described at paragraph 3.48 the nature of the half pizza and half football adverts that Sky ran at the time in order to draw attention to the limited proposition that BT could offer relative to Sky's own retail offering.

(iv) In light of Sky's historic spoiling tactics[✂]. Over the period May to September 2013, based on Nielsen data, Sky's marketing expenditure on Sky Sports increased by 100% as compared with the previous year.[315]

(v) BT has previously set out in Section 3 above its view that the creation and channel-specific marketing of SS5 was: (i) a direct response to BT's acquisition of Champions League rights, and was intended to maximise Sky's value in this content by linking the channel's launch to a minimum one-year broadband contract, which was free for two years as long as the customer kept the Sky Sports pack, with a view to locking in subscribers who were out of contract [✂]; and (ii) to assist Sky in migrating sports content away from its regulated channels onto unregulated channels that it was not required to wholesale to rivals.

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[313] Figures from Nielsen Ad Dynamix.

[314] See Sky's results for Q1 2010/11, published on 30 September 2010, page 9.

[315] BT notes that although Sky's marketing expenditure doubled in response to the launch of BT Sport, the increase in Sky's marketing expenditure was not of the same magnitude (400% increase) as Sky's response when BT was first afforded the opportunity in 2010 to retail Sky Sports 1 and 2 following the WMO intervention. As such, it is clear that Sky perceives the retailing of even a sub-set of its Sky Sports proposition as a greater competitive threat than BT Sport.

Sky has material advantages when bidding for live sports rights

4.48. BT agrees with Ofcom's finding that Sky continues to have a significant advantage when bidding for sports rights. Indeed, for the reasons set out below, Ofcom's tentative finding that *"Sky appears to have a significant advantage"*[316] underplays the strength of the available evidence that clearly supports a conclusive finding of Sky's enduring and material bidding advantages.

4.49. In particular, below BT explains that:

(i) First, as identified in 2010, Sky's bidding advantages perpetuate a 'vicious circle': Sky's systematic ability to win perishable sports rights at the upstream level, combined with the limited wholesale distribution of its Sky Sports proposition, bolsters its position at the wholesale and retail levels, further entrenching its strong market position across the value chain. The outcome of past Premier League auctions clearly demonstrate the vicious circle in action.(paragraph 4.51 to 4.57) and the outcome of the 2015 auction amply demonstrates Sky's unassailable advantage in this regard;

(ii) Second, the vicious circle is not limited to high value rights such as Premier League rights, but rather Sky's systematic advantages in bidding for rights applies to all live sports rights. (paragraph 4.58 to 4.66);

(iii) Third, BT's ability to monetise its investment in sports rights indirectly by providing BT Sport for free to its broadband subscribers does not overcome Sky's bidding advantages encapsulated in the vicious circle. This is particularly true since Sky also has the option to monetise its sports rights investments indirectly, and bundles its pay TV offering with its broadband services. (paragraph 4.67 to 4.83); and

(iv) Finally, BT explains why the outcome of the 2013 Champions League auction does not provide evidence that Sky's bidding advantages have been eroded, due to the exceptional circumstances of that auction (paragraphs 4.84 to 4.89).

<u>The bidding advantages that Ofcom identified in 2010 still remain today: Sky's incumbency advantages arise from enduring high barriers to entry absent regulation</u>

4.50. In 2010, Ofcom identified a number of factors that led to Sky's incumbency advantages when bidding for premium sports rights. These included "*the time it takes to build a subscriber base, the advantage of being vertically integrated with the largest platform*

[316] "*Sky appears to have a significant advantage when bidding for sports rights*" paragraphs 6.36 to 6.40 of the Consultation Document.

operator and thereby able to bundle key sports channels with other pay TV services and some bidder specific advantages."[317]

4.51. In 2010, BT agreed with Ofcom's analysis, and in the course of the Pay TV Appeals commissioned Compass Lexecon to produce an economic model which demonstrated precisely why Sky would be able systematically to outbid rivals as a result of its incumbency advantages.[318] This economic model proved BT's submissions that:

(i) Sky's existing, large installed retail pay TV subscriber base with an established, substantial, willingness to pay for its premium sports channels affords it a structural advantage in bidding for live sports rights.[319, 320]

(ii) In contrast to Sky, any rival bidder seeking to acquire sports rights faces a "time to build" problem. Even if it were to win an individual set of sports rights, and even assuming those individual rights in themselves were sufficient to induce switching, it would take time to build its own base of subscribers who are willing to pay for this premium sports content to the same level as Sky's pre-existing base.

(iii) Thus, at the outset of any rights auction, Sky will always be in a position to extract more value from a given set of rights than a rival bidder over the short lifespan of those rights: from day 1 Sky will be able to extract retail revenues from the totality of its Sky Sports subscriber base over the entire rights period, whereas a rival requires time to build its base of subscribers who are willing to pay for this premium sports content and so will never be able to recoup as much as Sky.[321]

(iv) Equally, as discussed at paragraphs 4.33 to 4.40 above, given Sky's existing scale it will be better placed to spread a higher absolute rights cost across its base than a

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317 Consultation Document, paragraph 6.36.2 and Pay TV statement, paragraph 5.474.

318 Compass Lexecon, *Modelling static and dynamic competition in the retail market*, revised version 30 April 2014, provided by BT to Ofcom in response to the WMO Information Request in November 2014.

319 While not as important as Sky's installed retail subscriber base, the scale of Sky's wholesale subscriber base with a large willingness to pay for the Sky Sports proposition can also reinforce this effect. In addition, for the reasons discussed in Section 7 of this submission, Sky's revenue from its commercial subscribers also reinforces this effect.

320 These findings apply irrespective of whether the sports subscribers are stand-alone pay TV subscribers with a willingness to pay for premium sports channels, or triple-play subscribers with a willingness to pay for premium sports channels, or acquired their pay TV services in some other form of bundle (e.g. dual play). This is due to the fact that, in light of the stringent regulation of wholesale inputs, the incremental costs of telephony and broadband wholesale inputs are uniform since Sky has regulated access to BT's infrastructure and, therefore, it can replicate BT's offerings at the same or very similar incremental costs. As such, the primary differentiating factor is access to wholesale content.

321 This is implicitly recognised in Ofcom's VULA investigation as Ofcom accepts that where revenues grow over the VULA review period, it is appropriate to use the level of revenues at the end of the period rather than the average revenues in the margin assessment (Ofcom's Draft Statement on the Fixed Access Market Review: Approach to the VULA margin, 15 January 2015, e.g. paragraph 6.311 to 6.313).

rival bidder of a smaller scale. Sky also enjoys a range of bidder-specific advantages, including branding advantages, and lower risk and relationship advantages as a result of being the incumbent winner in sports rights auctions over many years.[322]

(v) Consequently Sky will systematically, and on average prevail in acquiring and renewing sports rights. This does not mean that it is impossible for a rival to win sports rights in specific circumstances, but rather that if Sky is also vying for those rights, a rival will only be able to outbid Sky in exceptional circumstances, in particular:

(a) If the rival believes (rightly or wrongly) that it will be able to extract more value for the rights in aggregate than Sky believes it is possible to achieve, notwithstanding the relative scale of Sky's subscriber base; or

(b) Sky makes an error in judging the rival's valuation of the rights, and the auction structure punishes Sky for misjudging the rival's willingness to pay.

(vi) Moreover, a rival bidder cannot build its customer base slowly in the hope of matching or leapfrogging Sky in the distant future because, unlike the investments made in other industries, live sports rights are "perishable" i.e. the winner of a sports rights auction only has a limited, fixed, period over which to monetise the rights won (typically three years), before they are re-sold again. Thus, in order to slowly build a base, a rival would need to have certainty that it would be capable of outbidding Sky in multiple auctions over time, which, given Sky's bidding advantages it simply cannot assume would be the case.[323]

4.52. It is clear why BT refers to Sky's bidding advantages as a 'vicious circle': by limiting the distribution of its Sky Sports proposition (either by not providing access at all, or by providing access only on terms that do not permit effective competition), Sky is able to prevent other pay TV operators from growing their own premium sports subscriber base with an established, positive, willingness to pay for premium sports channels over time, thereby limiting their ability to challenge for live sports rights in the future. In turn, Sky continues to prevail in acquiring live sports rights, bolstering its position at the wholesale and retail levels, allowing it to maintain and grow its subscriber base, which in turn enables it to continue to bid successfully in upstream content auctions in the future, entrenching its position across the pay TV value chain. Given Sky's bidding advantages it will also be better

[322] See footnote 238above, on page 91.

[323] Of course, to the extent that subscribers are willing to switch from Sky to a rival as a result of the rival's acquisition of a given set of rights, once the rival loses those rights, the subscriber can be expected to switch back to Sky.

placed to strengthen its Sky Sports proposition over time (as evidenced by the data BT has provided in Section 2 of this response), and maintain that position in the future.

4.53. As a result of the self-reinforcing nature of the vicious circle, it can only be unwound with targeted regulation at the wholesale level: by addressing Sky's limited distribution of its Sky Sports proposition (both in terms of access to the full Sky Sports proposition and on terms that permit fair and effective competition), pay TV operators will be able to grow their own premium sports subscriber base with an established, positive, willingness to pay for premium sports channels over time, and potentially become a challenger for key sports rights in the future.

4.54. As the evidence set out in Section 2 above demonstrates, the key elements underpinning Sky's structural advantages when bidding for rights remain in effect today:[324]

(i) Sky has retained a large installed subscriber base of premium sports subscribers with a high willingness to pay for its Sky Sports proposition, as explained at paragraphs 2.2 to 2.3 above. This is further supported by the evidence above at paragraphs 4.16 to 4.29 on retail market shares.

(ii) There are still issues with the limited distribution of the Sky Sports proposition, as explained at paragraphs 2.49 to 2.56.

(iii) Sky has further strengthened its rights position since Ofcom undertook its analysis in 2010, as explained at paragraphs 2.11 to 2.25.

The outcome of Premier League rights auctions clearly demonstrate Sky's bidding advantages

4.55. Moreover, as Ofcom recognises,[325] the outcome of recent Premier League auctions clearly demonstrates Sky's bidding advantages: the amount that Sky is capable of committing in order to ensure it retains the maximum rights allowed is far in excess of the sum that a rival with a materially smaller subscriber base would be capable of bidding for these rights:

(i) First, as Ofcom notes, other than in one instance, Sky has always secured the maximum number of Premier League games that it is permitted to hold, as well as the most attractive pack containing preferential first picks and the best broadcast slots.

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[324] BT also notes that Ofcom's plans to introduce ex ante regulation which will constrain the amount Sky's main rival when bidding for rights can pay for sports rights has, itself, created further barriers that strengthen Sky's bidding advantages. (Ofcom's Draft Statement on the Fixed Access Market Reviews: Approach to the VULA margin, 15 January 2015)

[325] Consultation Document, paragraph 6.36.1.

(ii) Second, evidence from the 2012 Premier League auction is particularly instructive. As Ofcom is aware, [✂] However, [✂] into the 2012 Auction Sky was still able to secure the maximum number of games that it was permitted to acquire. In order to do so, Sky was in a position to increase its bid by £660 million from £1.62 billion in 2009, to £2.28 billion in 2012.

(iii) Finally, evidence from the most recent 2015 Premier League Auction underscores the extent of Sky's bidding power. In order to guarantee it the maximum number of Premier League matches including those packages with the most attractive matches, Sky was in a position to increase its bid by almost £1.9 billion from its 2012 bid, to £4.186 billion. It increased its bid by 83% in order to ensure that it maintained its Premier League leadership. The sums that Sky is willing and able to bid give a clear indication not only of Sky's bidding advantages, but also of the difficulty rival broadcasters such as BT face in challenging Sky for the acquisition of rights.

4.56. It is clear that the WMO Remedy has had no impact on limiting Sky's ability to outbid competitors.

The vicious circle is not limited to high value sports rights such as Premier League

4.57. For the reasons set out in detail in Section 3 above, the focus of Ofcom's analysis to ensure fair and effective competition should be on channels and packages of channels, rather than on individual sporting events. In order to build a premium sports channel that is attractive to subscribers, and is capable of competing with Sky, it is necessary to amass a wide range of content.[326] A premium sports channel cannot be built around Premier League rights alone.[327]

4.58. Therefore, being able to win a range of second-tier rights is also important in order to build a sports channel or package of channels. However, Sky's bidding advantages are not limited to rights with values at the level of Premier League rights. In fact, Sky also has a systematic advantage in acquiring second-tier rights of a much lower value:

(i) Sky's primary bidding advantages stem from its large installed pay TV subscriber base with an established, substantial, willingness to pay for its premium sports

[326] As Ofcom has previously recognised itself "*[t]he aggregation of attractive content by broadcasters is essential in order to create channels which viewers wish to watch*." (Pay TV Statement, paragraph 4.79). See also Pay TV Statement paragraph 5.19: "*[w]e considered that Sky's market power was based on the aggregation of rights to specific sporting competitions by sporting bodies such as the Premier League, and the further aggregation by Sky of the rights to different competitions*"

[327] BT also notes that a "mixed genres" channel is also unlikely to be a profit maximising strategy as evidenced by the fact that no successful bidder for major sports rights has attempted to monetise the rights in this way.

channels. In contrast, a rival bidder[328] (such as BT) faces a time to build problem, since it does not have a large installed retail pay TV subscriber base with an established, substantial, willingness to pay for premium sports channels. Thus, Sky will always be in a position to extract more value from a given set of rights than a rival bidder over the short lifespan of those rights.

(ii) Once this primary advantage is accepted, it is clear that this advantage exists regardless of the absolute value of the rights: since Sky already has the vast majority of subscribers with a high willingness to pay for a wide range of individual sports (golf, rugby, cricket, tennis, F1), a rival bidder equally faces a 'time to build' problem in terms of persuading subscribers who are willing to pay for those sports to switch from Sky. Therefore, Sky will always be in a position to extract relatively more value from a given set of rights than a rival bidder, regardless of the absolute value ultimately paid for those rights.

(iii) Consequently, absent an effective WMO Remedy, Sky will systematically and on average prevail in acquiring these rights where it goes up against a rival bidder:[329] since Sky is better placed to monetise the given set of sports rights, its maximum value will always be higher, and therefore a rival who bids more than Sky in order to secure the rights would not be expected to recoup the value of its bid.

4.59. In many respects, Sky's incumbency advantages in terms of the vicious circle may be even stronger when it comes to bidding for second-tier rights, given the way in which such rights are frequently sold. In the case of the majority Premier League rights, these represent coverage of the most attractive football tournament in the UK, and provide a large volume of rights spread over the course of a year. In contrast, in terms of many second-tier rights, there is frequently not a single set of rights that is perceived as being the most important tournament. In fact, there are multiple events within the sport, all of which may be perceived as similarly important, and the rights for each of these events are sold separately. This reinforces Sky's incumbency advantages. To take the example of golf:

(i) The Major championships consist of four different annual tournaments (the US Masters Tournament, the US Open, The British Open Championship and the US PGA Championship), but the rights to these events are all sold separately, and Sky currently has all four (with the US Masters shared with the BBC for the final two

[328] BT uses the word "bidder" loosely here to refer to those who are interested in acquiring a given set of rights. For many sets of rights there will not be an open tender for those rights, but rather deals will be done as part of bilateral commercial negotiations. However, the same underlying principles discussed here apply.
[329] It is important to note that given Sky's extensive range of second-tier sports rights, it does not always choose to bid for all second-tier rights.

rounds). In addition, there are the two main regular golf tours, the European Tour and the US PGA Tour, which involve weekly tournaments scheduled over the course of the year, culminating in end of season competitions. The Ryder Cup is a further significant competition, played between the US and Europe bi-annually. Sky hold rights to all of these tournaments, which are all sold separately.

(ii) In the case of the Majors and the Ryder Cup, each of these golf tournaments only lasts for a number of days, or at best one week, per year. It would not be possible to build a sports channel proposition around a single such event: golf fans would be unlikely to find a single one week tournament sufficiently attractive to switch subscription, relative to the offering available from Sky. In the case of the longer duration US PGA Tour and European Tour, Sky has renewed these rights until 2019 and 2022 respectively.

(iii) The key problem is that the rights to each golfing event are rarely sold at the same time and the sales of the individual rights are often staggered over a number of years. This means that Sky, with its portfolio of golf rights, can fit each individual golf right into its existing portfolio and monetise it immediately, as it already has the relevant premium sports subscribers with a willingness to pay for golf. In contrast, a rival starts with no subscribers with a proven willingness to pay for golf, as it is reasonable to expect that golf fans with a high willingness to pay will already subscribe to Sky Sports, and acquiring one golfing event (whether a high profile short event such as the British Open, or a longer duration event such as the US PGA Tour) will be insufficient to persuade many of those subscribers to switch to BT Sport.

(iv) Therefore, for a rival bidder, the potential revenues from buying such rights are lower than for Sky, and the risk it takes in bidding for them is higher. As a consequence Sky will rationally be able to bid more for each individual right as it becomes available.[330]

(v) In practice, what this frequently means is that a rival bidder is simply not incentivised to try to bid for an individual sports right, particularly those of shorter duration. For example[✂]

[330] While this aggregation value can be demonstrated most clearly when the rights are all related to the same sport, the same principle applies also across different sporting events for the “long tail” of individual sports rights with comparatively low individual valuations. Despite their individually low valuations, in aggregate 29% of subscribers consider these to be important.

(vi) Moreover, Sky's aggregation of sporting events also hedges its risk; even if it loses rights to one particular event to a rival, the majority of fans of the relevant sport (or in fact, sports fans in general) will not switch if it retains enough of the rights to that sport for the majority of subscribers. Therefore, Sky is in a more stable and secure position from which to bid on rights, whereas its rivals must take on considerable risk.[331]

4.60. Therefore, despite the lower amounts involved when bidding for second-tier rights, Sky's advantages, and the vicious circle arise with each of these just the same. As a result of these issues, Sky will systematically and on average be able to outbid rivals to secure these rights.[332]

4.61. It is also notable that for second-tier rights there are frequently a number of intangible factors that further reinforce the vicious circle. For example, it is frequently the case that no open auction tender process is held. [✂],[333][✂],[334][✂].[335] [✂]. Recent examples of these intangible factors in action include:

(i) The RFU [✂]. Sky has since renewed these rights until 2020; In June 2014, the USGA [✂], again allowing Sky to renew its rights;

(ii) [✂] SANZAR had formally agreed to renew with Sky.

(iii) [✂]

(iv) Super League Rugby [✂] Sky has now renewed its deal until 2021.

(v) The recent Football League rights renewal is an example of a renewal that occurred as part of 'in-life' contractual negotiations.[336] [✂] a deal was ultimately struck with Sky in July 2013.[337] Sky's contract with the Football League was for a rights period from August 2015 ending in 2019. BT understands that this contract contained an extension (that Sky was entitled to exercise at its sole discretion) of one year to the

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[331] [✂]

[332] BT also notes that unlike the case for Premier League rights, where, as a result of the "no single buyer rule", at least some portion of these rights are preserved for a third party other than Sky, this is not the case for any other sports.

[333] [✂]

[334] See footnote 238 above, on page 91.

[335] For example, this appears to have been the case with the recent Football League rights renewal (http://www.sportindustry.biz/news/sky-sports-extends-football-league-deal#VvxH7KCbw1SoqbAq.99).

[336] "Sky Sports extends Football League deal", Sport Industry, 20 February 2015, available at: http://www.sportindustry.biz/news/sky-sports-extends-football-league-deal#VvxH7KCbw1SoqbAq.99.

[337] Football League rights deal from August 2015 to end of 2017/2018 season was announced 18 July 2013. https://corporate.sky.com/media-centre/news-page/2013/football_league_and_sky_sports_agree_new_broadcasting_partnership

end of the 2019/20 season and a further extension (that can only be exercised if jointly agreed by Sky and the Football League) of one additional year to the end of the 2020/21 season. Thus far, Sky has exercised the first of these rights, giving Sky exclusive coverage until 2020.[338]

4.62. In discussions with Ofcom,[339] it appeared that as a result of observing that certain sporting events were available FTA Ofcom had erroneously surmised that this may mean that Sky's bidding advantages might be lower for certain types of sports. This is not the case. As discussed at paragraph 4.11(ii) above, many of the sports rights that are available FTA are not permitted to be acquired by pay TV broadcasters, as they are Category A Listed Events. More relevant for an assessment of Sky's bidding advantages, many sporting events are available FTA as the rights holders have deliberately chosen the strategy of ensuring their rights are broadcast FTA in order to maximise exposure for their sport rather than maximising potential revenues via pay TV.

4.63. All sports rights sellers must make a trade-off between greater exposure/prominence in order to maintain interest in the sport more generally as well as lucrative sponsorship deals (which is achieved through FTA availability), and maximising revenues for their rights (achieved through pay TV exclusivity). While many rights holders manage this with some form of dual model (e.g. F1 rights on Sky, or UEFA's requirements that BT must make certain matches available FTA), some prioritise exposure, and sell all of their rights FTA (like Wimbledon). Since those rights holders have made the choice not to offer the rights via pay TV, this provides no insight into Sky's bidding advantages for other sports rights within that sporting genre. It is also possible that a given set of sports rights are insufficiently attractive to incrementally add to subscription take-up/retention on pay TV channels. In that case pay TV operators may place a low value on such rights, and hence it may be profit maximising for a rights holder to make these rights available FTA. However, again, this provides no insight into Sky's bidding advantages with regards to live rights for other competitions within the same sport.[340]

4.64. The only relevant data point with respect to Sky's bidding advantages in this context, would be if Sky and a FTA broadcaster went head to head for a set of rights, and the FTA

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[338] The extension until end of 2018/19 season with possibility of extension to 2019/20 season was announced 20 February 2015 http://www.sportindustry.biz/news/sky-sports-extends-football-league-deal#VvxH7KCbw1SoqbAq.99

[339] Wednesday 4 February 2015.

[340] To take a clear example, in Rugby League Sky hold the key Super League rights, showing more than 90 live matches from 5 February – 10 October 2015, whereas the FTA coverage on BBC is limited to the less prestigious Challenge Cup competition, which last season amounted to only seven matches broadcast live on BBC between 18 March and 31 August 2014 (2015 broadcasting details not yet publicly available as of February 2015).

broadcaster were to outbid Sky on an expenditure basis for the rights. BT is obviously not privy to such information, but notes that recently various events that used to be strongly associated with FTA (such as the Masters and British Open golf tournaments, and Formula One) have moved to pay TV on Sky Sports, as evidenced in Section 2.

4.65. For the reasons set out above, Sky will be able systematically and on average to outbid rivals for live premium sports rights, even second-tier rights where the absolute cost of the rights is lower.

<u>BT's model of indirectly monetisation its sports rights via its broadband subscriber base does not overcome Sky's material bidding advantages</u>

4.66. In the Consultation Document, Ofcom notes that BT's business model is similar to that of Setanta and ESPN in many respects, and therefore Ofcom "*expect BT to face one or more of the disadvantages identified in 2010*".[341] However, Ofcom also queries whether the way in which BT monetises its sports rights, by offering them for free to its broadband customers, provides BT with the ability to overcome Sky's bidding advantages. On this point Ofcom concludes:

> "*Overall it is not clear whether BT's strategy of bundling a light sports offering for free with broadband overcomes Sky's advantage of being the vertically integrated operator on the largest platform.*"[342]

4.67. BT is surprised that Ofcom has raised this question, even in such a tentative fashion, as BT has previously addressed this issue in detail in its Competition Act investigation against Sky, including providing an economic model that addressed this point. As the evidence summarised below demonstrates BT's approach of monetising its sports rights indirectly through its broadband customers is incapable of over-turning Sky's bidding advantages.

4.68. It is important to be clear what the relevant question is with respect to BT's indirect monetisation strategy. It is clearly the case that, as a result of its ability to monetise its investment in sports rights through incremental broadband subscriptions and retentions, BT is in a somewhat better position than an operator who bid for and won premium sports rights and started with no means to monetise the rights at all. As a result of the strategy that BT adopted in giving BT Sport away for free to its broadband base, [✂] Such an option would not have been available to an entrant without a broadband subscriber base.

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[341] Consultation Document, paragraph A8.10.
[342] Consultation Document, paragraph A8.13.

4.69. However, this is not the relevant question for Ofcom's WMO Review. The relevant question is whether the fact that BT is able indirectly to monetise its sports rights in this way is sufficient to overcome Sky's bidding advantages. Whether or not BT may be in a better position than other potential bidders, the issue is whether BT has, or is likely to, overcome Sky's bidding advantages such that Sky is no longer in a position systematically and on average to outbid BT (and others) for live sports rights. As such, it is irrelevant if BT is stronger new entrant than another kind: the issue is whether the gulf between Sky and other bidders has now closed.[343]

4.70. When BT acquired the minority Premier League rights in 2012 it had various options as to how to monetise those rights at the retail level. In particular, it could:

(i) attempt to directly monetise its rights, like ESPN or Setanta had done, [✂]; or

(ii) indirectly monetise its rights by offering its sports content for free to its existing broadband subscriber base [✂][344]

4.71. BT chose a retail model[345] that blended both of these options:

(i) direct monetisation of the rights via the DSat platform where the highest concentration of premium sports channel subscribers with a high willingness to pay for sports channels were located. As a result of existing Conditional Access regulation this meant that BT could retail directly to subscribers [✂][346],[✂]. BT currently has [✂] such subscribers; and

(ii) indirect monetisation through BT broadband subscribers who receive BT Sport for free.

4.72. It is clear that BT's direct monetisation strategy has had little effect on Sky's bidding advantages: BT's installed base of direct subscribers who pay for the BT Sport channels on a stand-alone basis is [✂], whereas, as set out in Section 2, Sky has 5 to 6 million premium sports subscribers to its retail products. Therefore, Sky has an additional [✂] direct sports subscribers over BT. As such, in line with the model described above at paragraph 4.52, Sky

[343] In this respect, BT believes that the outcome of the latest Premier League auction is particularly instructive.
[344] A survey commissioned by TalkTalk in the context of Ofcom's consultation on its proposed VULA margin consultation conducted by the market research agency Ipsos MORI suggested that 50% of BT broadband customers do not value BT Sport and that, of those that do, 50% have zero willingness to pay for the content. The average value is below £3 per month (available at http://stakeholders.ofcom.org.uk/binaries/consultations/VULA-margin/responses/TalkTalk_Group_-_Annex_-_Ipsos_MORI_Survey_data.xlsx). [✂]
[345] BT also monetised its rights via wholesale arrangements and via sales to commercial premises.
[346] And who most likely took a dual or triple-play service from Sky to access their broadband.

remains in a position to extract vastly more value from the direct sale of acquired rights than BT can.

4.73. The question, then, is whether BT's strategy of indirect monetisation of its rights can overcome the remaining "value gap" created by Sky's additional [✂] sports subscribers with a high willingness to pay for premium sports channels, such that Sky can no longer be expected systematically to outbid BT in future auctions. There are a number of reasons why this is demonstrably not the case, set out below.

4.74. The first is to note that Sky equally has the opportunity to pursue a mixed strategy of direct and indirect monetisation. As set out in Section 2 above, Sky also has a sizeable base of installed broadband subscribers (of a similar magnitude to BT) and could choose to offer one or more of its existing sports channels for free with broadband subscriptions.[347] However, indirect monetisation is only a rational strategy where giving away a sports channel for free to broadband subscribers is more profitable over the rights period than requiring subscribers to pay directly for those channels (either individually or when bundled in a package of channels). As Sky's behaviour clearly demonstrates, to date a strategy of pure direct monetisation has been more profitable for Sky than a strategy that also includes indirect monetisation.[348]

4.75. Sky's behaviour therefore clearly demonstrates that offering premium sports channels indirectly [✂]

4.76. BT also notes that if Ofcom examines BT's indirect revenue benefits as a result of the fact that it offers BT Sport for free with broadband, then Ofcom must equally assess the incremental revenue benefits to Sky of offering broadband for free with its pay TV offerings (which, as the data at paragraph 2.3(ix) shows, has been an extremely effective strategy). Similarly, Ofcom must consider the fact that Sky's buy through model from basics ensures that it derives incremental revenues from sports subscribers that it might otherwise not achieve. As a result Sky's advantages from "indirect" monetisation (albeit with respect to different products) are likely to more than outweigh the benefits that BT derives from offering BT Sport for free.

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[347] BT notes that Sky has chosen to do the opposite (i.e.to give broadband away for free with its sports channels), a strategy that will further underpin its bidding advantages by further reducing: (i) the (already very low) levels of pay TV switching (see paragraph 4.42 above); and (ii) Sky's own very low levels of churn (see paragraph 2.3(iv)above).

[348] It is important to note that, despite the existence of the WMO remedy, Sky has been able to create new, distinct channels such as SS5 and F1, which it could have used for indirect monetisation purposes. Given the high degree of differentiation of these channels (through Sky's deliberate branding), Sky could have offered these channels indirectly, while continuing to charge for its other Sky Sports channels directly. However, it was clearly more profitable for Sky to include the new content within its existing Sky Sports proposition.

4.77. However, even if a consideration of Sky's own "indirect" advantages is omitted, it is still clear that BT could not overcome Sky's bidding advantages as a result of its indirect monetisation strategy. BT does not have a sufficiently high volume of indirect subscribers [✂] to overcome Sky's large installed subscriber base with a high willingness to pay for premium sports channels. BT only has [✂] indirect retail subscribers (excluding app only subscribers[349]) in total. As set out above, when BT's direct subscribers are factored in, Sky still maintains a gap of [✂] more direct sports subscribers. Thus, even from this most basic calculation it is clear that the number of Sky's [✂] direct subscribers is greater than the number of BT's [✂] indirect subscribers, meaning that Sky will still be able to outbid BT systematically and on average.

4.78. More importantly, the absolute size of BT's indirect subscriber base is not the relevant subscriber number for a bidding assessment. [✂][350],[✂].[351]

4.79. Therefore the only indirect BT Sport subscribers who matter for the purposes of rights valuation (and hence for assessing Sky's bidding advantages) [✂].[352] This number is likely to be considerably lower than the [✂] total indirect subscribers set out at paragraph 4.78 above, because:

(i) by definition, indirect subscribers, particularly those who currently receive BT Sport via the BT TV platform, [✂]

(ii) as a result, given these subscribers [✂] (and given the low levels of pay TV switching generally as described in paragraph 3.64(iii) above), it is [✂][353]; and

(iii) [✂][354], [✂].[355]

4.80. Indeed, even if the absolute size of BT's broadband base compared to Sky's wasn't irrelevant and having a larger broadband base **did** make it easier to indirectly monetise sports rights, the size of BT's broadband base would still not be significant enough to overcome Sky's

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[349] [✂] including app only. Figures as at 20 February 2015.

[350] [✂]

[351] [✂]In addition, as noted at footnote 176 of Ofcom's Consultation Document up to 50% of subscribers receiving BT Sport for free place no value on BT Sport, as shown by responses to Ofcom's November 2014 survey (see footnote 257 above).

[352] [✂]

[353] As set out above, this is supported by Ofcom's own survey research that 45% of BT Sport subscribers on Sky DSat and taking BT broadband gave only non-sport reasons for taking BT Sport (see Consultation Document, footnote 176). It is also consistent with the TalkTalk research previously highlighted showing that around 50% of those subscribers who are receiving BT Sport for free place no value on BT Sport.

[354] [✂]

[355] BT has another approximately [✂] subscribers who are out of contract broadband subscribers that pay £6.75 per month. These subscribers are somewhere between direct and indirect subscribers but as the numbers are small, will make no material difference to either calculation.

advantages in direct monetisation. This is for the simple reason that no matter how large the absolute broadband base, [✂]. Therefore, for BT to overcome Sky's direct monetisation strategy with an indirect monetisation strategy would require BT's broadband subscriber base to be many multiples larger than Sky's subscriber base. As such BT's ability to indirectly monetise its rights can't overcome Sky's ability to directly monetise rights, even without considering the fact that it is also open to Sky to attract these indirect subscribers itself.

4.81. In that respect, it is important to note that the value from indirectly monetising a given set of rights is likely to be similar for both BT and Sky. As discussed above, the relevant pool of indirect subscribers for the purposes of bid valuations [✂].[356]

4.82. Overall then it is clear that BT's strategy of indirectly monetising its investment in sports rights by giving BT Sport away for free to its broadband subscribers is not sufficient to overcome Sky's existing advantages when bidding for rights. Accordingly, the finding as to Sky's enduring structural advantages in premium sports auctions is unaffected.

<u>The Champions League rights auction does not provide evidence that Sky's bidding advantages have been eroded</u>

4.83. BT notes Ofcom's assessment of BT's acquisition of the Champions League rights, and in particular, its view that the outcome of the 2013 UEFA Auction "*may indicate that the barriers to BT's ability to bid for rights are lower than in the past.*"[357] BT refutes this suggestion. For the reasons set out above, Sky's bidding advantages, including vis-à-vis BT, remain as strong today as in 2010.

4.84. Ofcom also appears to imply that the outcome of the 2013 UEFA Auction demonstrates that Sky's advantages in acquiring rights have been eroded other than for Premier League rights (due to the high cost of those rights) i.e. Ofcom appears to consider that it is the relative cost of Premier League rights over Champions League rights that impacted on BT's ability to acquire the Champions League rights in this case.[358] That is simply incorrect, and would imply that BT is now in a position where it would be able to outbid Sky for sports rights, providing they are relatively less costly than live Premier League rights. Such an inference would fundamentally mischaracterise the nature of Sky's bidding advantages for the reasons explained in detail above.

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[356] BT notes that while, in principle, the same opportunity to attract the pool applies to both BT and Sky, Sky may have a greater advantage in retaining its subscribers for the reasons set out in footnote 50 above.
[357] Consultation Document paragraph A8.6.
[358] Consultation Document paragraph A8.6.

4.85. However, as BT has previously explained, the vicious circle model shows that Sky can systematically and on average outbid its rivals for rights. This does not mean that it is impossible for a rival to win sports rights, but rather that if Sky is also vying for those rights, a rival will only be able to outbid Sky in exceptional circumstances, in particular:

(i) if the rival believes (rightly or wrongly) that it will be able to extract more value for the rights in aggregate than Sky believes it is possible to achieve, notwithstanding the relative scale of Sky's subscriber base; or

(ii) Sky makes an error in judging the rival's valuation of the rights, and the auction structure punishes Sky for misjudging the rival's willingness to pay.

4.86. [✂]

(i) As BT explained in Section 2 above[✂]

(ii) [✂]

(iii) [✂] [359]

(iv) [✂] In this regard, it has been reported that: "*While Sky insisted that BT had paid far beyond what it was prepared to invest, industry gossip was rife* ***that they [Sky] had tried to make a final bid***" (emphasis added).[360] [✂][361]

4.87. As a result, the circumstances of the 2013 UEFA Auction were fully consistent with the exceptional circumstances identified under the vicious circle model described above. [✂].[362] For this to occur, [✂]

4.88. Therefore, BT's success in the 2013 Champions League auction, when properly understood as being attributable to exceptional circumstances, cannot lead to a conclusion [✂] nor that Sky's bidding advantages have been eroded. Indeed, the outcome of the 2015 Premier League Auction, in which (as noted at paragraph 4.56(iii) above) Sky again won the maximum number of games, is a strong indication that the 2013 UEFA Auction does not represent a systematic change to the competitive conditions in bidding for sports rights.

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[359] [✂]

[360] *'Gavin Patterson: the man behind BT Sport's Champions League raid'* (11 November 2013): http://www.theguardian.com/media/2013/nov/11/gavin-patterson-bt-sport-champions-league.

[361] Ofcom is obviously better placed than BT to seek information from Sky as to whether it did contact UEFA and the extent to which it was willing to increase its bid had there been subsequent auction rounds.

[362] Annex 2 of BT's Composite Factual and Legal Submission, provided by BT to Ofcom in response to the WMO Information Request in November 2014.

5. LIMITED DISTRIBUTION OF THE SKY SPORTS PROPOSITION WILL HAVE A MATERIAL EFFECT ON COMPETITION

5.1. BT notes Ofcom's assessment that "*limited distribution of Sky Sports may be prejudicial to fair and effective competition.*"[363] However, for the reasons elaborated on in this section BT believes that it is undoubtedly the case that the limited distribution of the Sky Sports proposition is prejudicial to fair and effective competition.

5.2. There appears to be some inconsistency in Ofcom's assessment as to whether the competition issues arising from limited distribution are due to an inability to offer "key sports content" or due to the importance of the Sky Sports proposition overall. Although Ofcom carries out all of its analysis on the effects of limited distribution by assessing the impact of the limited distribution of Sky Sports (which for the reasons set out in Section 3 above, BT believes is the correct basis for this analysis), Ofcom concludes that: "*Rival platforms which are unable to offer the **key sports content** available on Sky Sports may face difficulties in competing for a sizeable proportion of subscribers*".[364] This inconsistency is further compounded by the fact that Ofcom then goes on to state that this is "*due to the importance attributed by consumers to **Sky Sports** and to **Sky's market position***". [365]

5.3. BT believes that this analytical inconsistency arises from the fact that Ofcom's assessment of "key sports content" in Section 5 of its Consultation Document is divorced from the reality of the products that are actually bought and sold, namely premium sports channels and packages of channels such as Sky Sports. For the detailed reasons set out in Section 3 above, the correct approach is to consider the impact of the limited distribution of the Sky Sports proposition (as a whole), rather than individual pieces of content available within that proposition.

BT agrees with Ofcom's views on the possible forms that limited distribution may take

5.4. As was the case in the Pay TV Statement,[366] Ofcom recognises that limited distribution is not simply limited to direct with-holding of wholesale supply, but in fact encompasses a number

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[363] Consultation Document, paragraph 6.65.
[364] Consultation Document, paragraph 6.65.
[365] Consultation Document, paragraph 6.65 (emphasis added).
[366] Ofcom's Pay TV Statement was predicated on two aspects of Sky's conduct that were considered prejudicial to fair and effective competition, namely *"[r]estricted distribution of Sky's Core Premium channels [and] [h]igh wholesale prices for Sky's Core Premium channels*" (para 9.28). In relation to high wholesale prices, Ofcom noted that "***the level of Sky's wholesale and retail pricing is also prejudicial to fair and effective competition***" (para 9.108) (emphasis added). Ofcom's concern of restricted distribution also related to withholding supply, see para 11.129 of the Pay TV Statement: "[*w]e have explained in Section 7, **we believe that Sky has a broader set of reasons for withholding supply. As we explain at paragraphs 7.190 to 7.201, Sky has a strategic incentive to protect its position at the wholesale level**. Through this position, Sky is currently able to*

of broader practices that can prejudice fair and effective competition between pay TV retailers, including in particular:[367]

(i) an outright failure to wholesale the Sky Sports proposition to rival retailers at all;

(ii) wholesaling the Sky Sports proposition at rate-card prices that are too high to allow a rival retailer to become an effective competing retailer of those channels. As Ofcom found in the Pay TV Statement, Sky's rate-card prices are set at a level which is too high to ensure fair and effective competition;[368]

(iii) limiting wholesale supply in a way that reduces the value of the Sky Sports proposition to consumers. This includes wholesaling only a subset of the Sky Sports proposition, (such as a restricted range of the channels that make up the Sky Sports proposition, or non-supply of important additional services like HD, interactive, on-demand content, multi-room or the ability to offer the service across multiple in-home devices), such that a rival's retail proposition is weaker than that available from Sky itself;[369]

(iv) including terms and conditions for wholesale supply that are anti-competitive[370] or limit a retailer's ability to compete effectively either at the retail level, or in other parts of the value chain. This would include, for example, Sky's insistence on the anti-competitive Grant-Back Condition, which formed the basis of the BT CA98 Complaint, or an insistence on high minimum revenue guarantees;

(v) introducing terms that place restrictions on the kinds of marketing that rivals can undertake using the Sky Sports brand or logos, or restrict the kinds of propositions that rivals can offer (for example, preventing them from offering Sky Sports for free or bundled with certain propositions); and

(vi) self-retailing the Sky Sports proposition at high retail prices in order to manage cannibalisation in such a way as to ensure no effective competition with its own

earn returns significantly in excess of its cost of capital. It is not surprising that a remedy intended to ensure fair and effective competition may cut across Sky's strategic incentives" (emphasis added).

[367] Consultation Document, paragraph 7.3.

[368] The validity of Ofcom's pricing concerns was confirmed last year when the Court of Appeal upheld BT's argument that the CAT had failed to deal with Ofcom's concerns in its 2010 Pay TV Statement about Sky's rate-card prices for Sky Sports 1 and 2 and therefore the CAT had failed in its duty to deal with the appeal on its merits. (Judgment of the Court of Appeal of 17 February 2014, [2014] EWCA Civ 13).

[369] As the evidence set out in Section 3 of this submission shows, access to a subset of the Sky Sports proposition will not be sufficient to ensure fair and effective competition.

[370] BT notes that even when required to provide its channels on regulated terms, Sky still imposes terms that restrict fair and effective competition [✂]

retail proposition,[371] or denying its rivals the opportunity to innovate and create new or different bundles incorporating Sky Sports which might otherwise have increased competition.

5.5. BT notes, in particular that in each case, Sky may limit distribution uniformly to all rival retailers, or (for the reasons discussed in more detail in Section 6 below) it may only seek to limit distribution to certain pay TV retailers/platforms where it may perceive them to be a greater competitive threat.

5.6. As the evidence that BT has set out in detail in Section 2 above shows,[372] limited distribution of the Sky Sports proposition continues to occur, in various forms. In practice there has been only a very limited increase in the availability of the Sky Sports channels from rival retailers since Ofcom's intervention in 2010, and as far as BT is aware, what little changes in wholesale supply have occurred have been either: (i) on the basis of wholesale prices or terms that have not resulted in the emergence of fair and effective competition;[373] or (ii) due to enforced supply under the WMO Remedy (and even then that remains on the basis of high WMO prices that are set too high to ensure fair and effective competition). Indeed, as far as BT is aware, rate-card pricing and the imposition of a Grant-Back Condition are Sky 'standard terms' for all retailers, and any incentives for retailers with wholesale supply of Sky Sports to extensively market and sell the Sky Sports proposition are clearly muted given the apparent limited penetration rates on other platforms.

The limited distribution of the Sky Sports proposition has a material impact on fair and effective competition

5.7. BT agrees with Ofcom that it is the combination of the importance of the product to subscribers, and the market position of the product holder that will determine the impact that limited distribution may have. As set out in Section 3 above, access to the Sky Sports proposition is necessary to ensure fair and effective competition and, as set out in detail in Section 4 above, Sky has a strong market position (and market shares that would clearly be associated with dominance) at both the wholesale and retail level, as well as material bidding advantages when bidding for live sports rights.

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[371] In this regard, it is important that Ofcom recalls the relative retail prices that Sky adopted when self-retailing on the Video Networks Limited, (subsequently acquired by Tiscali and then TalkTalk). Pay TV Statement, paragraph 7.8

[372] See paragraphs 2.49 to 2.56.

[373] BT notes that, regardless of the profile of customers on a particular platform, Sky's wholesale rates remain problematic, and naturally limit the attractiveness of the offering that can be produced by competitors in order to appeal to their particular customer base.

5.8. As such, BT strongly believes that the limited distribution of the Sky Sports proposition will prejudice fair and effective competition between pay TV retailers. Rival retailers who are unable to offer the Sky Sports proposition will be unable to compete for a sizeable proportion of the most valuable pay TV subscribers. As BT sets out in detail in Section 3, in a business such as pay TV which is driven by high fixed costs, the wider addressable market and higher ARPU associated with premium sports subscribers is critical in terms of building a viable, competitive business. Therefore, BT endorses Ofcom's evidence that limited distribution of the Sky Sports proposition will restrict other pay TV retailers' ability to compete for a sizeable and high-value segment of pay TV subscribers,[374] and that consequently the limited distribution of Sky Sports will have a negative impact on static competition in the supply of pay TV.[375, 376]

5.9. In addition, the limited distribution of Sky Sports will also have a negative impact on dynamic competition in pay TV markets as well. For the reasons set out in detail in Section 4,[377] BT also agrees with Ofcom that "*Sky also enjoys a strong market position both as a supplier of key sports channels and as a pay TV retailer*".[378] In that Section BT has also set out its views on Sky's retail incumbency advantages due to its scale,[379] demonstrating that Ofcom is correct: without access to Sky Sports, rivals are at a scale disadvantage with respect to the fixed cost of platform operation and development, which means they are unable to exert effective competitive pressure on Sky.[380] BT also set out in detail its views on the 'vicious circle',[381] which shows again that Ofcom's analysis is correct: retaining its strong position in pay TV retailing gives Sky continued advantages when bidding for sports rights.[382]

5.10. In the context of the BT CA98 Complaint against Sky, BT commissioned Compass Lexecon to produce a stylised economic model to demonstrate the static and dynamic impact of Sky's imposition of the anti-competitive Grant-Back Condition.[383] While this model was originally

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[374] As highlighted in Section 3 (and as recognised by Ofcom in the Consultation Document, paragraph 6.11), this effect is not merely limited to those who actually subscribe to Sky Sport, but will also impact on those who value the option of subscribing to the channels at a point in the future, and hence will not select a platform that cannot offer such an option.

[375] Consultation Document, paragraph 6.57.

[376] BT notes that the introduction of NOW TV has further underscored these problems. As set out in Section 2, the NOW TV proposition targets a different market segment (i.e. those who are unwilling to pay for a monthly Sky Sports subscription), which provides Sky with incremental revenue from the sale of day or week passes. As such, NOW TV has reduced, rather than increased, the extent of static competition faced by Sky.

[377] See paragraphs 4.3 to 4.30, above.

[378] Consultation Document, paragraph 6.58.

[379] See paragraphs 4.31to 4.48.

[380] Consultation Document, paragraph 6.58.

[381] See paragraphs 4.49 to 4.89, above.

[382] Consultation Document, paragraph 6.58.

[383] Compass Lexecon, *Modelling static and dynamic competition in the retail market*, revised version 30 April 2014, submitted by BT to Ofcom in response to the WMO Information Request in November 2014.

produced in order to identify the static and dynamic economic consequences for consumers and the competitive process resulting from the anti-competitive Grant-Back Condition, it is generally applicable to any aspects of limited distribution. This model shows that:

(i) The limited distribution of the Sky Sports proposition[384] [✂]

(ii) In a static sense, consumers will be worse off under a scenario where Sky limits the distribution of its Sky Sports proposition. It will result in subscribers having less choice (given only a restricted premium sports offering is available to them on certain platforms) and Sky's customers paying higher retail prices since the (already limited) competitive constraint on Sky is further undermined. Overall, short-term consumer welfare is diminished with limited distribution.

(iii) Limited distribution of the Sky Sports proposition will also lower rival's (such as BT's) incentives to invest in product innovation and value-added services. In addition, Sky's price and market share advantages means that Sky is more likely to further entrench its market position over time, as it simply will not be profitable for rivals to match Sky's investments given the relative (and increasing) gap in scale/market shares.[385] Overall, in terms of future technological investment, consumers will be left worse off as a result of the limited distribution of the Sky Sports proposition, and reduced innovation around it.

(iv) Crucially, limited distribution will also weaken rivals' ability to bid in future for premium sports content. [✂]

(v) In short, limited distribution of the Sky Sports proposition will not only distort static price competition in the short-term, but will also distort dynamic non-price competition in the long run and entrench and increase Sky's market position at the retail and wholesale level, as well as further reinforcing its upstream bidding advantages.

5.11. BT also commissioned Compass Lexecon to undertake a discrete choice modelling analysis, using real subscribers' responses to a bespoke survey, in order to test whether the theoretical static results predicted by the stylised economic model were likely to be observable 'in real life'. The analysis of consumer data confirmed all of the critical,

[384] It is important to note that this model was designed only to look at a situation whereby Sky limited the wholesale distribution of the WMO regulated channels SS1 and SS2 to BT. The relevant findings would be further strengthened if the full Sky Sports proposition is assessed, since Sky's market share and pricing advantages that the model identifies would be further strengthened as a result of the inclusion of the full Sky Sports proposition.
[385] Note that the model fully corroborates BT's evidence as to scale disadvantage in terms of platform operation and development (as set out in Section 4 above, summarised in paragraph 5.9.

verifiable, assumptions within the Compass Lexecon theoretical model, and therefore validated the conclusions reached as to the impact of the limited distribution of the Sky Sports proposition 'in real life'.

5.12. BT agrees with Ofcom that it is difficult to measure the dynamic impact on competition in terms of the importance of the Sky Sports proposition in growing a pay TV subscriber base. However, BT notes Ofcom's statement that "*Recent evidence from the supply of Sky Sports on BT Cardinal and TalkTalk TV is inconclusive on the impact of Sky Sports on subscriber growth*". Ofcom goes on to highlight BT's view that "*While the launch of Sky Sports 1 and 2 on the BT Vision service did deliver material growth, in reality this growth was more muted than originally anticipated".*[386] But it is hardly surprising that recent evidence from TalkTalk and BT show muted levels of sports subscriber growth, when wholesale supply of the Sky Sports proposition in both cases is still subject to limited distribution:

(i) As BT has previously highlighted in Section 2, although TalkTalk has access to the full set of Sky Sports channels in SD, it does not have access to the channels in HD. In addition, to the extent that TalkTalk's supply is on the basis of rate-card prices, these prices are too high to allow fair and effective competition. Thus, TalkTalk has wholesale supply of SD channels only and on terms that will not allow it to be an effective competitor. It is notable that TalkTalk's "Sky Sports Boost" is more than 20% more expensive than Sky's "Sky Sports Pack" (£30 per month compared to £24.50 per month). As a result, the package is not broadly marketed by TalkTalk, nor is it innovatively packaged.

(ii) As such it is no surprise that TalkTalk's current base of retail subscribers has a limited appetite for premium sports channels. This underpins BT's view that the terms of wholesale supply to TalkTalk means it has no incentive to seek premium sports subscribers and compete effectively against Sky. In fact, TalkTalk's Chief Executive, Dido Harding, has commented: "*In terms of its impact on our business, fundamentally we're just not in the premium sports game. The reality is if you want premium sports you're not going to be a TalkTalk customer….*"[387] While BT does not have detailed figures on the take up of the Sky Sports channels on TalkTalk's platform, for these reasons, BT believes that it will be low.

(iii) As BT set out in detail in Section 2 above, for much of the period since 2010, BT was unable to offer any Sky Sports channels on its [✂] platform. As a result of Ofcom's not addressing the BT CA98 Complaint for a period of 21 months, BT did not have

[386] Consultation Document, paragraph 6.59.

[387]http://www.telegraph.co.uk/finance/newsbysector/mediatechnologyandtelecoms/telecoms/10059930/TalkTalk-backs-Peppa-Pig-over-BTs-Premier-League-football.html.

wholesale supply of any Sky Sports channels on its [✂] platform for much of the period that Ofcom has reviewed. It was only following the updated IRO Judgment that BT has had any Sky Sports channels on its BT YouView platform.[388] As such, [✂].

(iv) Moreover, for the reasons set out in detail in Section 3 above (and indeed in BT's outstanding appeal on the Pay TV Statement), the current WMO remedy is ineffective as a result of the fact that it covers only a subset of the Sky Sports proposition, and the WMO rates that persist remain too high to ensure fair and effective competition (as outlined below). The fact that BT has been unable to grow its retail pay TV subscriber base with only a sub-set of the Sky Sports proposition strongly supports BT's position that access to the full Sky Sports proposition is required for a pay TV retailer to be able to compete effectively.

(v) Further reinforcing this effect, as BT set out in detail in the course of the Pay TV Proceedings, the level of WMO prices has been incorrectly set too high, due to flaws in the current WMO methodology. In particular, Ofcom's modelling assumptions around fixed costs and churn rates, its treatment of multi-room and discounts, and its approach in terms of the headline reference retail price it uses for WMO adjustments all led to WMO prices that were too high to allow fair and effective competition. BT notes that in certain cases (such as with respect to discounts) the methodological approach adopted by Ofcom is inconsistent with its approach in other regulatory interventions (such as the VULA margin squeeze). Moreover, many of these errors have been exacerbated over time, leading to a WMO price which is now in excess of rate-card prices (which, in themselves are too high to ensure fair and effective competition).

(vi) Finally, the fact that Sky has been able aggressively to take advantage of deficiencies in the current WMO methodology and has actively sought to move its content off the regulated channels,[389] without appropriate monitoring and enforcement on the part of Ofcom, has further served to undermine the effectiveness of the current WMO remedy in terms of delivering subscriber growth for competing retailers. In particular:

(a) Sky now offers discounts as standard on its headline retail price. In 2010, when Ofcom introduced the WMO remedy, Sky did not undertake

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[388] Without any direct marketing, BT was able to sign up [✂] new Sky Sports subscribers on its YouView platform in the first two weeks of the channels being made available, supporting BT's position that there was latent demand for even this (limited) Sky Sports offering.

[389] See paragraph 3.52 to 3.53 above.

discounting off its headline prices. As set out in the non-confidential version of Mr Darcey's second witness statement in the Pay TV Proceedings, Sky ceased discounting its TV packages in above the line acquisition marketing at the end of 2006, due to concerns that such discounting could operate to devalue Sky's pay TV proposition.[390] Annex 7, paragraph 1.230 of the Pay TV Statement makes clear that the WMO price adjustment mechanism should be based on Sky's advertised retail prices. Ofcom interprets this as Sky's 'headline' retail price notwithstanding the fundamental shift in Sky's behaviour. Therefore there is now a persistent discrepancy between Sky's headline prices and the price it uses to attract retail subscribers as a result of Sky's virtually continuous practice of discounting off its headline price, which materially undermines the efficacy of the WMO remedy.[391]

(b) As set out in Section 3 in more detail, Sky has shifted content on a very large scale from the regulated channels onto its unregulated sports channels. Most notably, Sky's launch of SS5 on 12 August 2014 was largely created from sporting events previously on the regulated sports channels. On a conservative basis, BT estimates that in the twelve-month period from 12 August 2014, Sky will broadcast at least 162 live football matches (over 360 hours of content) on SS5 that, but for the launch of Sky Sports 5, would have been broadcast on SS1 and SS2. In fact, BT estimates that 37% of the content that goes to make up the SS5 channel was previously on SS1 and 29% on SS2.[392] Sky has also shifted the Ryder Cup from SS1 to SS4 (rebadged Sky Sports Ryder Cup), and has rebalanced the amount of coverage of many other events towards SS3 and SS4 (US Open tennis, ATP Tour tennis, US Open golf, European Tour golf, USPGA golf, etc).

5.13. Despite the difficulties of measuring the impact on long-term dynamic competition, BT still believes that it is an essential component of Ofcom's analysis of the effects of limited distribution. While the presence of short term static impacts is a clear indicator of significant adverse effects on competition (as Sky's advantages are so strong that it can translate them into immediate financial and competitive advantages), static impacts are less

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[390] Second witness statement of Michael Darcey, paragraphs 106 to 110 (non-confidential version).

[391] It is important to note, that at the time of the Pay TV Statement, BT informed Ofcom that this was likely to occur and suggested Ofcom should change its methodology to address this concern.

[392] It is important to note that these estimates are based on live match data recorded by BARB. As such they do not take account of the substantial additional content shown behind the red button for these football tournaments and thus under-estimate the total amount of content that will move in practice. The content shown behind the red button is likely to be substantial in the case of the Champions League where up to 8 matches are shown simultaneously in the initial group stages.

important than dynamic competitive effects. In fact, for the reasons set out in detail in Section 6, in order to achieve long-term dynamic benefits Sky may choose to forgo some revenue in the short term, precisely because of the relative importance of the long-term dynamic benefits of maintaining its market position. Therefore, the focus of Ofcom's analysis should be on the dynamic benefits of addressing limited distribution of the Sky Sports proposition and the benefits for the competitive process (and hence for consumers) that this will bring:

(i) BT has already set out at length in Section 4 above how the limited distribution of the Sky Sports proposition creates a vicious circle, which further entrenches Sky's market position at all levels of the value chain. By creating the conditions in the long run that allow Sky's rivals to bid successfully for live sports rights, Ofcom can unlock fair and effective competition across the entire value chain in pay TV.

(ii) However, it is also important to recognise that long before the vicious circle is fully unwound, the process of competitive rivalry will deliver dynamic benefits for consumers. Retail rivals who are interested in acquiring rights will have an increased incentive to build up their subscriber bases quickly, as large subscriber bases are necessary to be able to monetise sports rights and successfully bid for them. This is likely to result in more aggressive retail competition for customers from the outset which would bring benefits to customers in the form of improved offers, more choice and better prices.

(iii) Intensified retail competition will enable and incentivise Sky's rivals to innovate at the downstream level of the supply chain, making corresponding investments in their respective platforms, retail packaging and price points to seek to win retail market share where they were previously unable to do so. This is likely to encompass both product innovation (increasing quality and/or variety) and process innovation (reducing costs and thereby prices).

Limited distribution of BT Sport has no impact on fair and effective competition

5.14. As set out above, BT agrees with Ofcom that it is the importance of the channel proposition to subscribers, combined with the market position of the channel holder that will determine the impact of limited distribution. In light of the evidence contained in Section 3 of this Submission clearly demonstrating that none of the BT Sport channels individually, nor when considered as a single package of channels, are necessary to ensure fair and effective competition, and the evidence contained in Section 4 showing BT's limited market position (with market shares that are significantly below the levels that could be expected to impact on competition),[393] it is clear that even if BT engaged in the limited distribution of BT Sport (which, as the evidence set out in Section 2, and discussed further in Section 6 below shows, it does not), it could not have any impact on fair and effective competition.

5.15. BT notes Ofcom's assertion that the limited distribution of BT Sport "*may have a small impact on short-term competition as rival platforms without access to BT Sport would find it difficult to compete for between 5% and 10% of pay TV customers.*"[394] For the reasons set out in detail in Section 3 above, Ofcom's analysis materially overstates the impact that BT Sport is likely to have on platform switching. It is likely to be considerably lower than the 5% to 10% of pay TV customers that Ofcom has identified, such that the presence or absence of BT Sport is not a sufficient driver of pay TV subscribers' decisions to have an impact on the competitive process.[395]

5.16. Moreover, the presence or absence of BT Sport has no impact on building a base of customers as empirically demonstrated by the situation with respect to TalkTalk. TalkTalk does not currently have access to BT Sport, yet its pay TV base has grown rapidly, adding 600,000[396] subscribers since the launch of BT Sport. In contrast over the same period, BT's own TV subscriber base has only grown by [✂] subscribers.[397]

5.17. In any event, as the evidence in Section 4 demonstrates, BT Sport is a recent entrant, with a very small market share at both the wholesale and retail level on any reasonable metric deployed.[398] It is attempting to compete at the retail level against an entrenched incumbent with material incumbency advantages, and upstream in the acquisition of sports rights against an incumbent with significant bidding advantages. When this competitive dynamic is properly appreciated, it is clear that, in light of its market position, the limited distribution of BT Sport could not have an impact on competition, regardless of the proportion of respondents to Ofcom's survey who claim that BT Sport may influence their subscription decision. As such it would be disproportionate and inappropriate to consider regulating BT Sport even were it to engage in limited distribution (which it does not).

5.18. BT also notes Ofcom's claim that "*limited distribution of BT Sport could allow BT to grow its BT TV subscriber base and monetise sports rights more successfully than it otherwise would*

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[393] BT notes, for example, that in the EU merger context there is a presumption that a market share below 25% is not liable to impede effective competition (para 32 of the EU Merger Regulation).

[394] Ofcom Consultation Document, paragraph 6.66.

[395] As set out in detail in Section 3, BT's acquisition of the Champions League rights does not change this assessment.

[396] Based on TalkTalk quarterly results to end September 2013 and December 2014 respectively.

[397] Based on BT internal subscriber data for the weeks ending 26 July 2013 and 20 February 2015, respectively.

[398] BT notes that Ofcom states that "*BT's share of supply of both key sports channels and retail supply is less than 25%*." In fact, as the analysis set out in Section 4 shows, [✂].

have. In the medium to long term this could give BT a chance to overcome the barriers to expansion and act as a more effective competitor to Sky in both the supply of key sports channels and at the retail level."[399] While BT accepts the point that Ofcom is making in principle (i.e. that the dynamic benefits from the limited distribution of BT Sport could be beneficial in the long run and outweigh any static competition concerns), in practice it is unlikely that the limited distribution of BT Sport could have any impact on the competitive process at all:

(i) For Ofcom's hypothesis to be correct: (i) BT Sport would need to be a sufficiently important proposition in isolation to drive subscription decisions for a large enough group of subscribers; and (ii) BT's market position would need to be sufficiently strong that it could act independently of the competitive pressures from Sky, to drive take-up to BT's TV platform as a result of limited distribution. For the reasons set out in Section 3 and Section 4 summarised above, neither of these conditions are met.

(ii) Equally, if Ofcom was correct, and the limited distribution of BT Sport was capable of driving subscriptions to BT's TV platform in sufficient numbers to allow BT ultimately to overcome Sky's bidding advantages, then this would imply that BT should have a strong incentive not to make its channels available on the two largest platforms (Sky's DSat and Virgin Media's platforms), yet (for the reasons set out in detail in Section 6) BT makes BT Sport available on both of these platforms. Moreover, BT has also sought to make BT Sport available on smaller platforms, as evidenced by its wholesale discussions with TalkTalk (discussed in more detail in Section 6).

(iii) Similarly, [✂]

(iv) Furthermore, Ofcom's analysis ignores the other disadvantages that BT's platform faces vis-à-vis other competitors (especially Sky). BT cannot offer the Sky Sports proposition, it cannot offer Sky Movies in HD and it does not have access to any Sky basic channels (in SD or HD). In light of exceptionally low switching levels in digital TV and pay TV (as discussed at paragraph 4.42 above), it is unclear on what basis Ofcom believes that the limited distribution of BT Sport would be capable of overcoming such disadvantages in order to allow BT to overcome Sky's bidding advantages and act as a more effective competitor to Sky in both the supply of key sports channels and at the retail level.

[399] Consultation Document, paragraph 6.69.

6. SKY HAS AN INCENTIVE TO LIMIT THE DISTRIBUTION OF ITS SKY SPORTS PROPOSITION

6.1. In Section 7 of the Consultation Document, Ofcom reaches the conclusion that "*there are risks that Sky might have incentives to not supply rival retailer's platforms or to supply only on unfavourable terms.*"[400] However, in light of the available evidence, BT believes that this conclusion is too tentative: Sky has a strong incentive to limit the distribution of its Sky Sports proposition, in particular to BT. The evidence in this section shows that:

(i) Sky (and only Sky) has the ability to impede fair and effective competition through the limited distribution of its Sky Sports proposition (paragraphs 6.3to 6.4);

(ii) Sky has both a static, and an even stronger dynamic, incentive to limit the distribution of its Sky Sports proposition (paragraphs 6.5 to 6.16); and

(iii) By reference to observable market outcomes, it is clear that, in practice, Sky has limited the distribution of its Sky Sports proposition (paragraphs 6.17 to 6.21).

6.2. The evidence in this section also shows that BT does not have an incentive to limit the distribution of BT Sport (paragraphs 6.22 to 6.30).

Sky has the ability to impede fair and effective competition through the limited distribution of its Sky Sports proposition

6.3. The evidence set out in the proceeding Sections 2 to 5 of this Submission demonstrated that Sky has the ability to impede fair and effective competition through the limited distribution of its Sky Sports proposition:

(i) The evidence in Section 3 demonstrates the importance of the Sky Sports proposition in subscribers' subscription decisions. It is sufficiently important to a large enough number of subscribers to impact on consumer subscription behaviour and choice of platform for a material number of subscribers.

(ii) The evidence in Section 4 demonstrates that Sky has a strong market position (with market shares that would clearly be associated with dominance in competition law) across the pay TV value chain, and that it enjoys retail incumbency advantages (particularly in relation to its scale) as well as material bidding advantages when bidding for live sports rights that further reinforce Sky's market position at the wholesale and retail level.

(iii) Section 5 shows the material impact on rivals' ability to compete resulting from limited distribution of the Sky Sports proposition. In a business such as pay TV which

[400] Consultation Document, paragraph 7.19.

is driven by high fixed costs, the wider addressable market and higher ARPU associated with premium sports subscribers is essential in terms of building a viable, competitive business. As such the limited distribution of the Sky Sports proposition will restrict other pay TV retailers' ability to compete for a sizeable and high-value segment of pay TV subscribers, and consequently will have a negative impact on static competition in the supply of pay TV services. The impact on dynamic competition resulting from the vicious circle will be even worse, and limited distribution of the Sky Sports proposition will also lower rivals' incentives to invest in product innovation and value-added services to the detriment of consumers.

6.4. As a consequence, it is clear that Sky has the ability to impede fair and effective competition through limited distribution of its Sky Sports proposition. BT also agrees with Ofcom's view that there are many different forms that this limited distribution might take (see paragraph 5.4 above).

Sky has a strong incentive to limit the emergence of fair and effective competition by limiting the distribution of its Sky Sports proposition

6.5. Having determined that Sky has the ability to impede fair and effective competition through the limited distribution of its Sky Sports proposition, it is then appropriate to assess whether Sky is likely to have an incentive to do so. For the reasons set out below, Sky has clear static and dynamic incentives to prevent effective competition emerging across the pay TV value chain in order to protect its strong market position and the incumbency advantages that it enjoys both at the retail level and when bidding for rights.

<u>Sky's static incentive to limit the distribution of its Sky Sports proposition</u>

6.6. BT agrees with Ofcom's assessment at paragraph 7.12 of the Consultation Document that Sky's static incentives to supply will depend on the trade-off between the revenues it may gain from wholesaling to a rival retailer against the retail revenues it might lose as a result of a rival retailer being able to offer the Sky Sports proposition on a competing platform.

6.7. In assessing Sky's static incentives to limit the distribution of its Sky Sports proposition, it is important to recognise at the outset that the vast majority of sports subscribers with a high willingness to pay for premium sports channels at current retail prices, most likely already have a relationship with Sky Sports, either at the retail level on Sky's own platform, or via its wholesale arrangements with Virgin Media. As discussed at Section 3 above, given the importance of these channels in subscribers' decision making, it is unlikely that there are material numbers of subscribers who are willing to pay for Sky Sports at current retail prices that are currently residing on other pay TV platforms where the full Sky Sports proposition is unavailable. Moreover, the introduction of NOW TV has also allowed Sky to capture the residual category of potential subscribers who are not willing to subscribe to the Sky Sports proposition as part of a wider pay TV subscription on a monthly basis, but who do have a propensity to consume this content for shorter time periods or at different intervals.

6.8. Against this background, it must be recognised that Sky's static incentive to wholesale its Sky Sports proposition to additional pay TV retailers is likely to be very low:

(i) As there are likely to be few subscribers who are willing to pay for Sky Sports at current monthly subscription retail prices residing on platforms other than Sky's DSat and Virgin Media's platforms, the revenue upside from wholesaling to an additional platform is likely to be low. As Ofcom recognises, this is particularly likely to be the case for platforms such as BT's where the total number of subscribers is also low.[401]

(ii) However, for those subscribers for whom Sky Sports was the primary force behind their original Sky subscription decision, there is a risk that some portion of these might switch to another platform that better meets their needs overall if Sky Sports was more widely available.

(iii) In the event Sky wholesaled on prices and terms that allowed for fair and effective competition, there is also the possibility that a rival retailer might offer Sky Sports at a lower retail price or in a more attractive bundle (e.g. with different or no buy-through requirements)[402] than prevails in the market today, exacerbating the potential risk of switching away from the Sky DSat platform or forcing Sky to lower its own retail prices to retain the subscriber.

6.9. In summary, Sky's static incentive to wholesale will obviously be influenced by its determination of the revenues potentially realisable: thus, the larger the overall subscriber base of a retailer the higher the likelihood that there are some potential Sky Sports subscribers residing on that platform, and thus the larger the potential wholesale revenues for Sky in making Sky Sports available to that rival retailer. There is a lower static incentive for Sky to supply to rivals with smaller pay TV subscriber bases, particularly if they are most likely to expand by capturing some of Sky's retail market share.

6.10. Sky can mitigate any static downside it faces from wholesale supply by engaging in practices that are designed to limit the distribution of its Sky Sports proposition, either in terms of

[401] Consultation Document, paragraph 7.14.
[402] BT notes that while Sky has a strong incentive to protect its direct revenues from premium sports subscribers (the vast majority of whom pay an incremental sum of £16.50 to £24.50 per month for access to Sky Sports), this is strongly reinforced by its desire to protect the 'buy-through' model for the core of its subscriber base. A la carte access to Sky Sports on a monthly subscription basis, without requiring a basic subscription would likely be perceived by Sky as a material threat to its retail revenues, and hence market position overall.

price or in terms of content. BT sets out a number of examples based on Sky's existing practices discussed throughout this Submission:

(i) Sky may only wholesale its Sky Sports proposition to a rival at a wholesale price that is sufficiently high to limit the impact of platform switching away from Sky, i.e. by setting a high wholesale price, Sky can indirectly force its rival to charge high retail prices (or risk making substantial losses on the sale of Sky Sports) that mean they cannot compete effectively with Sky for its existing retail subscribers. It is important to note that in light of Sky's significant scale relative to other pay TV rivals, and its entrenched retail incumbency advantages the wholesale price that it can charge may pass a 'traditional' margin squeeze, but would still be too high to allow a pay TV rival of much smaller scale to compete effectively.

(ii) Equally, Sky can provide a substandard or partial product to its rivals, for example by only wholesaling a sub-set of the Sky Sports channels, or only wholesaling SD rather than HD versions of the Sky Sports proposition. This would allow Sky to access revenues from consumers with some interest in Sky Sports, whilst simultaneously making it very difficult for rivals to attract subscribers away from the Sky platform. Sky may also place restrictions on the kinds of marketing that rivals can undertake using the Sky Sports brand or logos, or restrict the kinds of propositions that they can offer (for example, preventing them from offering Sky Sports for free).

(iii) As discussed in BT's CA98 Complaint, Sky might introduce terms and conditions to limit a rival's ability to benefit from their own investment in platform or proposition differentiation. As set out in the BT CA98 Complaint, [✂].

(iv) Sky might also refuse to wholesale its channels entirely, or insist on a self-retail arrangement which would allow Sky to set the price itself on a rival's platform. In this way Sky would ensure it had the best of all worlds, as it would effectively only be 'competing' with itself: it could secure any revenues from subscribers unwilling to switch from their current platform, and could set retail prices at a level that would manage the cannibalisation risk against its own DSat (or NOW TV) subscriber base. Self-retail would also deny its rival the opportunity to innovate and create new or different bundles incorporating Sky Sports which might otherwise have led to switching.

6.11. By undertaking one or more of these limited distribution strategies it would be possible for Sky to capture some incremental wholesale (or in the case of self-retail, retail) revenues from subscribers on a rival's platform, whilst simultaneously reducing the likelihood that Sky's own retail subscribers would switch away from its DSat or NOW TV offerings. As BT has highlighted in Section 2 (and elaborates on in more detail at paragraphs 6.16 to 6.20 below), there is ample evidence that since 2010, there has been only a very little change in the availability of Sky Sports. BT observes that any changes in wholesale supply that may have been introduced have either been: (i) on the basis of wholesale prices or terms that have not resulted in the emergence of fair and effective competition;[403] or (ii) as a result of enforced supply under the WMO Remedy. Therefore, any changes to Sky's wholesale supply since the Pay TV Statement have not been as a result of market forces altering Sky's incentives. Moreover, without the WMO Remedy, it is evident that wholesale supply of the Sky Sports proposition would be even more limited than at present.

Sky's dynamic incentives to limit the distribution of its Sky Sports proposition

6.12. In Section 2 above, BT has set out evidence of Sky's high and persistent levels of profitability, and its sustained growth in subscriber numbers and subscription revenues since 2010. In Section 4, BT has highlighted Sky's high and persistent market shares at both the wholesale and the retail levels, its retail incumbency advantages and Sky's material bidding advantages when bidding for sports rights.

6.13. The consequence of Sky's market position and profitability is that it has a powerful incentive to protect that position over the long-term, the inevitable consequence of which is that it is incentivised to impede the development of fair and effective competition at the retail level. BT described in detail the vicious circle that allows Sky to do just that in Section 4 (see paragraphs 4.52 to 4.55). The self-reinforcing nature of the vicious circle is underpinned by limited distribution of the Sky Sports proposition. If the Sky Sports proposition was wholesaled to Sky's rivals on terms (including prices) that permitted fair and effective competition, Sky's market position across the value chain would be threatened, as a 'virtuous circle' was created instead:

(i) rival retailers would have access to attractive content capable of driving subscription behaviour allowing them to grow scale and compete more effectively at the retail level as they overcame Sky's retail incumbency advantages;

(ii) as discussed in Section 5, on its own, this would bring benefits to consumers in terms of improved offers, more choice and better prices. It would also increase rivals' incentives to innovate at the downstream level of the supply chain, making corresponding investments in their respective platforms, retail packaging and price points to seek to win retail market share where they were previously unable to do so. This is likely to encompass both product innovation (increasing quality and/or variety) and process innovation (reducing costs and thereby prices);

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[403] As far as BT is aware, rate-card pricing and the imposition of a Grant-Back Condition are Sky 'standard terms' for all retailers, and any incentives for retailers with wholesale supply of Sky Sports to extensively market and sell Sky Sports are clearly muted given the apparent limited penetration rates on other platforms.

(iii) by developing their own subscriber base with an established, positive, willingness to pay for premium sports content over time, vertically integrated rivals would be better placed to challenge for live sports rights in the future;

(iv) by the same token, the erosion of Sky's own subscriber base would reduce its ability systematically to outbid rivals for relevant sports rights; and

(v) upstream sports rights auctions would, therefore, become more contestable as Sky's entrenched bidding advantages are diminished. This would enable rivals to bid more successfully for sports rights and thus develop their own, attractive sports propositions, capable of competing at the wholesale and retail levels.

6.14. There is, therefore, a clear basis for concluding that Sky has a strong dynamic incentive to limit the wholesale distribution of its Sky Sports proposition, in order to protect its current strong market position in pay TV. This is not limited merely to protecting its premium sports subscribers and revenues from the outcome of effective competition, but is further reinforced by its incentives to protect its current 'buy-through' model, as well as wider benefits in adjacent communications markets such as in the provision of triple-play and broadband services (as discussed in Section 2).

6.15. Moreover, it is also reasonable to assume that Sky's dynamic incentives to limit the distribution of its Sky Sports proposition will necessarily vary with respect to different rivals. As Ofcom recognises, as a result of BT's considerable investment in BT Sport, Sky is likely to view BT in particular as a more serious threat to its market position,[404] as absent the limited distribution of the Sky Sports proposition, there is greater prospect of BT becoming a genuine challenger for sports rights over the long-term (providing a rivalry that Sky has not in practice previously faced). The fact that this is likely to be the case is borne out by Sky's actual conduct in practice, with more limited distribution of the Sky Sports proposition to BT than other rival operators as well as a targeted competitive response to BT's development of its sports offerings (see paragraph 4.47). For example, Virgin Media has access to the full Sky Sports proposition, and TalkTalk has access to all of the Sky Sports channels in SD. Neither retailer is a rival at the wholesale level, or in bidding for sports rights. In contrast, as regards BT, who is a rival at the wholesale level and does bid for rights:

(i) As set out in detail in Section 2, prior to the CAT ruling in November 2014 updating the IRO[405] BT had **no** supply of any Sky Sports channels on its primary, strategic platform.

[404] Consultation Document, paragraph 7.18.
[405] See footnote 96, on page 34, above.

(ii) Prior to the CAT ruling updating the Interim Relief Order (which Sky resisted before the Tribunal), Sky had prevented BT from having wholesale access to any Sky Sports channels on BT's YouView platform on fair and reasonable terms by seeking to impose the anti-competitive Grant-Back Condition as a pre-requisite for wholesale supply.[406] The Grant-Back Condition is a term that seeks to undermine any rival pay TV retailer's incentive and ability to compete in channel development and distribution, by allowing Sky to appropriate their upstream investment and maintain its market position.[407] The CAT determined that it was an inappropriate condition for Sky to seek to impose.[408]

(iii) Moreover, BT only has wholesale supply of the SS1 and SS2 channels on its YouView platform, and wholesale supply of SS1, SS2 and SS5 on its Cardinal platform, i.e. it does not have wholesale supply of the Sky Sports proposition. [✂].[409]

6.16. Sky has stated (although BT cannot verify) that all of its wholesale deals include similar terms to the Grant-Back Condition.[410] BT notes that, unlike BT, [✂] However, Sky's universal imposition of a Grant-Back term reinforces concerns as to Sky's incentives to limit the distribution of its Sky Sports proposition: it appears that Sky makes it a pre-condition that any rival who acquires premium sports rights, and creates a channel that may allow it to differentiate its retail proposition from Sky, is forced to wholesale that channel to Sky, or forego wholesale supply of the Sky Sports proposition. Therefore, as standard, Sky includes terms that undermine a rival's incentive and ability to bid against Sky for sports rights and develop their own sports channel, by ensuring that any retail rival who makes that investment will not be able to use it as a point of differentiation at the retail level.

<u>It is evident that Sky has limited the distribution of its Sky Sports proposition in practice</u>

6.17. While BT believes that it is instructive to consider Sky's incentives to limit the distribution of its Sky Sports proposition, as explained in Annex 1, consistent with competition law orthodoxy, Ofcom's analysis should focus on the objective, observable market outcome that limited distribution of the Sky Sports proposition is occurring and has had an impact on fair and effective competition in pay TV markets. Thus, an appreciation of the importance of the

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[406] Indeed, the economic model that BT commissioned Compass Lexecon to prepare referenced in Section 5 found that Sky's stipulation of the Grant-Back Condition [✂]

[407] In this regard it fits squarely in Ofcom's definition of limited distribution as set out at paragraph 7.3 of the Consultation Document.

[408] IRO, para 67: *"BT has spent some £1.5 billion acquiring football broadcasting rights in order to improve its position on the market and I do not see that BT should be required, in effect, to deprive itself of the competitive gain from that investment in order to achieve the benefit of the WMO remedy ordered by Ofcom"*.

[409] BT is currently in the process of requesting [✂]

[410] [✂]

Sky Sports proposition, Sky's market position, the observable fact of limited distribution of the Sky Sports proposition and the observable fact of a lack of fair and effective competition in pay TV markets provides a more than sufficient basis for Ofcom to intervene. When considering Sky's incentives, Ofcom is not required by s.316 Communications Act 2003 to consider whether Sky acted in a particular way out of any subjective, malign anti-competitive intent, i.e. Ofcom should avoid getting drawn into speculation as to Sky's intent and whether or not Sky "deliberately" limits the distribution of its Sky Sports proposition specifically to impede competition. It is sufficient for Ofcom to observe, on the basis of its economic analysis, that the limited distribution of the Sky Sports proposition is likely to have the effect of limiting the emergence of fair and effective competition.

6.18. As the evidence in Section 2 clearly demonstrates, limited distribution of the Sky Sports proposition has occurred (and continues to occur) in various forms. Sky limits distribution by: (i) charging wholesale prices that are too high to allow rivals to compete effectively; (ii) imposing terms and conditions for wholesale supply that are anti-competitive and/or limit a retailer's ability to compete effectively either at the retail level, or in other parts of the value chain (such as the Grant-Back Condition); and (iii) by reducing the value of the Sky Sports proposition it wholesales by restricting the range of channels it makes available and by not supplying essential additional services such as HD versions of the channels, and other add-ons that consumers view as important discussed in more detail in Section 8 of this Submission.

6.19. In addition to the evidence in Section 2, BT also notes the strength of evidence emphasising Sky's unwillingness to depart from wholesale rate-card prices that are too high to ensure fair and effective competition:

(i) Prior to the introduction of the WMO, Sky's practice in negotiating wholesale deals was that the price should be set at the cable rate-card level. In the Pay TV Proceedings, Sky confirmed that during negotiation discussions "*Sky sought to negotiate for rate card prices*"[411] and that "*Sky's view throughout the period of the wholesale negotiations with BT was that the appropriate price for a wholesale deal was the cable rate card price*".[412]

(ii) In subsequent negotiations with BT the only deviation from rate-card prices that Sky was willing to countenance was a penetration discount arrangement. However, Sky

[411] Third witness statement of Michael Darcey, paragraph 346 (non-confidential version).
[412] Third witness statement of Michael Darcey, paragraph (non-confidential version). See also the First witness statement of Michael Darcey (non-confidential version), paragraph 532 stating that Sky was "*prepared to offer to BT Sky's premium channels on a wholesale basis if no retail deal could be reached. Any such offer was, however, to be based on cable rate card prices*".

had discussed such an arrangement with Ofcom in 2007 in relation to commitments it might provide to enable an early resolution of Ofcom's Pay TV investigation.[413] Ofcom had concluded that penetration discounts of the sort proposed were insufficient to address its competition concerns and close the investigation because: "at *moderate levels of platform penetration the price that was on offer would not have enabled a retailer on DTT, with the scale that such a retailer would be likely to be able to achieve, to compete with Sky",* and because "*there was a high risk that this would effectively have turned [other retailers] into pure resellers of Sky's content…[which] would have been likely to reduce incentives to innovate".*[414] As such, the only form of discount from rate-card price that Sky was willing to offer to BT would equally have been insufficient to enable fair and effective competition.

(iii) Finally, Sky's subsequent pricing behaviour outside of the WMO regime demonstrates that Sky continues to seek rate-card prices ([✂].

6.20. It is, therefore, apparent that without regulation Sky has consistently been willing only to offer its channels at wholesale prices that would not allow fair and effective competition to emerge[415] (at least vis-à-vis BT), providing further evidence that Sky has limited the distribution of its Sky Sports proposition.[416]

<u>Conclusions on Sky's incentives to limit the distribution of its Sky Sports proposition</u>

6.21. In summary, BT considers that Ofcom can be much more forceful in its conclusions that Sky has a strong incentive to limit the emergence of competition through the limited distribution of its Sky Sports proposition:

(i) BT's analysis above demonstrates that in view of its market position and profitability, Sky has a static incentive to resist wholesale supply to other retailers (particularly smaller retailers) which is likely to generate insufficient revenue to offset a potential loss of retail revenue as Sky cannibalises its own market share.

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[413] The discussions are summarised in Annex 2 to the Pay TV Statement, "*Summary of discussions between Ofcom and Sky, late 2007 and early 2008*". Just as it had in its negotiations with BT, during these discussions Sky refused to consider the possibility of reducing its existing wholesale rate-card prices below the level then applied to its wholesale arrangement with Virgin Media.

[414] Pay TV Statement, paragraph 9.98

[415] However, as noted at paragraph 5.12 above, BT also has concerns that regulated WMO prices have been incorrectly set too high, due to flaws with the current WMO methodology, and that Sky has persistently taken advantage of deficiencies in the WMO pricing methodology. These errors have undermined the effectiveness of the current WMO remedy in terms of delivering fair and effective competition.

[416] Moreover, notwithstanding the CAT's findings that Sky was a "*willing wholesaler*", BT notes that prior to the imposition of the WMO Remedy, Sky had not concluded wholesale supply deals with either BT or Top-Up TV, despite repeated requests over a three year period.

(ii) More importantly, Sky has a powerful dynamic incentive to impede the emergence of effective competition at the retail level in order to preserve the vicious circle. Wholesale access to the Sky Sports proposition on terms that allow effective competition would be capable of driving subscribers towards rival platforms, which in turn would make vertically integrated rivals more likely to bid successfully in sports rights auctions, which, in the long-term, would diminish Sky's strength in pay TV markets.

(iii) Sky appears to have acted in line with such incentives: there is ample observable evidence of the limited distribution of its Sky Sports proposition impeding fair and effective competition, particularly with respect to BT where, absent the limited distribution of the Sky Sports proposition, there would be a greater prospect of BT becoming a genuine challenger for live sports rights in the future. Even with respect to retailers other than BT, there appears to be limited observable evidence that their terms of wholesale supply have led to a strong incentive to market or innovate around the Sky Sports proposition. Overall, as the evidence in Section 2 and Section 4 demonstrates it is clear that Sky is not effectively constrained.

BT has neither the ability nor the incentive to limit the distribution of BT Sport

6.22. BT notes Ofcom's erroneous suggestion that BT may "*have incentives not to supply TalkTalk with its channels so as to protect its own broadband base and to acquire customers from TalkTalk for its bundled pay TV/BT Sport/BT broadband product*"[417] and that "*This is reflected in BT's current supply arrangements where BT Sport is… unavailable on TalkTalk's YouView platform.*"[418] BT refutes these assertions for the reasons set out in detail below.

6.23. The evidence contained in Section 3 of this Submission clearly demonstrates that none of the BT Sport channels individually, nor when considered as a single package of channels, are necessary to ensure fair and effective competition. The evidence contained in Section 4 of this Submission shows BT's limited market position, with market shares that are significantly below the levels that could be expected to impact on competition.[419] As a result, the evidence in Section 5 makes clear that the limited distribution of BT Sport would not have the ability to impede fair and effective competition. The objective, observable market evidence also supports the fact that the presence or absence of BT Sport on a platform has no impact on fair and effective competition. In the circumstances, absent the ability to limit

[417] Consultation Document, paragraph 7.27.
[418] Consultation Document, paragraph 7.27.
[419] As set out in Section 4, BT notes that, for example, in the EU merger context there is a presumption that a market share below 25% is not liable to impede effective competition (para 32 of the EU Merger Regulation).

distribution in a manner that would impede fair and effective competition, further enquiry into BT's incentives is sterile: clearly there can be no incentive to limit distribution where there can be no effect from doing so.

6.24. Equally, BT's observable, objective behaviour demonstrates that BT has made its channels available on a wide range of platforms and on terms that do not impede fair and effective competition. This, in itself, provides compelling evidence that BT is incentivised to extend, rather than to limit, distribution of its channels. Nevertheless, BT addressees each of the assertions made by Ofcom with respect to its incentives to wholesale its BT Sport proposition in turn.

6.25. As Ofcom recognises,[420] BT has a strong static incentive to make its channels available on the Sky DSat and Virgin Media platforms. Equally, for the reasons set out in Section 5, (and contrary to Ofcom's assertion),[421] BT has no strategic incentive to limit the distribution of BT Sport on these platforms ([✂]):

(i) As discussed above (see paragraph 6.7), there is a strong likelihood that all those subscribers with a willingness to pay for premium sports channels at current market prices currently take Sky Sports. As the evidence in Section 3 shows, [✂]

(ii) In this regard, BT notes that there are currently [✂] subscribers on the Virgin Media platform with access to BT Sport, [✂] who get it free in the Virgin XL pack and [✂] who pay £15 per month. BT estimates that in the 2014/15 financial year, it will receive revenues from Virgin Media of [✂] for wholesale supply of BT Sport. Therefore, [✂]

(iii) Similarly, as set out in Section 2, Sky has an established base of approximately 5 to 6 million sports subscribers, with a high willingness to pay for premium sports channels. As the evidence in Section 3 of this Submission shows, [✂]

6.26. BT disputes Ofcom's assertion that it may be incentivised to refrain from supplying BT Sport to subscribers on the TalkTalk YouView platform. TalkTalk and BT's relative market positions and respective offerings confirm objectively that BT is, in fact, incentivised to supply BT Sport to TalkTalk:

(i) [✂] TalkTalk is primarily a broadband/telephony provider with a limited interest in pay TV and premium sports. As TalkTalk's Chief Executive, Dido Harding, has commented: "*In terms of its impact on our business, fundamentally we're just not in the premium sports game. The reality is if you want premium sports you're not going*

[420] Consultation Document, paragraph 7.40
[421] Consultation Document, paragraph 7.40.

to be a TalkTalk customer. We're not the right place for you to be and we're really relaxed about that. Our most frequently-watched on-demand content is Peppa Pig. That's our market, not people who want to spend a chunk of money on premium football matches."[422]

(ii) As the evidence in Section 3 shows, [✂] Moreover, TalkTalk subscribers have access to the Sky Sports channels and Sky basic channels on the TalkTalk platform: [✂]

(iii) As set out in Section 5, the fact that the presence or absence of BT Sport on TalkTalk's platform has no impact on take up of TalkTalk's pay TV offering, is empirically demonstrated by the relative speed with which TalkTalk's pay TV subscriber base has grown [✂] since the launch of BT Sport (see paragraph 5.16).

6.27. Ofcom suggests that the fact that a wholesale deal is not already in place with TalkTalk is evidence of BT's incentives to limit the distribution of its BT Sport channels to TalkTalk.[423] However, contrary to the impression given in the Consultation Document, BT has, in fact [✂]

(i) As BT has shown above, BT in fact does have a static incentive to supply BT Sport to TalkTalk on fair and reasonable terms. However, TalkTalk has less urgency in terms of its incentive to acquire BT Sport on such terms due to the profile of TalkTalk's customer base [✂].[424][✂].

(ii) TalkTalk's approach opens up further negotiating complexities for BT: [✂]

(a) [✂]

(b) TalkTalk has a retail subscriber base [✂][425]

(c) [✂]

(iii) Moreover, negotiations with TalkTalk have been against the backdrop of an impending regulatory review, [✂]:[426][✂].

6.28. For the reasons set out above, BT has neither the incentive nor ability to limit the distribution of BT Sport to any party, including TalkTalk.

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[422] http://www.telegraph.co.uk/finance/newsbysector/mediatechnologyandtelecoms/telecoms/10059930/TalkTalk-backs-Peppa-Pig-over-BTs-Premier-League-football.html

[423] Consultation Document, paragraph 7.41.

[424] [✂].

[425] [✂].

[426] [✂].

6.29. Finally, BT notes that even if, contrary to the detailed evidence set out in Sections 2 to 6 of this Submission, Ofcom was to conclude that BT does have both the ability and incentive to limit the distribution of BT Sport to TalkTalk in a way that would impede TalkTalk's ability to compete, this in itself would still not justify regulation of BT Sport. Ofcom's focus must be on the competitive process itself, not on the ability of individual competitors to compete.

6.30. In this regard, BT notes and agrees with Ofcom's view that if BT **were** to limit the distribution of its BT Sport channels (which it does not do), "*The small impact on static competition from limited distribution of BT's key sports content could therefore be offset if BT is able to establish itself as a more effective competitor [to Sky].*"[427] As Ofcom appears to recognise,[428] if BT **could** strengthen its position by adopting a strategy of limiting the distribution of BT Sport, the overall dynamic impact on the competitive process would likely be beneficial in the long run, in light of Sky's entrenched market position. However, for the reasons set out in Sections 2 to 6, such analysis is merely theoretical, as BT has neither the incentive nor ability to limit the distribution of BT Sport in a way that would impede any pay TV operator's ability to compete, including TalkTalk.

[427] Consultation Document, paragraph 8.21.
[428] Consultation Document, paragraph 6.69.

7. COMMERCIAL PREMISES MUST FORM PART OF THIS REVIEW

7.1. In the Consultation Document, Ofcom states that it has not included commercial supply (e.g. the supply to pubs and clubs) within the scope of this review, and that it does not expect any regulation to include this type of supply.[429] In order to support this position Ofcom appears to rely on its statement in the Pay TV Statement that it "*had not seen any evidence of limited distribution of premium sports content in this sector and we considered that the nature of competition for this type of supply was different to residential supply".*[430] It is not clear what evidence Ofcom has evaluated in order to reach this conclusion, since none is presented in the Consultation Document. In any event, while BT accepts that the nature of competition for commercial supply is different to residential supply, Ofcom has failed to grapple with the fact that there is an intrinsic link between commercial supply and competition concerns in residential markets, which BT explains in detail below.

Commercial supply cannot be divorced from the competition concerns in residential markets

7.2. In Section 4 of this Submission, BT set out in detail the vicious circle, which explains Sky's bidding advantages arising from its large installed base of subscribers with a high willingness to pay for Sky Sports. In addition to these advantages that Sky derives from its **residential** subscription base, Sky also derives a material bidding advantage from its large installed **commercial** subscriber base. Specifically, as a result of the fact that Sky does not face effective competition in the commercial sector, it enjoys the security of a significant retail revenue stream of around £[✂][431] per annum from pubs and clubs that take Sky Sports. In contrast, over 18 months after the launch of BT Sport into a number of commercial premises, BT has [✂] of Sky's commercial revenue stream (£[✂]),[✂] This gap in commercial revenues provides Sky with a lucrative revenue stream that it can use to underpin its bids for live sports rights, further reinforcing Sky's existing bidding advantages. As a result of these bidding advantages, Sky can systematically and on average outbid its rivals, which in turn bolsters Sky's strong market positions at the retail and wholesale level in the residential pay TV market.

7.3. As such, it is impossible to divorce Sky's bidding advantages resulting from the lack of effective competition that it faces in the commercial sector from the competition concerns that Ofcom has focused on in the residential sector. Any steps that Ofcom puts in place to unwind the vicious circle in relation to the residential sector will be undermined if Ofcom fails also to factor in Sky's bidding advantages arising from its position in the commercial sector. Since the WMO remedy has been ineffective to date (as evidence by the data on

[429] Consultation Document, paragraph 8.10.
[430] Consultation Document, paragraph 2.8, footnote 12.
[431] Based on BT internal estimates.

Sky's profitability in Section 2 and its market shares in Section 4), it is incumbent on Ofcom to consider and address all aspects of Sky's bidding advantages, including those arising from the commercial sector.

An analysis of the commercial sector shows that for the majority of commercial premises, Sky acts independently of competitive pressures from BT Sport

7.4. The commercial sector comprises pubs, clubs, hotels, leisure facilities, licensed bookmakers and a range of other licensed and unlicensed premises. In total this accounts for approximately £222 million in revenues per year, covering 45,000 individual properties. Within the commercial premises sector, BT has focussed on Sky's bidding advantages arising in the supply to pubs,[432] as this accounts for the vast majority (73%) of the total annualised value[433] (and 57% of total volume[434]) of licensed premises as a whole.

7.5. Based on BT's experience of the commercial premises sector since August 2013, the range of sports pubs can be broken down into the following three distinct segments, which face different conditions in determining their pay TV sports subscription decisions:

(i) **National Pubs with Sports**: These are outlets owned by national pub groups,[435] which are interested in showing a full range of sports content (in particular, all the Premier League matches) and therefore take BT Sport in addition to their existing Sky Sports subscription. In the financial year 2014/15, BT estimates that this portion of pubs accounted for approximately [✂]% of the total annualised value generated from pubs. In addition:

(a) They are typically publicly limited or private equity-backed companies that aspire to homogeneity at outlet level in order to ensure a consistent customer offering and drive cost savings through economies of scale and scalability.

(b) They have centralised branding, marketing and finance functions which take all necessary strategic decisions: (i) to ensure a consistent customer proposition across outlets; and (ii) based on their assessment of the most profitable market segmentation, whether to focus on food/alcohol/sports

[432] A "pub" for these purposes is as defined by the U.K. Valuation Office Agency for business ratings (https://www.gov.uk/government/organisations/valuation-office-agency). There are currently approximately 16,000 pubs in the UK.

[433] The estimated total annualised revenue generated by subscriptions in commercial premises (without regard to the size or the rateable value of individual premises).

[434] The estimated total number of Sky Sports and BT Sport subscriptions taken by commercial premises.

[435] Not all pubs within a given national group will take football, but football pubs will typically share the characteristics set out in paragraph 7.5(i).

sales (or any combination of these three). Approximately [✂]% choose to take sports. Thus, in order to achieve a consistent customer experience, they will operate a centralised customer proposition and where appropriate overall regional variations.

(c) For national pubs that take sports, the centrally managed aspects of the customer proposition will also include decisions around which pay TV sports subscriptions are taken up (namely, Sky Sports or Sky Sports plus BT Sport) and to which pubs this will apply.

(d) In order to ensure they have a full consumer proposition, those pubs within a national pub group that are designated to be sports pubs will typically wish to show the full range of sports available in order to offer a "full" sports proposition. As a result, [✂].[436][✂]%.

(ii) **Sports Pubs**: These are outlets owned by regional pub groups and independent pubs, which take Sky Sports and may also chose to take BT Sport depending on affordability. This is by far the largest market segment, and in the financial year 2014/15, BT estimates that this portion of pubs accounted for approximately [✂]% of the total annualised value generated from pubs. Sky retains material advantages over BT in this market segment:

(a) These pubs are typically owner-or lessee occupied with decisions around branding and marketing being taken at an outlet level (rather than by a centralised team as in the case of the National Sports Pubs). They will typically have a fixed budget.

(b) These pubs face a choice as to whether to take Sky Sports, BT Sport or both. [✂][437][✂].

(c) Given the more [✂]

(iii) **Sports Lite Pubs**: These are pubs which previously did not take Sky Sports (or had cancelled their subscription at some point in the past),[438] but have now chosen to

[436] It is worth noting that despite the fact that Sky previously retailed both Sky Sports and ESPN to these pubs, when it ceased to retail ESPN, and BT Sport entered the market, Sky continued to charge these pubs the same price, and in August 2014 increased its price again by 5.5%. (Source: "Sky Business announces 5% price increase, Morning Advertiser, 12 June 2014, available at: http://www.morningadvertiser.co.uk/General-News/Sky-Business-announces-5-price-increase).

[437] Since demand for sports propositions in pubs is largely derived from consumer preferences, the analysis set out in Section 3 as to the relative strength of the Sky Sports proposition equally applies here, though may be somewhat more events driven.

take BT Sport [✂] In the financial year 2014/15, BT estimates that this portion of pubs accounted for approximately [✂]% of the total annualised value generated from pubs.

(a) They are price-sensitive sports-focused pubs, where sport can provide part of the proposition, generally owned by regional groups and independent pubs, but operated by sole traders based in the pub.

(b) [✂]

(c) They do not have a current subscription to Sky Sports – they place some positive value on TV sports entertainment, yet this valuation does not exceed the price for Sky Sports. [✂]

7.6. It is clear from the evidence set out above that Sky continues to enjoy material advantages in the commercial sector in terms of [✂]. It is these [✂] revenues that underpin its bidding advantages for live sports rights described above.

7.7. In order to address this problem, BT believes that, at a minimum, Ofcom should take into account commercial revenues in assessing the competition issues in pay TV, and devising the remedy required to address those problems. Ofcom should also consider whether it is necessary to regulate wholesale supply of Sky Sports within the commercial sector as this would allow BT to innovate in terms of pricing, packaging and bundling of sports subscriptions in this sector which would open the door for increased competition with Sky and would start to redress the imbalance in bidding for sports rights resulting from the current lack of competition in the commercial sector.

Ofcom's reasons for omitting the commercial sector from its review are not sound

7.8. As discussed above, Ofcom has not set out its reasoning for omitting the commercial sector from its WMO review, other than to rely on its exclusion in the Pay TV Statement.[439] However, examining Ofcom's reasons in the Pay TV Statement shows that they are not applicable to BT's concerns set out above as to the inter-linkages between the commercial sector and the residential sector:

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[438] While these pubs may have subscribed to Sky Sports at a point in the past, there has been no substitution in this segment of Sky Sports for BT Sport, as by definition these pubs did not have any pay TV sports subscription immediately before the launch of BT Sport – thus there could be no switching to BT Sport.

[439] The fact that this is a review of the current WMO remedy is equally not a valid reason, since Ofcom has included a wide range of new market factors in the current review that were not part of its assessment in the Pay TV Statement.

(i) **Nature of competition:** Ofcom previously observed that competition in commercial premises focussed on "*the price of standalone sports rather than pricing and innovation across wider bundles*"[440] and "*[u]nlike the residential market, the market for commercial supply features limited scope for innovating around premium content.*"[441] However, there is no reason why this should be the case. Competition in commercial premises can incorporate innovation around the nature of the sports bundle provided, as well as around wider bundles of products (including broadband and telephony). BT understands, for example, that Sky has offered bundled Wi-Fi with its sports offering for the last two years. Ofcom's assumption that the business model would be based purely around resale of content is not supported. In any event, more effective price competition should be a sufficient basis for Ofcom to consider this matter, particularly in light of the importance of this revenue stream when bidding for rights.

(ii) **Lucrative pricing:** Ofcom also stated that "*Another focus of respondents' objections fell on the lucrative commercial revenues relating to commercial supply. […] a broadcaster argued that the highly lucrative commercial market is a key cornerstone of Sky's premium revenues, and thus of its ability to dominate the consumer market for premium sports content. However, we do not believe that lucrative commercial revenues are a substantial reason for intervention, as we are not intervening to remove Sky's market power itself, or to address concerns related to levels of pricing, only to ensure that restricted wholesale supply does not prevent effective competition.*"[442] As set out above, BT's concerns do not relate to Sky's pricing levels in the commercial sector in and of themselves, but rather the consequence of Sky being permitted to retain a lucrative revenue source that it can use to underpin its bid for live sports rights, reinforcing Sky's bidding advantages. However, BT notes that, as the competition regulator, a lack of effective competition in the commercial sector ought to be a concern for Ofcom, particularly if this results in high prices for consumers (in this case publicans, and ultimately their customers). Therefore more effective price competition should be a sufficient basis for Ofcom to consider this matter, particularly in light of the importance of this revenue stream when bidding for rights.

(iii) **Reason for intervention:** Finally, Ofcom explained that it believed it would only be justified to intervene in relation to commercial premises if it was appropriate for ensuring fair and effective competition but that "*we do not see evidence of restricted*

[440] Pay TV Statement, paragraph 1.55.
[441] Pay TV Statement, paragraph 9.225.
[442] Pay TV Statement, paragraph 9.229.

wholesale supply to commercial premises and we do not believe a wholesale must-offer obligation is the appropriate means to address any concerns regarding high retail prices. As a result, we consider the most appropriate response in these circumstances is to include consideration of commercial supply in any future assessment of the sale of Premier League rights under CA98."[443] As explained above, BT's primary position is to ensure that Ofcom appropriately takes into account, as part of this review, the large, unchallenged revenue source that Sky uses to underpin its bidding for sports rights, and reflects this when devising the remedy required to address the identified competition problems. This is an issue with ensuring fair and effective competition in residential markets in the long-term and therefore sits squarely within Ofcom's s.316 powers rather than a CA98 investigation.[444] In addition, BT notes that Ofcom's 2010 analysis is not correct: there is no wholesale supply to commercial premises (supply is presently on a direct retail basis only), and as a result of the high prices that Sky is able to charge, distribution to pubs is more limited than it would be in the event Sky faced effective competition in the commercial sector. BT believes that packaging (and pricing) innovation in this sector would be in the best interests of consumers.

7.9. For these reasons, BT does not accept Ofcom's provisional assessment that supply to commercial premises should be excluded from the scope of the WMO Review. BT requests that Ofcom reconsiders this matter in order to ensure that the outcome of the current review delivers fair and effective competition.

[443] Pay TV Statement, paragraph 9.230.
[444] Moreover, BT notes that despite making this statement in 2010, Ofcom has not undertaken a CA98 investigation to consider the other issues raised.

8. BT'S CONCLUSIONS AND VIEWS ON THE NEXT STEPS IN THIS REVIEW

8.1. In this section, BT summarises the conclusions arising from the evidence and analysis contained in Sections 2 to 7 of this Submission. BT also provides some preliminary remarks on next steps in terms of the scope and form of the regulation required.

BT agrees with Ofcom's conclusions, though they are expressed more tentatively than the evidence warrants

8.2. In its final conclusions, Ofcom states that "*In light of our view that there may be circumstances in which Sky has incentives to engage in such practices, and our assessment of the impact of such practices being engaged in, we believe it may be appropriate to maintain regulation on Sky with the objective of ensuring fair and effective competition.*[445] For the reasons set out in detail in this Submission, it is clear that there are compelling reasons why Ofcom's review needs to focus on the appropriate regulation of the Sky Sports proposition, and should not focus on BT Sport. BT summarises its conclusions, based on the supporting evidence in this Submission, below.

8.3. BT has established in Section 2 of this Submission that market developments since the introduction of the WMO remedy in 2010 demonstrate clearly that fair and effective competition has not emerged. In fact, Sky's position in terms of retail subscriber numbers (both in total and in terms of premium sports subscribers), profitability, and control of live sports rights, has strengthened rather than weakened. Moreover, as a result of the lack of fair and effective competition in pay TV markets, problems are spilling over into adjacent markets, such as in the provision of broadband and triple-play services.

8.4. A major reason for the strengthening of Sky's market position was Ofcom's failure to impose regulation in 2010 that addressed the source of Sky's market strength, which stems from the Sky Sports proposition. For the reasons set out in detail in Section 3 of this Submission, it is imperative that Ofcom does not repeat this error. However, BT has explained that Ofcom's theoretical exercise identifying the importance of individual sporting events in isolation, which is divorced from the reality that live sporting events are sold collectively in premium sports channels and packages of premium sports channels, will fail to address the core issue as to the scope of the regulation necessary to ensure fair and effective competition in pay TV markets going forward. BT has explained why it is essential that Ofcom's product analysis

[445] Consultation Document, paragraph 8.8.

focuses on premium sports channels and packages of sports channels. Correctly analysed on this basis it is evident that the Sky Sports proposition (and not a subset of this proposition) is necessary for rival pay TV retailers to be able to compete effectively.

8.5. BT has explained in detail that Sky currently enjoys a high market share, typically associated with dominance, at both the wholesale and retail level and has material incumbency advantages at the retail level and when bidding for sports rights (see Section 4). The limited distribution of the Sky Sports proposition (either by not providing access at all, or by providing access only on terms that do not permit effective competition) materially impedes fair and effective competition (see Section 5). In Section 6 of this Submission BT has also explained that Sky has a strong incentive to limit the distribution of its Sky Sports proposition, in order to protect its strong market position (and consequent high profitability) across the pay TV value chain. This incentive is strongest vis-à-vis rivals such as BT, which, as a result of its considerable investment in BT Sport, is likely to be viewed by Sky as a more serious threat to its market position. Therefore, Sky has both the ability and incentive to impede fair and effective competition through the limited distribution of its Sky Sports proposition. Moreover, the objective, observable market outcome is clear that limited distribution of the Sky Sports proposition is occurring and has had an impact on fair and effective competition in pay TV markets.

8.6. BT also notes Ofcom's conclusions that "*[o]verall, we are not satisfied that the impact of limited distribution of BT's key content is sufficient to give rise to concerns at this point in time. Given the uncertainty around the impact of limited distribution of its key content (based on its current sports rights holdings) and its relatively recent entry into the market, we are not minded at the current time to consider imposition of a remedy on BT.*"[446] For the reasons set out in this Submission, Ofcom's conclusions with regard to BT are unduly tentative.

8.7. Contrary to Ofcom's assertions, the evidence in Section 3 of this Submission shows that BT Sport (even when it includes Champions League rights) is insufficient to drive pay TV subscriber's platform switching decisions. Section 4 demonstrates that BT's market shares are at a level where it does not have the ability to impact on competition, and as a result Section 5 shows that even if BT were to limit the distribution of BT Sport (which it does not)

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[446] Consultation Document, paragraph 8.22.

it would not have the ability to impede fair and effective competition as a result. Consequently, as Section 6 establishes, BT has neither a static nor dynamic incentive to limit the distribution of BT Sport even to smaller platforms such as TalkTalk's YouView platform. However, BT agrees with Ofcom's view that if BT **were** to limit the distribution of its BT Sport channels to TalkTalk (which it does not do), "*The small impact on static competition from limited distribution of BT's key sports content could therefore be offset if BT is able to establish itself as a more effective competitor [to Sky].*"[447]

8.8. There is, therefore, no evidential or legal basis for regulating BT Sport and it would be unlawful of Ofcom to do so. Ofcom should not, therefore, spend time unnecessarily analysing BT Sport, but rather must focus on Sky Sports as the sole source of barriers to fair and effective competition.

Next steps: the scope of the remedy required: regulation of the full Sky Sports proposition

8.9. Going forward, BT believes that it is essential not only that the WMO remedy is maintained, but that it is made fit for purpose. BT understands that Ofcom is not, at this stage, consulting on the nature or design of any potential remedy, and that Ofcom has merely set out its high level views on the next steps for assessing these issues. Ofcom highlights that a critical next step in the WMO Review is to determine the question of the scope of any intervention going forward. BT agrees that this is an essential first step. As set out above, BT firmly believes that one of the key reasons why the WMO remedy has been ineffective to date is because Ofcom failed to appropriately determine the necessary scope of regulation in 2010, and as a result limited its intervention to the regulation of SS1 and SS2. Far from achieving the results that Ofcom intended in 2010, the WMO has been impotent in addressing the competition problems that persist across the pay TV value chain. BT believes it is essential that this error is not repeated.

8.10. While BT understands that issues of scope are to be determined in the next phase of the WMO Review, it nonetheless sets out its views on the preliminary matters that Ofcom has raised.

8.11. **Which sports channels would be included in the obligation**: Ofcom states that its *"current view is that Premier League and Champions League represent key sports content and therefore we may consider an approach which links the regulation to the channels on which*

[447] Consultation Document, paragraph 8.21.

this content is shown."[448] BT has examined the issue of which sports channels it would be necessary to include within a regulatory obligation in detail in Section 3, and does not reiterate these arguments here. However, the conclusions from that analysis are clear: Ofcom must ensure that the full Sky Sports proposition should be made available on terms that allow fair and effective competition going forward. In practice, this means extending the prospective regulation to SS1, SS2, SS3, SS4, SS5, F1 and SS News HQ[449]. In addition, for the substantive reasons set out in Section 3, and in light of the evidence of Sky's past gaming of its regulatory obligations (see paragraphs 3.42 to 3.59) any regulatory obligations should also extend to any future sports channels that Sky creates and bundles with its existing Sky Sports proposition.

8.12. **What other services should be within scope**: Ofcom states that *"The WMO includes both SD and HD versions of SS1&2 although with more limited obligations for HD. We would need to consider whether any distinction between SD and HD remained appropriate*"[450] and "*The WMO covers the key sports content shown via the red button associated with SS1&2 channels. We would need to consider whether this remains appropriate and the extent to which any new services might also fall within the regulation*."[451]

8.13. Again, BT reiterates that it is necessary to ensure that the full Sky Sports proposition is made available on terms that ensure fair and effective competition: this includes HD and interactivity. As Ofcom has recognised in its Consultation Document, limited distribution includes providing wholesale supply but in a way that reduces the value of the regulated product to consumers. The Sky Sports channels in SD or without red button content and services would clearly be inferior to the Sky Sports proposition retailed by Sky. As a result, wholesale access that does not include these aspects of the Sky Sports proposition would materially reduce the value of the Sky Sports product that a rival retailer was able to offer to consumers. Consumers now expect to have access to channels, particularly sports channels, in HD, and it is essential that rivals are able to meet these expectations. Moreover given the past evidence of Sky's gaming of its regulatory obligations there would be a material risk that excluding interactive services would provide scope for Sky to undermine the efficacy of the remedy by shifting content behind the red button.

8.14. As Ofcom notes, under the current WMO regulation, the current HD and interactive obligations merely require Sky to offer these services on FRND terms, with no specific regulated price. In 2010, HD was still in its infancy, and so Ofcom determined that this was

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[448] Consultation Document, paragraph 8.9.1.

[449] Although SS News HQ is not a premium sports channel per se, for the reasons set out in Section 3, it plays a vital role in stitching the rest of the Sky Sports proposition together.

[450] Consultation Document, paragraph 8.9.2.

[451] Consultation Document, paragraph 8.9.3.

an appropriate approach "*because high-definition is a relatively recent innovation and there is a degree of uncertainty as to the appropriate approach to setting a price.*"[452] In the case of interactivity, more practical considerations drove Ofcom's approach, namely that there were additional, retailer specific technical requirements (and hence costs) to delivering red button services.

8.15. According to Ofcom's 2014 Infrastructure Report, the penetration rate of HD TV has now reached 69% of households[453] and there are now a large number of HD channels (including all the PSBs) broadcast in the UK.[454] It is clear that HD is now no longer in its infancy, and so any uncertainty around its importance, take-up rates or associated marketing costs no longer exists, allowing a regulated price to be set correctly. Given the increased prevalence and importance of HD services since Ofcom's 2010 Statement, particularly for sports subscribers, BT believes that there is no longer any cogent basis for differential regulation of the SD and HD versions of the Sky Sports channels, and it is appropriate and proportionate to extend regulation to the wholesale price of Sky Sports in HD.

8.16. For similar reasons, BT also believes that such a remedy should also extend to the ability to provide access to Sky Sports via multi-devices within home (i.e. a rival retailer should be able to provide access to Sky Sports via a TV, laptop, tablet, etc with a single subscription, similar to Sky Go), and (as is the case today) multi-room.[455] Again, large portions of consumers now expect this functionality, and an inability to offer it would reduce the value of the product to consumers. Although these services may only have small subscriber bases today, they have the capacity to become considerably more important over the next three years – as was the case for HD (i.e. before Ofcom is likely to review any remedy again).

8.17. In designing a remedy, it is fundamental that it is able to reflect the prevailing market conditions and is 'future-proofed', insofar as possible, to avoid it becoming obsolete shortly after its implementation. Therefore, Ofcom must also ensure that any remedy adequately incorporates an ability for other developments such as versions of Sky Sports channels to be accommodated within the construct of any remedy (without the need for a fundamental review of the scope of the remedy first to be conducted).

8.18. **Which pay TV platforms would be eligible to request supply:** Ofcom states that "*We have explained in Section 6 that our assessment is focussed on competition between pay TV*

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[452] Ofcom Pay TV Statement, paragraph 1.55. In particular, Ofcom cited the difficulties of correctly allocating marketing costs to a product in its first growth stage (paragraph 9.282).

[453] Section 6 (http://stakeholders.ofcom.org.uk/binaries/research/infrastructure/2014/IR_6.pdf).

[454] There are 73 HD channels available on Sky's DSat platform according to its website (http://www.sky.com/products/ways-to-watch/sky-plus-hd/).

[455] However, for the reasons set out in BT's appeal, multi-room should not be automatically included in the baseline wholesale price.

platform retailers (i.e. Sky, BT, TalkTalk, Virgin Media and any other new entrants with similar services) and not OTT retailers. This would therefore appear to be the appropriate focus for any regulation but we would need to consider this further."[456] For the reasons set out in paragraph 2.63 BT does not believe that the inclusion or exclusion of OTT retailers would alter Ofcom's competition analysis.

8.19. In BT's view, a far more important question is the fact that in 2010, Ofcom determined that the WMO remedy would not be applicable to Sky's DSat platform, notwithstanding the existence of the Technical Platform Services regime,[457] which allows rival retailers to retail directly to consumers using Sky's set-top boxes. The basis for this exclusion in 2010 was unclear. In principle, if the WMO remedy also applied to Sky's DSat platform, it would be open to a third party retailer to provide Sky Sports (and packages including Sky Sports) directly to Sky's installed retail subscriber base. Given the low levels of switching in pay TV markets (see paragraph 4.42), Ofcom must consider the possibility of allowing rivals to sell Sky Sports on regulated terms directly to Sky's sports subscribers on the satellite platform in order to more swiftly deliver the benefits of retail competition to consumers.

8.20. BT also notes that Ofcom states "*[a]s outlined in Section 2 we have not included supply for onward retail to commercial premises (e.g. pubs and clubs) within the scope of this review. Therefore we would not expect any regulation to include this type of supply.*"[458] For the reasons set out in detail in Section 7 of this Submission, BT does not believe that it is possible to consider and address the issues with fair and effective competition in retail pay TV markets, without also considering certain aspects of the commercial sector. In particular, Ofcom must reflect the fact that Sky's commercial premises revenues afford it an unchallenged, lucrative revenue source that it can use to underpin its bids for live sports rights, further underscoring Sky's bidding advantages for live sports rights.

8.21. Again, in order to ensure any remedy is future-proofed, BT believes that it is necessary that it is designed with sufficient flexibility so as to cover new technological developments in platforms and distribution.[459]

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[456] Consultation Document, paragraph 8.9.4.

[457] See Provision of Technical Platform Services Guidelines and Explanatory Statement, published 21 September 2006 (***http://stakeholders.ofcom.org.uk/consultations/tpsguidelines/statement/***).

[458] Consultation Document, paragraph 8.10.

[459] BT recognises that issues with wholesale supply to BT's YouView platform arose primarily due to limitations in the original IRO, but that process makes clear that if future delivery technologies are not adequately covered by the remedy, Sky will be able to use such limitations to limit the distribution of its Sky Sports proposition in a way that impedes fair and effective competition.

Next steps: the form of the regulation required: wholesale access on specified terms

8.22. BT notes Ofcom's preliminary assessment that there are two broad approaches that might be adopted to target the practices that it has identified that impede fair and effective competition. These are: (i) an access requirement to make content available on competing retail pay TV platforms either via wholesale or self-retail arrangements; and (ii) an obligation to offer the regulated product on specified terms.[460] BT also notes that Ofcom states "*If we do not identify practices which may be prejudicial to fair and effective competition, we will remove the existing WMO regulation.*"[461]

8.23. Ofcom does not set out any discussion on these possible options at this stage, and BT understands that these are questions for the next phase of the WMO Review. Therefore, at this stage, BT makes only limited, preliminary observations.

8.24. BT strongly believes that any access obligations without terms (including prices) being pre-specified will risk being, or becoming, ineffectual.[462] This is based on the evidence set out in this Submission demonstrating Sky's incentive and ability to limit distribution by: (i) offering prices that do not allow rivals to compete effectively; and (ii) imposing terms,[463] such as the Grant-Back condition, which undermine a rival pay TV retailer's incentive and ability to compete in channel development and distribution.

8.25. Equally, in order to be effective, any remedy must take the form of a requirement for Sky to provide <u>wholesale</u> access to the Sky Sports proposition (on specified prices and terms). In this regard, BT notes Ofcom's suggestion that Sky self-retailing, where technically possible, might be considered as a potential remedy. However, while BT does not consider that self-retailing is intrinsically problematic per se, in the case of Sky Sports it would be an ineffectual solution to the competition problems that Ofcom has identified, which stem primarily from Sky's strong market position, vast retail incumbency advantages and consequent material bidding advantages. It is unclear how a solution based around Sky self-retailing the Sky Sports proposition could be expected to address these issues when self-retail would effectively entail Sky 'competing' with itself across multiple platforms at the retail level and displacing the platform retailer from key elements of the customer relationship. In particular:

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[460] Consultation Document, paragraph 8.12 to 8.14.
[461] Consultation Document, heading paragraph 8.18.
[462] It is important to note that the reason that Ofcom's WMO remedy has failed to deliver fair and effective competition to date is not necessarily due to the structure of the remedy itself but rather issues to do with scope (as discussed above in Section 4) and errors in the methodological application (as set out at paragraph 5.12 of this submission).
[463] BT also notes that even when required to provide its channels on regulated terms, Sky still imposes terms that restrict fair and effective competition [✂]

(i) Absent additional regulation, it cannot be expected that the retail prices that Sky would set for Sky Sports on a rival's platform would be at a level that would be likely to compete effectively with Sky's own DSat prices. To do so would risk cannibalising Sky's own DSat subscriber base by incentivising switching to the rival's platform. This pricing concern is likely to be even more acute since Sky will also seek to protect its incremental revenue streams from Sky Sports day and week passes on NOW TV. Consequently, the likelihood that absent regulation Sky would set a retail price on a rival's platform that allowed that rival to compete effectively for premium sports subscribers (or pay TV subscribers generally) is very low.

(ii) Equally, it would be unlikely that merely requiring Sky to self-retail on rivals' platforms would facilitate package and bundling innovation on those platforms capable of incentivising switching to rivals' platforms. In particular, since prices would be subject to change by Sky on a reactive basis to rivals' propositions, Sky would be in a position to undermine any such innovation to the extent it created effective competition for its own retail proposition (either on its DSat platform or via NOW TV).

(iii) Finally, a remedy built around self-retailing would enable Sky to create a direct contractual relationship with rivals' customers. While such relationships are not necessarily an issue per se, in light of Sky's control over pricing and bundling, as well as its substantial retail incumbency advantages (particularly due to its scale and marketing advantages discussed at paragraphs 4.31 to 4.48 above), Sky would be in a strong position to persuade its rivals' customers to switch to Sky's own DSat or NOW TV offerings.

(iv) As such, rather than resulting in fair and effective competition, a remedy based around self-retail may risk further entrenching Sky's strong market position.

Regulation of the Sky Sports proposition would be proportionate

8.26. BT notes Ofcom's statement that "*[i]n considering whether regulation is appropriate to ensure fair and effective competition in the provision of retail pay TV services, we will also need to make an assessment about the proportionality of any remedies*".[464] BT also notes the factors that Ofcom has said it will consider in order to assess proportionality.[465] Based on the evidence contained in this Submission, BT believes that regulated wholesale access to the Sky Sports proposition would be a practical and proportionate remedy, that meets the

[464] Consultation Document, paragraph 8.15.
[465] Consultation Document, paragraph 8.16.

criteria Ofcom has set out, and would deliver material benefits to consumers both in pay TV, and in wider communications markets.

8.27. In the time that Ofcom has been working on pay TV issues since the original complaint at the beginning of 2007, the regulatory regime in pay TV has been proven to be ineffective and unbalanced relative to regulation in fixed telecommunications. In that time, Sky has gone from being a new entrant in fixed telecoms to having the second largest share in the market, primarily by bundling its irreplicable pay TV content with broadband services. As a result of the highly effective wholesale regulatory interventions in broadband, Sky's retail broadband subscriber numbers have grown from 716,000[466] in 2007 to 5.4 million in 2015.[467] BT has no ability to differentiate its downstream retail broadband products as a result of differentiated wholesale products because all CPs access the same wholesale products.

8.28. In contrast, Sky is permitted systematically to limit the wholesale distribution of its Sky Sports proposition, to price it in a manner that restricts retail competition, and to discriminate between rivals, particularly to BT's disadvantage. As a result, despite regulatory intervention, BT's retail subscribers to Sky's regulated sports channels have gone from zero to [✂] thousand over the period 2010 to 2015 while Sky's wholesale and retail market positions have strengthened overall. This does not amount to any substantial impact to promote fair and effective competition despite 8 years of effort from Ofcom.

8.29. The time has come for Ofcom to deal with the imbalance and ineffectiveness of the pay TV regulatory regime properly and put all players in an increasingly converging triple-play space on to a level playing field.

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466 Based on BT's internal tracking of Sky's published quarterly data for Q1 2007/08.

467 Based on BT's internal tracking of Sky's published quarterly data for Q3 2014/15.

ANNEX 1: LEGAL AND ANALYTICAL FRAMEWORK

1. Notwithstanding that the WMO continues to be the subject of litigation, BT agrees with Ofcom[468] that both the CAT and Court of Appeal have made clear that Ofcom has the power under section 316 of the Act to impose a remedy such as the WMO in order to ensure fair and effective competition in the provision of relevant licensed services.[469]

2. BT submits that there are four main considerations concerning the applicable legal framework and the manner in which Ofcom should exercise its powers under section 316. These are in addition to recognised public law requirements.[470] In BT's view, taking into account these factors will assist Ofcom in ensuring that it properly exercises its powers under the Act, and that the conclusions reached in the course of the present review are duly reasoned, reasonable and robust.

The need for an orthodox analytical approach

3. BT considers that, where Ofcom has identified a potential impediment to fair and effective competition for the purposes of section 316 of the Act (such as, in the present context, the limited distribution of relevant content[471]) it is necessary to ensure the proportionality of any remedy ultimately imposed. In order to do so, BT believes that Ofcom must adopt an orthodox analytical approach, which means that Ofcom should consider the following factors (or explain why it has not done so):

    i. the characteristics of the relevant economic product market or market(s);

    ii. an examination of the market position of parties active on each relevant market; and

    iii. in light of those market positions to consider whether any party has both the ability and incentive to prevent, restrict or distort fair and effective competition and if so, whether regulating that party would ensure fair and effective competition.

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468 Consultation Document, paragraph 2.5.

469 BT also agrees that given the ongoing need for "*a comprehensive solution to a general problem affecting the relevant markets*" (to use Ofcom's formulation at paragraph 9.8 of the Pay TV Statement), it would not be more appropriate in this case for Ofcom to use its Competition Act powers, rather than proceed under section 316 of the Act.

470 Ofcom, of course, acknowledges the public law constraints under which it operates through its regulatory principles, even in the context of an initial consultation. Of particular relevance for these purposes is BT's expectation that Ofcom will, per its fourth regulatory principle, "*ensure its interventions will be **evidence-based, proportionate, consistent**, accountable and transparent in both **deliberation** and outcome*" (emphasis added)

471 Consultation Document, paragraph 1.6.

4. In BT's view, an assessment of these factors is necessary for an appropriately structured analysis under section 316 of whether impediments to fair and effective competition exist (and, if so, the need for, and scope of, any regulatory intervention).

5. Indeed, BT observes that in its previous Pay TV review, Ofcom correctly undertook what it described as an "*orthodox competition analysis*"[472] under section 316 by first defining the relevant markets, then considering Sky's market position and market power, and then considering Sky's ability and incentive to act in a manner that was prejudicial to fair and effective competition.[473] BT believes that Ofcom must again carry out its assessment on this basis and a failure to do so would depart from what Ofcom has previously accepted is the orthodox approach, and risks distorting the analysis conducted. This will have implications for the ambit of the review exercise now undertaken by Ofcom, and the robustness of the regulatory conclusions reached. Whilst BT has not sought to undertake a comprehensive market definition exercise in this Submission, the evidence laid out in Sections 2 to 7 support findings of market power in relation to the Sky Sports proposition, such that its limited distribution impedes fair and effective competition.

6. The importance of an orthodox approach was confirmed in the Pay TV Proceedings before the CAT, where Barling J held (uncontroverted by the Court of Appeal) that while section 316 does not require Ofcom to "*analyse [contested practices] specifically by reference to the principles and case law applicable to Article 102 (or some approximation thereto) in order to establish jurisdiction to act… **[t]his…does not mean that Ofcom's investigation and analysis should be carried out without consideration of those principles***" (emphasis added). Moreover, he held that: "*Ofcom **must, of course, have regard to such general competition policy analysis as is applied in many contexts,** including the competition rules but also, for example, in the merger and market investigation regimes under the 2002 Act*"[474] (emphasis added).

7. The analytical framework now advanced by Ofcom in the present Consultation Document largely encompasses an orthodox approach in broad terms. However, in BT's view, Ofcom should develop its analysis more fully, with appropriate regard to market realities. Specifically, BT has the following observations in relation to Ofcom's approach in the Consultation Document:

    i. As discussed in detail in Section 3 of BT's main Submission, by focusing on "*key content*"[475] (i.e. individual sets of sports rights in isolation) Ofcom does not direct its analysis to the actual products that exist in the market. Individual rights are not bought by consumers, nor are they sold by pay TV retailers or wholesalers. As a

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472 Pay TV Proceedings, CAT, Ofcom's Defence, paragraph 64.

473 Third Pay TV Consultation, paragraph 2.13, outlining the approach taken by Ofcom.

474 *British Sky Broadcasting and others v Office of Communications and* others [2012] CAT 20 (the ***CAT Judgment***), at [155].

475 Consultation Document, paragraphs 4.2 – 4.3.

result, Ofcom's theoretical exercise identifying the importance of individual sporting events in isolation, is divorced from the reality that live sporting events are sold collectively in premium sports channels and packages of premium sports channels.

ii. Ofcom has acknowledged that consideration of the relevant market in the context of an assessment under section 316 is a necessary first step "*in order to understand properly the competitive dynamics in play*".[476] By divorcing its assessment in the Consultation Document from market reality, Ofcom risks failing to take into account the full extent of such competitive dynamics, with the attendant risk that – in the subsequent design of any remedy – Ofcom's intervention is misdirected or incomplete and will not correctly identify the scope of the regulation necessary to ensure fair and effective competition in pay TV markets going forward.

iii. Instead, as discussed in detail in Section 3, the correct starting point for Ofcom's review of the WMO Remedy should be to focus on the relevant products in this review: the sports *channels* and packages of channels which are available to pay TV subscribers and to consider which of these drive subscribers to subscribe to a particular pay TV service, rather than considering the impact of individual content rights in isolation. BT agrees that this necessarily entails a consideration of the sporting events shown on those channels, and their value to consumers. However, it requires an assessment of this content **in aggregate** (including other relevant factors such as branding[477]), not on the basis of individual pieces of content. [478]

iv. The approach presently advocated by Ofcom materially distorts its analysis of market participants' true market positions and the absolute and relative importance of their respective offerings. By focusing on individual rights in isolation, Ofcom's analysis over-states the position of BT Sport on the basis of its acquisition of a small number of individual rights some of which, erroneously in BT's view, Ofcom considers to be 'key'.[479] It also under-states the position of Sky Sports, given that Sky

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[476] Pay TV Proceedings, CAT, Ofcom's Defence, para 65.

[477] This will also include the manner in which consumers have access to those channels, notably via way of buy-through from a package of basic channels, and pricing based on a mixed bundled strategy.

[478] Indeed, Ofcom has previously acknowledged this fact itself having concluded that the attractiveness of a pay TV sport offering depends upon "*having some content that is seen as highly attractive, **along with a range of moderately attractive conten**t*". Moreover, Ofcom has also explicitly acknowledged that Sky's conduct supports this analysis: "[t]*he importance of offering **both highly attractive content as well as a range of moderately attractive content is shown by Sky's conduct.** Rather than just acquiring the most attractive sports content, Sky has also acquired a range of rights which it has used to assemble not one but four [now six] sports channels*". (Pay TV Statement, paragraph 5.93 and footnote 173.) (emphasis added).

[479] In particular, as discussed further in Section 3, Ofcom overstates the importance of the Champions League rights that were recently acquired by BT. In addition, as discussed in Section 2 Ofcom risks overstating BT's position as a result of the minority Premier League rights it holds.

continues to hold a significant aggregation of a wide range of rights which are considerably more attractive to consumers, and has materially strengthened its position since 2010 (as evidenced in Section 3).

v. BT agrees with Ofcom's principal conclusion that Sky continues to have a strong market position.[480] As discussed in detail in Section 4 it is evident that Sky enjoys a strong market position (with market shares equivalent to dominance) across all parts of the value chain, as well as material incumbency advantages at the retail level and significant bidding advantages for sports rights. However, Ofcom's assessment of Sky's market position is presently subsumed in Ofcom's assessment of the impact of limited distribution.[481] BT believes that a more orthodox approach with respect to Ofcom's assessment of the relevant products combined with a greater separation of Ofcom's market power assessment would have meant that Sky's enduring and entrenched dominance (and the material incumbency advantages and bidding advantages that it enjoys) would have been more apparent at a much earlier stage in Ofcom's analysis. Equally, such an approach would have identified that BT as recent entrant broadcaster has neither the ability nor incentive to limit the distribution of its BT Sport channels in a manner that could limit fair and effective competition.

The purpose of intervention under section 316

8. Where a party is active on a market but does not have the ability or incentive to distort fair and effective competition it would be inappropriate and unlawful for Ofcom to seek to regulate that party pursuant to section 316.

9. The purpose of section 316, in light of the statutory context, is to allow Ofcom "to impose conditions so as to ensure fair and effective competition in the wholesale and retail provision of licensed services to consumers generally".[482] As such, it would be perverse and contrary to the statutory purpose for Ofcom to seek to impose conditions upon an undertaking that is incapable of impeding fair and effective competition in the provision of licensed services. It is therefore <u>only</u> Sky, as the entrenched, dominant incumbent, that should, on the facts, be susceptible to regulation under section 316.

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[480] BT observes that Ofcom's findings in this regard are based on its analysis of the sports <u>channels</u> and packages of channels actually sold by Sky, for example Ofcom's assessment of shares of supply to customers considers channels containing key sports content (see Consultation Document, para 6.46).

[481] Consultation Document, para 6.29 *et seq*.

[482] *British Telecommunications PLC v Office of Communications and Others* [2014] EWCA Civ 133 (the ***CA Judgment***), per Vos LJ at [116], with regard, inter alia to Ofcom's statutory duty to further the interests of consumers in relevant markets (including, in this context, the pay TV market), where appropriate by promoting competition (Section 3(1)(b) of the Act). "*In the provision of*" for the purposes of section 316 of the Act must be construed widely in light of the statutory context (per Aikens LJ at [79]).

Objective evidence provides the best indicator that the limited distribution of Sky Sports has an effect on fair and effective competition

10. Ofcom has identified two broad types of limited distribution, namely failure to supply, or supply on terms that do not allow fair and effective competition,[483] which may impede the emergence of fair and effective competition in pay TV markets. The CAT's judgment (endorsed by the Court of Appeal) confirms that Ofcom's jurisdiction under section 316 of the Act extends to any practice which Ofcom can show to be prejudicial to fair and effective competition and so clearly extends to the limited distribution of the Sky Sports proposition as described in the Consultation Document.[484]

11. In an assessment as to whether there is a risk that Sky would engage in such limited distribution of the Sky Sports proposition (i.e. whether Sky has the ability and incentive to engage in the identified conduct), BT considers that Ofcom's analysis should focus upon the objective, observable market outcomes. As explained in detail in this Submission, limited distribution of the Sky Sports proposition **is** occurring and **has had** an impact on fair and effective competition in pay TV markets (as the evidence in Section 3 and 5 of this Submission demonstrates). Thus, an appreciation of the importance of the Sky Sports proposition, Sky's market position, the observable fact of limited distribution of the Sky Sports proposition and the observable fact of a lack of fair and effective competition in pay TV markets provides a more than sufficient basis for Ofcom to intervene. When considering Sky's incentives, Ofcom is not required by section 316 to consider whether Sky acted in a particular way out of any subjective, malign anti-competitive intent, i.e. Ofcom should avoid getting drawn into speculation as to Sky's intent and whether or not Sky "deliberately" limits the distribution of its Sky Sports proposition specifically to impede competition. It is sufficient for Ofcom to observe, on the basis of its economic analysis, that the limited distribution of the Sky Sports proposition is likely to have the <u>effect</u> of limiting the emergence of fair and effective competition.

12. This objective approach is also consistent with competition law orthodoxy, the importance of which is discussed above.[485] In particular, when engaging in an analogous assessment in the merger context of the likely incentives of merging parties to foreclose access to inputs to an actual or potential downstream rival, the European Commission will undertake an objective analysis to ascertain whether there is a risk of a significant impediment to effective competition.[486] In assessing whether an impediment to effective competition will eventuate, the

483 Consultation Document, para 7.3.

484 CAT Judgment, at [110], CA Judgment at [73] – [80].

485 See paragraphs 5 to 6, above, and the authority cited therein.

486 Commission Guidelines on the assessment of non-horizontal mergers (2008/ C 265/07) at para 31. The Commission has regard, in particular, to the level of profits that the entity obtains upstream and downstream, market shares enjoyed on the downstream market, and extent to which the merged entity has the capacity to capture diverted demand (paras 40 – 44).

Commission will, in particular, take into account the type of strategies presently and/or previously adopted on the market.[487]

13. As such, BT considers that the observable market outcome, namely the existence of terms of wholesale supply by Sky that limit the distribution of its Sky Sports proposition (whether by withholding wholesale supply entirely or imposing wholesale prices or terms that do not allow rivals to compete effectively) and the fact that this has had an impact on fair and effective competition in pay TV markets, is sufficient to warrant Ofcom's intervention. BT does not consider it necessary that Ofcom go further and seek to establish Sky's subjective intentions in this regard.[488]

The timing of subsequent reviews

14. BT considers that Ofcom should, consistent with its approach to *ex ante* market reviews more generally, define the time period across which its forward-looking assessment is based.[489]

15. The timing of future reviews will naturally have a bearing on the time-frame of the forward looking evidence that Ofcom is required to consider within the scope of the current review. As such, as a matter of good administration,[490] Ofcom should specify both when it will undertake a further review, and the particular circumstances in which it envisages it would be appropriate to re-visit its analysis. BT considers that a review period of three years is appropriate. This would safeguard against the risk that future developments will overtake the conclusions Ofcom reaches in the present review process. It will also help establish a transparent framework that gives certainty to market participants and consumers, whilst appropriately reserving flexibility on Ofcom's part to respond to identified relevant and material developments.

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[487] *Ibid*. at para 45, citing Case No. COMP/M.3225 – Alcan/Pechiney (II) (2004) at para 40. By the same token, the CMA's UK Merger Assessment Guidelines set out that the CMA, when assessing the incentive for a vertically integrated firm to discriminate against a downstream rival will consider, objectively, whether it is likely to be profitable to do, cost and capacity considerations and the trade-off between lost profits on the input market and gains likely to be extracted in the market for the final product. OFT1254/CC2 (September 2010), at paras 5.6.1 to 5.6.12.

[488] As Ofcom is aware in an abuse of dominance context, abuse is held to be an objective concept, and Ofcom is not required to prove any subjective intent on the part of a dominant undertaking (see, e.g. Case 85/76 *Hoffmann-La Roche v Commission* [1979] ECR 461 at [91]). Whilst Ofcom is not <u>obliged</u> to apply such considerations in relation to section 316 of the Act, it is clearly informative and (as per the CAT's judgment cited at footnote 469, above) permitted to take such principles into account.

[489] For example, in previous telecoms market reviews, and in merger assessment contexts, Ofcom has previously clearly defined the time horizon applicable to its assessment (usually three years). It was, of course, Ofcom's initial expectation in relation to the Pay TV Statement that it would start a review of the WMO no later than three years from when the WMO remedy came into force (Pay TV Statement, paragraph 1.56).

[490] Consistent, in particular, with Ofcom's fourth regulatory principle referred to at footnote 457, above.

16. BT considers that such an approach would be consistent with Ofcom’s duty under section 318 of the Act and its and general obligation to keep regulatory burdens under review pursuant to section 6 of the Act.[491].

[491] See in particular sections 6(1) and 6(2)(b) of the Act.

ANNEX 2: OFCOM'S CONSULTATION QUESTIONS

Question	Response
Market developments	
Question 3.1: Have we accurately represented the key developments in pay TV since 2010? Are there any other developments which you consider may be relevant to our assessment?	BT does not believe that Ofcom has accurately represented the key developments in pay TV since 2010, for the reasons set out in Section 2 of this Submission. Section 2 also sets out the other developments that BT considers are relevant to Ofcom's assessment.
Analytical Framework	
Question 4.1: Do you agree with our proposed analytical framework for identifying whether limited distribution of key content is a practice which may be prejudicial to fair and effective competition in pay TV services?	BT sets out its views on Ofcom's analytical framework in Annex 1. For the reasons set out in that Annex, and in more detail in Section 3, BT does not fully agree with the implementation of Ofcom's analytical framework, particularly as regards its assessment of the relevant products for this assessment.
Identifying key sport	
Question 5.1: Do you agree with our assessment that sports content is an important driver of choice in pay TV services? If not please provide evidence to support your view.	As set out in Section 3 of this Submission, BT agrees that sports content is an important driver of choice in pay TV services. However, for the reasons set out in that section, BT does not believe that Ofcom's approach of considering the importance of individual sporting events in isolation is appropriate.
Question 5.2: Do you agree with our assessment that live Premier League matches represent key content in competition for pay TV services? If not please provide evidence to support your view.	BT sets out its views on the relative importance of live Premier League matches in Section 3 of this Submission. For the reasons set out in that section, BT believes that Ofcom's analysis focusing on live Premier League matches is not appropriate.
Question 5.3: Do you agree with our assessment that live Champions League	BT does not believe that live Champions League matches represent key

Question	Response
matches also represent key content in competition for pay TV services, albeit to a lesser degree than Premier League content? If not please provide evidence to support your view.	content in competition for pay TV services, as set out in detail in Section 3 of this Submission.
Question 5.4: Do you agree with our assessment of the importance of other sports events? If not please provide evidence to support your view.	BT does not agree with Ofcom's assessment of the importance of other sports events for the reasons set out in Section 3.
Impact of limited distribution	
Question 6.1: Do you agree with our assessment that limited distribution of Sky Sports may be prejudicial to fair and effective competition?	BT believes that the limited distribution of Sky Sports is prejudicial to fair and effective competition, for the reasons set out in Sections 2, 3, 4 and 5 of this Submission.
Question 6.2: Do you agree with our assessment that limited distribution of BT Sport is unlikely to be prejudicial to fair and effective competition?	BT believes that the limited distribution of BT Sport could not be prejudicial to fair and effective competition, for the reasons set out in Sections 2, 3, 4 and 5 of this Submission.
Assessing incentives to limit distribution	
Question 7.1: Do you agree with our assessment of Sky's incentives to limit distribution of its key content? If not please explain why.	BT agrees with Ofcom's assessment of Sky's incentives to limit distribution of its Sky Sports proposition for the reasons set out in Section 6.
Question 7.2: Do you agree with our assessment of BT's incentives to limit distribution of its key content? If not please explain why.	BT sets out its views on Ofcom's assessment of BT's incentives to limit distribution of its BT Sport proposition in Section 6.
Next steps	
Question 8.1: Do you consider it appropriate to maintain some form of regulation on Sky in order to ensure fair and effective competition in pay TV? Please provide evidence to support your view.	BT not only believes that it is appropriate to maintain some form of regulation on Sky in order to ensure fair and effective competition in pay TV, BT believes that existing regulation most be materially strengthened. BT's reasons are contained in Sections 2 to 8 of this Submission.

Question	Response
Question 8.2: Do you agree with the potential options for regulation we have identified? Do you believe there are other options we should consider?	BT sets out its preliminary views on the potential options for regulation in Section 8 of this Submission.
Question 8.3: Do you consider that the WMO obligation placed on Sky is no longer required to ensure fair and effective competition in pay TV? Please provide evidence to support your view.	BT believes that the WMO obligation on Sky is certainly still required, and in fact that existing regulation must be materially strengthened. BT's reasons are contained in Sections 2 to 8 of this Submission.
Question 8.4: Do you agree with our assessment that it is unlikely to be appropriate to consider the imposition of regulation on BT to ensure fair and effective competition in pay TV at the current time? Please provide evidence to support your view	BT believes that it would be highly inappropriate to consider the imposition of regulation on BT to ensure fair and effective competition. BT's reasons are contained in Sections 2 to 8 of this Submission.

ANNEX 3: INDEX OF SUPPORTING DATA ANNEXES

1. BT provides various annexes of supporting data and evidence referenced within the main Submission. The index below provides Ofcom with a reference to each of these annexes for ease of reference.

Annex	Paragraph reference	Document
3-1	2.5	Evidence of Sky promotional offers
3-2	2.5	Evidence of Sky promotional offers
3-3	2.13(vi)	Sky Sports 'Compare Live Fixtures online'
3-4	2.9, 2.24, 2.25	Sky Sports rights spreadsheet
3-5	2.27	Corrected representation of Figure 3.4 of the Consultation Document
4-1	3.45(i)	Sky Sports product web page
4-2	3.45(i)	Sky Movies product web page
4-3	3.45(ii)	Sky Sports advertisements February – August 2014
4-4	3.45(ii)	Selection of current Sky Sports online advertisements
4-5	3.45(iii)	Web page advertisement for Sky Sports "Ultimate Weekend" (22-25 May 2014)
4-6	3.45(iii)	Web page advertisements for Sky Sports "Another big weekend" (7-9 and 21-23 November 2014)
4-7	3.45(iv)	Screenshots of Sky Sports promotional video (May 2014)
4-8	3.45(v)	Sky Go screenshots (25 February 2015)
4-9	3.45(vi)	Selection of Sky Sports press releases
4-10	3.47	Selection of Sky Sports advertisements (summer 2010)

GLOSSARY

Term	Definition
2006, 2009, 2012, and 2015 PL Auctions	The auction for the UK broadcasting rights for the Premier League held in 2006 (for the 2007/08 – 2009/10 seasons), 2009 (for the 2010/11 – 2012/13 seasons), 2012 (for the 2013/14 – 2015/16 seasons), and 2015 (for the 2016/17 – 2018/19 seasons)
2013 UCL Auction	The auction for the UK broadcasting rights for the UEFA Champions League rights (for the 2015/16 to 2017/18 seasons) held in November 2013. This auction also included the sale of the Europa League rights.
4K	A display device or content having horizontal resolution in the order of 4,000 pixels
ARPU	Average revenue per user. A measurement used by pay-television or mobile companies to indicate the average monthly revenue earned from a subscriber.
BARB	Broadcasters' Audience Research Board. The pan-industry body which measures television viewing
BT	BT Telecommunications plc
BT Sport	The TV channels BT Sport 1, BT Sport 2 and ESPN.
BT TV	BT's retail pay TV offering (comprising services over YouView or Cardinal STBs)
BT CA98 Complaint	BT's complaint against Sky under the Competition Act 1998 about the wholesale supply of SS1&2 to BT's YouView platform
The Act	Communications Act 2003
CAT	Competition Appeal Tribunal
CAT Judgment	*British Sky Broadcasting and others v Office of Communications and* others

Term	Definition
	[2012] CAT 20
CA98	Competition Act 1998
Cardinal	BT's [✂] platform, used along with YouView, to deliver its BT TV service. The Cardinal platform exists in two variants, Cardinal 2.0 and Classic
CC	Competition Commission. The CC has now closed and its functions have been transferred to the Competition and Markets Authority.
CMA	Competition and Markets Authority.
Court of Appeal or CA	Court of Appeal of England and Wales
CA Judgment	The Court of Appeal's judgment of 17 February 2014 in *BT v Sky, Ofcom and others* [2014] EWCA Civ 133
Consultation Document	Ofcom's consultation document published on 19 December 2014 (as updated), *"Review of the pay TV wholesale must-offer obligation*", including Ofcom's pay TV research, available at: http://stakeholders.ofcom.org.uk/consultations/wholesale-must-offer/
CPs	Communication Providers
DSat	Digital satellite.
DTT	Digital Terrestrial Television. A digital distribution technology using terrestrial transmitters
FRND	Fair, reasonable and non-discriminatory
FTA	Free-to-air. Broadcast content that people can watch or listen to without having to pay a subscription
Grant-Back Condition	Requirement of Sky whereby its wholesale supply of SS1&2 to BT's YouView platform is conditional on BT wholesaling BT Sport to Sky
HD	High Definition. A technology that provides viewers with better quality, high-resolution pictures.

Term	Definition
IPTV	Internet Protocol Television. The term used for television and/or video signals that are delivered to subscribers or viewers using Internet Protocol (IP), the technology that is also used to access the Internet. Typically used in the context of streamed linear and on-demand content, but also sometimes for downloaded video.
IRO	Interim Relief Order made by the CAT on 29 April 2010 in relation to the WMO remedy, as varied by the IRO Judgment
IRO Judgment	Judgment by the CAT on 5 November 2014 approving BT's application to vary the IRO to extend it to BT's YouView platform, [2014] CAT 17
MRGs	Minimum Revenue Guarantees
NOW TV	An internet-based instant streaming TV service provided by Sky. NOW TV is accessible through web browsers, via smartphone, tablets and Xbox games consoles, and through apps downloaded to STBs including those for YouView
Pay TV Proceedings or Appeals	All court proceedings resulting from the Pay TV Statement, in particular: (a) the CAT Judgment, and (b) the CA Judgment
Pay TV Statement	Ofcom's Pay TV Statement, 31 March 2010, available at: http://stakeholders.ofcom.org.uk/binaries/consultations/third_paytv/statement/paytv_statement.pdf
OTT	Over-the-top.
Premier League	The Premier League relates to both the football competition (currently the Barclays Premier League) and the organising body of the Barclays Premier League. References in this document are to the competition itself, rather than the organising body.
PSB	Public Service Broadcasting, or Public Service Broadcaster. The Communications Act in the UK defines the PSBs to include the BBC, ITV1, Channel 4, Five and S4C.
Self-retail	Where a content provider makes its content available to subscribers on another provider's platform, but has a direct billing relationship with the subscriber rather than making its content available to the platform

Term	Definition
	provider on a wholesale basis.
Sky Sports	The TV channels Sky Sports 1, Sky Sports 2, Sky Sports 3, Sky Sports 4, Sky Sports 5, and Sky Sports F1.
Sky Sports Proposition	A retail product include all of the Sky Sports channels and SS News HQ in SD and HD.
SD	Standard Definition. As opposed to high definition.
SS1&2 or the regulated SS channels	Sky Sports 1 and Sky Sports 2
SS3-5&F1 or the non-regulated SS channels	Sky Sports 3, Sky Sports 4, Sky Sports 5 and Sky Sports F1, and also includes SS News HQ
SS News HQ	Sky Sports News HQ
STB	Set-top Box.
TalkTalk	TalkTalk Telecom Group plc
UCL	UEFA Champions League, an annual continental football club competition organised by UEFA since 1992
UEFA	Union of European Football Associations. The governing body of football in Europe.
UEFA Rights	Live UK rights for the UEFA Champions League and UEFA Europa League, awarded to BT in November 2013 for the period 2015/16 to 2017/18.
UHD	Ultra HD, see also 4K
VULA	Virtual Unbundled Local Access; it provides access to NGA networks in a way that is similar to LLU. It provides a connection from the nearest 'local' aggregation point to the customer premises
VULA Margin Statement	Ofcom's draft statement "*Approach to the VULA Margin*", notified to the European Commission on 15 January 2015
WMO or WMO	Wholesale must-offer. The obligation imposed on Sky in the 2010 Pay TV Statement requiring it to offer to wholesale its SS1&2 channels (SD and

Term	Definition
Remedy	HD) with certain prices and terms set by Ofcom.
WMO Review	Ofcom's review of the WMO remedy, announced in April 2014; details available at http://stakeholders.ofcom.org.uk/consultations/wholesale-must-offer/
Virgin Media	Virgin Media Limited
YouView	A joint-venture between the BBC, ITV, Channel 4, Channel 5, Arqiva, BT and TalkTalk offering a subscription-free digital TV service, delivered via a combination of a broadband internet WRconnection, television aerial and a YouView set-top box. YouView is one of the two platform systems used by BT to deliver its BT TV service.