



Airtime Sales Rules Review Consultation

Response

Set out below is Sky's response to Ofcom's proposals to lift the withholding and conditional selling rules as per the Airtime Sales Rules Review Consultation of 29 March 2010 (the "ASR Consultation").

Before considering Ofcom's proposals, Sky wishes to raise two concerns regarding: (i) the limited time that stakeholders have had to consider the econometric model; and (ii) Ofcom's failure, thus far, to have due regard to the interplay between the ASR and COSTA rules, the review of which should be conducted in tandem.

Econometric Model

Stakeholders have been afforded only a few weeks to consider the econometric model¹, which is technically complex, and has been relied on by Ofcom in reaching its provisional conclusions, Ofcom itself having had several months to digest its implications.

In Ofcom's letter to Sky of 28 May 2010 ("Ofcom's Letter"), Ofcom states that the econometric analysis was not "heavily relied" on in reaching its provisional conclusions. However, the conclusion to lift the withholding rule appears to be based on the elasticities derived from the model. Indeed, on closer examination of the section entitled "*There is evidence to support the view that channels are not incentivised to withhold*"², the first sub-section³ relies completely on the outputs of the econometric model, and the remaining two sub-sections present no further evidence. In addition, the argument that broadcasters do not currently appear to withhold airtime, provided by Ofcom as a justification for removing the rule, is not strong given that the withholding rule is in place and the commercial analogue channels would need to manipulate their distribution to circumvent the strict application of the rule.

Whilst Ofcom has sought also to rely on other factors to support its view that the analogue channels are not incentivised to withhold, the model appears to form an important part of Ofcom's analysis.

Accordingly, Sky reserves its position to make further representations as may be appropriate in respect of ASR, once the robustness of the model and its implications for ASR are more fully

¹ Ofcom report "An econometric analysis of the TV advertising market" conducted by Analysys Mason published 25 May 2010.

² Page 38 of the ASR Consultation.

³ Entitled "Evidence from econometric studies".

understood, which work is being undertaken in the course of considering potential changes to COSTA.

Links between ASR and COSTA

In the Ofcom Letter and ASR Consultation⁴, Ofcom states that there are distinct differences in the scope and objectives of the COSTA review and the ASR Consultation. As stated previously, Sky considers that there are inextricable links between the two reviews and that it is not appropriate for Ofcom to consider them in isolation.⁵

Indeed, in the genesis of the withholding rule itself, an explicit link was made with the rules on minutage, as Ofcom records in the ASR Consultation⁶ (*“the commercial analogue channels had the tightest **restrictions on the amount of airtime** they were able to sell...**as a result** the ITC/Ofcom concluded that these broadcasters had the potential to withhold airtime and increase profits”* - emphasis added).

Moreover, a number of statements in the ASR Consultation highlight the links between the two sets of rules, for example:

- the statement that it would be useful for the ASR review to precede a review of COSTA because the position as to whether the PSBs are still required to sell all the airtime may be a relevant consideration in deciding whether to increase the minutage allowance.⁷
- The evidence relied upon to support a removal of the withholding rules considers the incentives of the PSBs and considers the cross-elasticity effects of changes in the amount of advertising minutage of individual PSBs.⁸ Clearly, the amount of advertising permitted by COSTA is relevant to incentives to sell airtime, as broadcasters seek to maximise revenue. Although it may not be currently in the interests of ITV or Channel 4, for example, to withhold airtime, their incentives to do so may be altered if they are permitted greater minutage by a change in COSTA.
- *“any increases in advertising minutes broadcast on non-PSB channels are likely to increase their supply of impacts...if advertisers switch to these channels...this switch in revenues may help to offset any increase in prices on PSBs. The extent to which other channels could undertake an increase in advertising minutes depends on a number of factors but in particular whether they are close to their advertising caps.”*⁹ This also suggests that any incentive for a PSB to withhold advertising airtime would be impacted by the ability of advertisers to switch to different channels, the amount of advertising permitted in turn having a bearing on their ability to switch.

⁴ Paragraph 2.27 of the ASR Consultation.

⁵ See Sky letter to Ofcom dated 26 May 2010.

⁶ Paragraph 2.8 of the ASR Consultation.

⁷ Paragraph 3.20 of the ASR Consultation.

⁸ Paragraphs 5.31-5.36 of the ASR Consultation.

⁹ Paragraph 5.43 of the ASR Consultation.

Ofcom also appears to be arguing (in both the ASR Consultation and the Ofcom Letter) that the ASR are about ensuring fair and effective competition, whereas COSTA is about consumer protection.¹⁰ This takes a rather narrow view, especially in light of Ofcom's statutory duties and its principal duty to further the interests of citizens and consumers where appropriate by promoting competition.¹¹ Indeed, fair and effective competition and the interests of the consumer are inextricably linked. Changes to COSTA would not only impact upon consumers but on competition (particularly if the result of any changes to COSTA would be to transfer wealth from newer content providers, to the incumbents, thereby reinforcing their market power) between broadcasters (just as the assessment of fair and effective competition in the context of the ASR must also include an analysis of the impact on consumers). There is therefore a clear overlap in the scope of both sets of rules.

Sky would encourage Ofcom, therefore, to give due consideration to the links between COSTA and ASR and to the appropriate scope of both reviews, which should be undertaken at the same time.

Proposal to lift the withholding rule for all the commercial analogue channels

Notwithstanding these reservations, Sky has a number of high level observations on Ofcom's proposal to lift the withholding rule:

- We note Ofcom's preliminary conclusion that there are limited incentives for ITV1, C4 and five to withhold advertising minutes on their main channels, based, in particular, on the results of the econometric model, which suggest that any revenue gains from doing so would be small.¹² Nevertheless, as Ofcom recognises in paragraph 5.36 of the ASR Consultation, a withholding strategy could result in increased revenues for ITV1, and it is not clear at this stage whether the results of the model can be relied upon (again highlighting the need for fuller testing of the model, before proceeding with the ASR Consultation).
- Moreover, we would suggest that ITV is in a stronger position than appears to be recognised in the ASR Consultation. Ofcom's focus on SOCI and SONAR measures in isolation of each other rather overlooks the important ratio between the two, which in ITV's case has increased over time, notwithstanding CRR, highlighting that its market power has not declined, relative to its competitors.¹³
- Indeed, the Competition Commission in its final report on CRR concluded that "*ITV1 retained an enhanced market position...primarily due to its unique ability to deliver large audiences*".¹⁴
- As long as CRR is in place to constrain the exercise of ITV's market power, ITV's ability to withhold airtime is constrained.

¹⁰ Paragraph 2.27 of the ASR Consultation.

¹¹ Section 3(1) of the Communications Act 2003.

¹² Paragraph 2.14 of the ASR Consultation.

¹³ See paragraph 5.26 of the Final Report of the Competition Commission – Review of IITV's CRR Undertakings published 12 May 2010 ("CC Report") where the CC noted ITV's premium has increased to 1.34 in 2009 from 1.28 in 2008.

¹⁴ Paragraph 26 of the CC Report.

- Should there be any change to the position on CRR, a fresh assessment of ITV's (in particular) ability and incentives to withhold airtime would be required.

Proposal to lift the conditional selling rule for all channels

In relation to conditional selling, we agree that such conduct is only a matter of potential concern where the seller has market power, which in the case of TV advertising, means ITV. As long as ITV is required by CRR to offer separate contracts for airtime on ITV1, there is sufficient protection already in place.¹⁵

It would not be appropriate, therefore, to maintain additional ex ante regulation, all the more so, where ex post competition enforcement is available as a backstop.

Conclusion

In short, Sky considers that it is not appropriate for Ofcom to conduct the ASR Consultation in isolation from its review of COSTA, given the clear linkages between the two sets of rules and commonalities in their purpose. The two sets of rules should be considered together, and once stakeholders have had sufficient opportunity to assess the robustness and implications of the econometric model. In due course, together with consideration of the minutage rules, it might be appropriate for Ofcom to lift the ASR, perhaps with greater certainty that CRR will remain. Should there be any change in the position of CRR, it would be incumbent on Ofcom to reassess the appropriateness of lifting the withholding and conditional selling rules, in so far as they relate to ITV.

¹⁵ Paragraphs 3.24- 3.25 of the ASR Consultation.