

ITC/Ofcom joint consultation on ITC Rules regarding Advertising Sales Arrangements

Consultation document

The deadline for comments is **14 November 2003**.

Contents

Section		Page
1	Introduction	1
2	Background	2
3	ITC/Ofcom proposals for Advertising Sales Arrangements	3
4	Additional rules in relation to ITV's airtime sales	4
5	Combinations of other licensees selling airtime	4
6	With-holding airtime and conditional selling	7
7	Summary of views sought	8
Annex A	ITC rules regarding Advertising Sales Arrangements issued May 2001	10

Introduction

1. Under Section 2(2)(a) of the Broadcasting Act 1990, The Independent Television Commission (ITC) has a statutory duty to “ensure fair and effective competition” in the provision of licensed broadcasting services and services connected with them. However, from December 2003, the ITC’s statutory functions in relation to the regulation of broadcasting and related services will cease to exist and Ofcom (the Office of Communications) will take responsibility for regulating all communications matters, including broadcasting, under its statutory functions as set out in the Communications Act 2003. This includes the responsibility for ensuring fair and effective competition in the provision of broadcasting and related services.
2. One of the ways in which the ITC fulfils its duty to ensure fair and effective competition is by issuing rules governing licensees’ airtime sales arrangements¹. In light of the Secretary of State’s decision today, following the Competition Commission’s (CC) investigation into the possible merger of Carlton and Granada, the ITC believes that our current rules regarding Advertising Sales Arrangements should be reviewed. Given the changing regulatory framework, the ITC and Ofcom wish to consult jointly on the extent to which ex ante rules are still necessary to protect this market, and if so the form any new rules should take. Consequently, this consultation paper seeks comments from interested parties as to the appropriateness of changing the rules in relation to airtime sale arrangements. To the extent that new rules are found to be necessary they would come into force with the new regulatory regime at the end of December 2003².
3. Given the necessity of ensuring that any new rules come into force in line with the new regulatory regime, this will be a five week consultation ending on the 14th of November. Responses should be returned to:

Nicola Floyd

Senior Competition and Regulation Manager

ITC
33 Foley Street
London
W1W 7TL

Ofcom
Riverside House
2a Southwark Bridge Road
London SE1 9HA

Telephone: 020 7306 7812

020 7981 3000

email: Nicola.Floyd@itc.org.uk

¹ Our current rules are set out in Annex A.

² Given that Carlton and Granada are unable to begin merger proceedings until after the repeal of the Broadcasting Act 1990, we believe it is appropriate to ensure that any new rules should be introduced in line with the new statutory regime at the end of December. Until then we would expect that current rules apply.

Background

4. Since the existing rules on Advertising Sales Arrangements were published in May 2001 the television advertising market has been undergoing a period of substantial change. The take up of digital television has been significant, and there has been rapid growth in the number of new digital channels. This has had a significant effect on “traditional” analogue viewing patterns, with ITV being most hard hit.
5. In the context of these changes the CC was asked to consider the potential effects on competition of a merger between the two major ITV companies - Carlton and Granada. One of the main focuses of the CC’s work was on the sale of Carlton and Granada’s airtime.
6. The CC concluded that the relevant economic market in this case was the television advertising market, and the relevant geographic market was the UK. This was quite a significant change from the CC’s last enquiry into an ITV merger, where it concluded that ITV was, in fact, a separate market segment in itself. However, even with this wider market definition a combined ITV would have more than 50% of the market.
7. The CC determined that competition between ITV and other commercial channels had to be viewed in the context of ITV’s overall declining share. However, despite this decline, the CC believed that other channels were not yet sufficiently close substitutes to prevent ITV demanding an increased share of advertisers/media buyers’ advertising budget for a given level of discount. Whilst analysis showed that – technically – the same coverage could be achieved with and without ITV, other considerations such as the difficulty of purchasing enough slots to achieve the required coverage, and the likelihood of obtaining a lower sales uplift without ITV, would act as a barrier to switching at least for some advertisers.
8. They, therefore, concluded that the proposed merger would have an adverse effect on competition in the television advertising sales market, and stated that some form of remedy would be necessary if the merger was to be allowed to go ahead. The CC found two remedies – the divestment of sales houses and the Contract Rights Renewal (CRR) – that would adequately address the competition issues found. Since both remedies addressed competition concerns, the majority of the CC opted for the CRR as the least intrusive, and therefore more proportionate, remedy.
9. The CRR essentially gives all organisations with a contract for advertising airtime with Carlton or Granada the right to renew the terms of their existing contracts without change for the duration of the remedy, assumed to be at least 3 years. That is, they are guaranteed the same terms and conditions they negotiated when there was competition between the Carlton and Granada sales houses. It also allows their share of broadcast commitments to change in line with any change in ITV’s share of commercial audiences. So they have a built in protection in the event that ITV’s share continues to decline. Those buyers that believe that they do not need the protection of the remedy are free to negotiate a new deal with ITV. Because the application of this remedy is quite complicated, an adjudicator, who is to be an expert in the TV advertising market, will be established to deal with any disputes swiftly and effectively³.
10. In our submissions to the Competition Commission in the course of the inquiry, the ITC and Ofcom made clear that we saw benefits from the consolidation of ITV’s

³ For further details on the CRR please see the ITC/Ofcom joint briefing in response to the Secretary of State’s decision on the ITV merger

broadcast functions as this was likely to reinforce ITV's ability to sustain its public service broadcasting commitments. However, these benefits had to be weighed against a potential lessening of competition that might arise from the merger, particularly in the television advertising market. We made clear that we were keen to find remedies that could address these issues. We believe that the CRR does so, and as a result we are committed to making sure it is an effective and proportionate remedy.

ITC/Ofcom proposals for Advertising Sales Arrangements

11. The ITC's 2001 *Rules Regarding Advertising Sales Arrangements* (the *Rules*) set out detailed rules as to how advertising time may be sold. They prohibit the joint selling of airtime by Carlton and Granada, as well as the two London Channel 3 licensees from selling airtime together. They also ban "share for ITV" deals, which commit a share of the buyer's total budget to ITV in return for preferential rates.
12. The *Rules* also set a limit of 5% on national licensees, or small Channel 3 licensees, who wish to sell their airtime jointly with other national licensees. In addition, national licensees with a market share equivalent to GMTV or less may resell their airtime jointly with either of the two main Channel 3 airtime sales houses.
13. The CC's decision today rewrites the structure of the TV advertising market. Inherent in the CC's findings is an assumption that the TV advertising market exhibits a greater degree of substitutability now than when they last examined this market back in July 2000, and consequently competition is stronger.
14. A natural consequence, therefore, of the CC's findings is a requirement on the ITC and Ofcom to examine the appropriateness of maintaining the ITC's 2001 *Rules*. In particular, given that competition has increased in this market, the ITC and Ofcom wish to consider whether the market is now sufficiently competitive that detailed ex ante rules are no longer necessary to protect competition, and the market can now default to protection under general competition law. On the other hand we recognise that the relaxation of rules in relation to Carlton and Granada selling airtime together is also accompanied by a detailed remedy in order to ensure effective competition in the future.
15. The ITC and Ofcom are, therefore, seeking views as to whether or not it is appropriate to remove ex ante rules in relation to airtime sales and simply rely on ex post competition law.
16. In considering this question there are three general areas where ex ante rules are currently applied in this market where we are seeking views as to whether it would be appropriate to relax our *Rules*, or indeed remove them altogether:
 - In relation to the selling of ITV's airtime, including allowing share for ITV deals;
 - Combinations of other licensees (in particular licensees with a NAR share greater than 5%) selling airtime jointly; and
 - With-holding airtime and conditional selling.
17. Each of these areas are discussed in more detail below.

Additional rules in relation to ITV's airtime sales

18. The CC's investigation into the effect on competition of Carlton and Granada selling their advertising together found that, following the repeal of the Broadcasting Act provisions preventing a merger, both companies could sell their airtime together when merged, subject to the CRR remedy. This remedy will be underpinned by a binding, statutory undertaking given to the Secretary of State by the parties and as a result the ITC's *Rules* do not need to be amended in order to implement the CRR.
19. Following the introduction of the CRR, therefore, the ITC and Ofcom will lift the current prohibition on joint selling of airtime by Granada and Carlton, as well as the ban on the two London Channel 3 licensees selling their airtime together in order to be consistent with the CC's findings.
20. The ITC is seeking views on the appropriateness of continuing to ban "share for ITV" deals. The CRR is predicated on the existence of share deals, and once Carlton and Granada merge advertisers and media buyers may combine their separate Carlton and Granada share deals into a deal covering all ITV except the smaller, non-consolidated ITV companies⁴. As such, the ITC and Ofcom's initial view is that it is unlikely to be practical to continue to ban share for ITV deals simply to exclude the smaller, non-consolidated licensees (on whose behalf Carlton and Granada currently sell airtime in any case). Indeed advertisers and media buyers may find it more convenient to commit a total share to ITV as they do to other national advertisers.
21. The ITC and Ofcom are also seeking views as to whether any additional rules are needed in relation to ITV's airtime sales in order to protect the market more generally. In particular we note that the CC has recommended that the CRR should be supported by additional undertakings to prevent material changes to the current airtime sales system, such as a commitment to maintain SAP for the duration of the remedy and to retain all regions and demographics that the parties currently sell. While these requirements will form part of Carlton and Granada's undertaking to the OFT, we would be interested in hearing views from respondents as to whether any further rules may be necessary to fully underpin the remedy.

Combinations of other licensees selling airtime

22. Under current ITC rules, national licensees and small Channel 3 licensees with a NAR share of 5% or less may combine to sell airtime jointly with each other or with any other national licensee. This means that smaller licensees may combine with larger licensees to sell their airtime, but larger sales houses, with NAR shares of 5% or more, (currently Channel 4, Five and BSkyB) cannot combine their sales operations⁵.
23. Given the CC's views in relation to the relaxation of sales rules for Carlton and Granada – the two largest airtime sales houses in the UK – we believe it may be appropriate to consider relaxing the rules prohibiting other larger sales houses from combining their sales businesses, or indeed removing restrictions entirely and relying only on ex post competition law.

⁴ SMG, Ulster and Channel

⁵ They cannot combine their sales operations with Carlton or Granada's sales businesses either.

24. On the one hand it could be argued that restrictions on the other larger sales houses selling together are no longer necessary, and reducing restrictions on joint selling would allow them to better compete with the merged ITV sales house. The full merger of the other larger sales houses (or any combination) would be considered under the Enterprise Act to establish whether it led to a substantial lessening of competition. To the extent that they stopped short of a full merger of their sales businesses but agreed jointly to sell airtime on each other's behalf, such an agreement could be considered under Chapter I of the Competition Act if it were to prevent, restrict or distort competition. As such, it could be argued that we should simply rely on general competition law to protect the market from any anti-competitive effects if the larger national sales houses were allowed to jointly sell their airtime.
25. On the other hand, it could be argued that allowing the joint selling of the other larger sales houses' airtime could simply lead to a duopoly with the merged ITV sales house, leading to a reduction in competition overall. In addition, it could be considered that, while Carlton and Granada's market shares are falling year on year, both Five and BSkyB's market shares are rising, making a combination of Channel 4, Five and BSkyB's businesses potentially more powerful over time than the merged ITV sales houses and as such could present a potentially more significant detriment to competition if not constrained.
26. The CC focussed its analysis on the degree of competition between ITV and all other parties in the TV advertising market. In order to inform our decision as to whether rules on joint selling of airtime by the other larger sales houses should be removed or relaxed the ITC and Ofcom must now assess the degree of competition that exists between all other players in the market. With that in mind, we would welcome respondents' views on the impact (if any) on competition if the following sales houses were allowed to jointly sell their airtime:
 - (i) All of the other larger sales houses with NAR shares greater than 5%
 - (ii) Two out of the three larger sales houses (eg Channel 4 and Five)
 - (iii) Either of the above permutations combined with other smaller multichannel channels or ITV licensees (SMG, UTV, Channel)
27. In considering the impact on competition we would particularly like to hear respondents' evidence on the following issues:
 - The extent to which they believe that advertising on multichannel could be considered to be a fully effective substitute for advertising on analogue terrestrial channels such as Channel 4 and Five.
 - The extent to which there is increased fragmentation in the UK TV market, and if so, what effect they believe this will have on the market power of analogue terrestrial channels, such as Channel 4 and Five, as well as on larger digital channels.
 - The extent to which share of broadcast commitments and premiums are increasing/decreasing for the larger sales houses, and how these have changed over the last three years.
 - The extent to which they believe that the growth in NAR shares experienced by Five and multichannel channels is likely to continue, particularly in light of any ITV merger accompanied by the CRR remedy

- The extent to which the advertising products (regions and demographics) that the larger sales houses sell could be considered to be substitutes or complements. In particular, are they substitutes/complements (i) in aggregate (ii) for particular types of advertisers?
 - Are there any specific types of advertiser or any particular demographic product that would see a substantial reduction in competition as a result of any combination of the larger sales houses selling their airtime together?
 - The extent to which allowing the three largest sales houses, other than ITV, to sell together will lead to a stronger competitor to a single ITV sales house.
 - The extent to which you believe maintaining separate buying points for the major sales houses is important. If so how many separate buying points should be maintained?
 - Any implications of television broadcasters combining with non-television advertising sales operations (such as cinema, radio, press or other).
28. To the extent that respondents feel that some relaxation of the existing rules in relation to the other larger sales houses is warranted we would be interested in views as to the extent of that relaxation. In particular, what combination of sales houses (all three, two out of three, a particular two out of three etc) should be allowed to sell together.
29. In addition, to the extent that consolidation among the other larger sales houses is acceptable, should there be limits as to how these sales houses can then combine with other, smaller, buying points in the multichannel environment? For example, if all three of the larger sales houses were allowed to combine, without limit, with all other smaller sales houses, over time it is possible that this new sales house could actually outstrip ITV, but with no remedy in place to curb any potential market power that it may have. Therefore we are also seeking views as to:
- Whether there should be a cap (in terms of NAR share) on total consolidation between non-ITV sales houses?
 - If so at what level should this cap be set?
30. The ITC and Ofcom would expect that it is appropriate to continue to prevent any of the larger sales houses, with a NAR of more than 5%, from selling their airtime with any new merged ITV sales house, although again we would seek views as to whether this requires specific ex ante rules or whether this issue should be dealt with under general competition law.
31. Current ITC rules also allow national licensees with a market share equivalent to GMTV or less to sell their airtime with Carlton and Granada's sales houses. While we believe that it is certainly appropriate for a merged ITV sales house to continue to sell on behalf of other ITV owned ventures, such as ITV2 and the other non-consolidated ITV licensees, as well as GMTV, we are seeking views whether it is appropriate for them also to be allowed to sell on behalf of independent third parties in the UK TV market. Clearly, if they were allowed to sell on behalf of independent third parties, any such sales would not be covered by the CRR. In considering this issue, we would particularly like views from independent third parties as to the impact that any such change would have on the choices open to it.

32. It is worth noting that the CC's report contains special arrangements to allow SMG, Ulster and Channel to continue to sell their airtime with the merged Carlton and Granada sales house. However, for the avoidance of doubt we believe that they should not be precluded from selling their airtime with any other national licensee if they chose to do so.
33. Whether or not there is a need to maintain ex ante rules in relation to joint selling, and if so the appropriate levels of joint selling that should be allowed, is an issue where the ITC and Ofcom would particularly like to hear the views of advertisers and media buyers.

With-holding airtime and conditional selling

With-holding airtime

34. The ITC regulates the amount of time that can be devoted to advertising by commercial channels in accordance with the relevant EC Directives⁶. These rules do not specify a minimum number of minutes to be sold. However, the ITC has, in the past, stated that failure by the terrestrial broadcasters to sell advertising time to the maximum extent in an attempt to restrict supply and push up prices is likely to be considered to be prejudicial to fair and effective competition, and as such, would breach the conditions of their licence.
35. The ITC and Ofcom believe that it would be appropriate to consolidate this statement as part of our rules on advertising arrangements going forward, and seek views as to whether respondents believe this to be appropriate. In particular, we would be interested in hearing views as to which licensees this rule should be applied to:
 - the analogue terrestrial licensees only?
 - broadcasters with large NAR shares (5% or more)?
 - all broadcasters?

Conditional selling

36. "Conditional selling" makes the sale of one of the licensee's products (for example ITV1) conditional on the advertiser/media buyer taking another product that the licensee sells (for example ITV2). In its 1996 *Consolidated Statement Regarding Advertising Sales Arrangements* the ITC confirmed that the practice known as "conditional selling" was incompatible with licensees obligation to refrain from practices that are prejudicial to fair and effective competition. While the 2001 *Rules* did not state that conditional selling was acceptable, for the avoidance of doubt the ITC and Ofcom believe that it would be appropriate to again explicitly incorporate this as part of the *Rules*. Again, we are seeking views as which licensees this rule should be applied to:

⁶ For Channels 3, 4 and 5 a maximum of 168 minutes a day is allowed, with an average of 7 minutes an hour overall and 8 minutes during peak hours. There is a maximum of 12 minutes allowed in any one clock hour.

- the analogue terrestrial licensees only?
- broadcasters with large NAR shares (5% or more)?
- all broadcasters?

Summary of views sought

37. To summarise, the ITC and Ofcom are seeking views as to whether or not it is appropriate to remove ex ante rules in relation to airtime sales and simply rely on ex post competition law. In considering this question the ITC would particularly like respondents to consider the following:

- In relation to additional rules on ITV's airtime sales:
 - Whether it is appropriate to lift the ban "share for ITV" deals
 - Whether any further rules are needed in relation to ITV's airtime sales in addition to those specified by the CC in order to protect the market more generally
- In relation to different combinations of licensees selling airtime:
 - Whether it is appropriate to remove or relax the rules prohibiting larger licensees (NAR share of more than 5%) from combining their sales houses and rely solely on general competition law or whether this could be expected to lead to an overall lessening of competition. We would be interested in hearing views on the impact (if any) on competition if the following sales houses were allowed to jointly sell their airtime:
 - (i) All of the larger sales houses with NAR shares greater than 5%, other than Carlton and Granada
 - (ii) Two out of the three other larger sales houses (eg Channel 4 and Five etc)
 - (iii) Either of the above permutations combined with other smaller multichannel channels or ITV licensees (SMG, UTV, Channel)
 - Whether it is appropriate to continue to prevent any of the larger sales houses, (NAR share of more than 5%) from selling their airtime with any new merged ITV sales house
 - Whether it is appropriate to maintain current rules allowing national licensees with a market share equivalent to GMTV or less to sell their airtime with Carlton and Granada after they merge their sales operations
 - Whether it is appropriate to continue to allow the non-consolidated ITV companies the option of selling their airtime with any other national licensee if they chose to do so.
- In relation to with-holding airtime and conditional selling:
 - Whether it would be appropriate to state, as part of the new *Rules*, that failure by broadcasters to sell advertising time to the maximum extent in an

attempt to restrict supply and push up prices will be considered to be prejudicial to fair and effective competition, and if so to which licensees this rule should be applied

- Whether it would be appropriate to state, as part of the new *Rules*, that the practice of conditional selling will be considered to be prejudicial to fair and effective competition, and if so to which licensees this rule should be applied

38. As previously stated, responses to the consultation should be returned by the end of Friday 14th November 2003. They should be addressed to:

Nicola Floyd

Senior Competition and Regulation Manager

ITC
33 Foley Street
London
W1W 7TL

Ofcom
Riverside House
2a Southwark Bridge Road
London SE1 9HA

Fax: 020 7306 7831
Telephone: 020 7306 7812

020 7981 3333
020 7981 3000

email: Nicola.Floyd@itc.org.uk

Annex A

ITC rules regarding Advertising Sales Arrangements issued May 2001

This statement replaces the ITC statement of 15 July 1996, which consolidated the ITC statements of 22 March and 27 April 94.

The revised rules will be effective from 17 May 2001 and will apply to any agreements made after this date.

Introduction

The ITC has a statutory duty to “ensure fair and effective competition” in the provision of licensed services. As part of this duty, it issues rules governing licensees’ airtime sales arrangements. This statement sets out revised rules, following a recent public consultation.

- **Relaxation of existing rules regarding Channel 3.**

The previous requirement whereby the ITC’s prior written consent is required for any sales arrangement involving more than one of the nine largest regional Channel 3 licensees has been removed, as has the limit of 25 per cent of total UK television advertising revenue previously placed on consent for sales organisations (whether in-house sales forces or separate sales houses) to sell advertising on behalf of television licensees.

- **Prohibition on joint selling of airtime by Granada and Carlton.**

The joint selling of airtime between Granada and Carlton, or any informal arrangement with the same effect, is prohibited. This prohibition may be subject to further review, following the passage of the Government’s Communications Bill.

- **The ban on the two London Channel 3 licensees selling their airtime together will remain.**

Because of the additional concentration of ITV’s advertising market share in the London region, the advertising time for the two London franchises must continue to be sold separately.

- **National licensees with a NAR share of 5% or less may sell airtime jointly with each other or with any other national licensee.**

This represents a relaxation of the ITC’s current rules, and will ensure continued competition for sales of national airtime between the large national commercial broadcasters, while allowing smaller licensees to sell jointly with each other or with any one of the larger broadcasters.

- **National licensees with a market share equivalent to GMTV or less may resell their airtime jointly with either of the two main Channel 3 airtime sales houses.**

This is an amendment of the existing rule, to allow GMTV to sell airtime jointly with either of the main Channel 3 airtime sales houses, if it should choose to do so.

- **Small Channel 3 licensees, that is, with 5% or less of UK NAR, may sell their airtime with any national licensees.**

This will offer an alternative to the main Channel 3 sales houses for the smaller Channel 3 licensees, such as SMG, Ulster and Channel.

- **‘Share for ITV’ deals are prohibited.**

The ITC considers that ‘share for ITV’ deals, which commit a share of the buyer’s total budget to ITV in return for preferential rates, are likely to have an anti-competitive effect. Accordingly, such deals, or any arrangement having a similar effect, are prohibited.

- **Ownership.**

The ITC will not permit the objectives of the above policy to be circumvented by a person controlling or having an interest in more than one sales organisation, where the sales organisations together handle business which could not be handled by a single sales organisation under the above rules.

The ITC will not permit any sales arrangement whereby the sales organisation includes a shareholding by an advertising agent, which would not be permissible under the Broadcasting Act 1990 in relation to a shareholding in an ITC licensee. The ITC also reserves the right to withhold consent for any sales arrangement involving a shareholding in a sales organisation (other than an ITC licensee) by a non-licensee who is a television advertiser.

- **Periodic Review**

The TV advertising market is undergoing rapid change. Over time, as more competition develops and as the market position of the main terrestrial players is eroded, it will be possible to reduce or remove the use of specific rules, and rely on general competition law. For this reason, the ITC, working with the competition authorities, will keep both the market and the revised rules under periodic review.

The policy outlined in this statement will be implemented, as necessary, by directions to the ITC licensees under the terms of their broadcasting licences.

17 May 2001