

PROJECT KANGAROO: VIRGIN MEDIA LIMITED ("VIRGIN MEDIA")

RESPONSE TO THE JV PARTIES' FURTHER REPRESENTATIONS

12 NOVEMBER 2008

1. INTRODUCTION AND EXECUTIVE SUMMARY

1.1 This submission sets out Virgin Media's observations on the following papers recently published on the Competition Commission's ("**CC**") website in relation to the proposed video on-demand ("**VOD**") joint venture between BBC Worldwide ("**BBCWW**"), Channel 4 Television Corporation ("**Channel 4**") and ITV plc ("**ITV**") (together, the "**JV Parties**"), referred to as "**Kangaroo**" (or the "**Kangaroo JV**"):

- (a) Joint Position Paper on the Effects of the Transaction on Competition, 2 October 2008 ("**Effects Paper**");
- (b) Market Definition – Additional Evidence, 13 October 2008 ("**Market Definition Paper**"); and
- (c) Updated Transaction Description ("**Transaction Description**").

1.2 Specifically, this submission is structured as follows:

- (a) Section 2 makes some general observations on the additional papers submitted by the JV Parties (in terms of structure, counterfactual and claimed benefits);
- (b) Section 3 comments on the JV Parties' approach to market definition (as set out in its Market Definition Paper);
- (c) Section 4 addresses the horizontal and vertical competition concerns arising as a result of the Kangaroo JV in relation to the syndication of content; and
- (d) Section 5 addresses the horizontal competition concerns arising as a result of the Kangaroo JV in relation to the retail provision of VOD services.

1.3 Despite the publication of the Transaction Description, it is still unclear how the Kangaroo JV will operate. In this regard, the Transaction Description and the Effects Paper exacerbate this lack of clarity as they make numerous statements on the intentions of the JV Parties, rather than explicitly stating what will actually occur or what the terms of the Kangaroo JV actually are. Notwithstanding this lack of clarity, Virgin Media's observations on the following points are worthy of note. The JV Parties' further representations may be summarised as follows:

- (a) many of the JV Parties' further representations provide, perhaps unintentional, support for Virgin Media's arguments as to why the Kangaroo JV will give rise to significant horizontal and vertical competition concerns. The JV Parties seek to address these concerns through a series of generalised statements of future intentions, none of which are certain or provable;
- (b) most of the benefits claimed by the JV Parties to arise from Kangaroo are either illusory or do not require the creation of the Kangaroo JV to be delivered. In any event, any such benefits that may arise cannot be expected to be passed on to consumers due to the very significant market power that will be enjoyed by the Kangaroo JV. Accordingly, it is clear that any such hypothetical benefits that do arise will not be sufficient to outweigh the substantial lessening of competition ("**SLC**") that will result from the Kangaroo JV. In short, the CC should be extremely wary about accepting the JV Parties' claims of hypothetical future consumer benefits, in particular given that under the counterfactual significant

benefits are already being delivered to consumers and may be expected to continue to be delivered to consumers in a more competitive environment;

- (c) the JV Parties' new Market Definition Paper raises no new arguments which have not previously been made. Further, the purported new analysis, much of which has been excised from the Market Definition Paper, does not appear to provide any cogent new evidence to suggest that the market definitions for the wholesale and retail supply of VOD services should be any different to those set out in Virgin Media's previous submissions;
- (d) nowhere in the Effects Paper do the JV Parties directly seek to address the impact on prices of the loss of horizontal competition between the JV Parties in the syndication of UK TV VOD rights to rival VOD service retailers (in the event that the Kangaroo JV and the JV Parties are prepared, in practice, to syndicate such rights to third parties). Regardless of the precise scope of the market definition for the wholesale provision of the content in the UK, Virgin Media considers that the JV Parties are each other's closest competitors for a wide range of content supplied on a VOD basis. Accordingly, Virgin Media continues to be strongly of the view that in the event that the Kangaroo JV was permitted to proceed, and was prepared to syndicate VOD rights to third party VOD service suppliers, those third parties would be forced to accept considerably worse terms (both price and non-price) for the supply of VOD content by the JV Parties;
- (e) the above horizontal concern arises only in the event that the JV Parties are prepared to syndicate content to third parties. However, nothing in the new papers addresses Virgin Media's very material concerns that the JV Parties will have both the ability and incentive to engage in input foreclosure [**CONFIDENTIAL**]. Indeed, again perhaps inadvertently, the JV Parties make a number of observations that there are very material grounds for such vertical concerns to arise; and
- (f) in considering the impact on competition in relation to the retailing of VOD content and services, the JV Parties have:
 - (i) overplayed the importance of their intention to offer a proportion of their content for free. This is simply a business choice in what is a two-sided market. There would be nothing to stop the Kangaroo JV from modifying its business model in the future to reflect market changes (e.g. a drop in advertising) or a change in strategy and therefore reduce the proportion of their content available on a free basis; and
 - (ii) very considerably overstated the competitive constraint that will be imposed on the Kangaroo JV by a combination of: (a) consumer unwillingness to pay for VOD content; (b) the perceived advantages from which other VOD service platforms benefit; and (c) the existence of other retail competitors. Moreover, the JV Parties have very materially understated the likely market position of the Kangaroo JV.

Accordingly, there is a very real risk that if the Kangaroo JV were to be permitted to proceed, it would give rise to an SLC in the retail supply of TV VOD services.

1.4 Accordingly, in the absence of suitable remedies to address the very significant horizontal and vertical competition concerns raised by Kangaroo, the CC should not permit the proposed transaction to proceed.

2. GENERAL OBSERVATIONS

2.1 This section sets out Virgin Media's general observations on the JV Parties' papers as recently published on the CC's website. In particular, the section makes some more specific comments on the JV Parties' representations in relation to:

- (a) the structure of Kangaroo;
- (b) the appropriate counterfactual;
- (c) the proposed benefits of Kangaroo; and
- (d) the fact that many of the comments made by the JV Parties support the arguments made by Virgin Media.

2.2 Each of these issues is discussed in turn below.

Structure of Kangaroo

2.3 Virgin Media has previously noted that it has found it difficult to comment on the implications of the Kangaroo JV because of the uncertainties in relation to the operation of Kangaroo. For example, on 12 September 2008, Malcolm Wall of Virgin Media told the CC during an oral hearing:

*"the form and the scope of the joint venture is still not transparent. In particular, the commercial objectives of Kangaroo remain unclear, including how these interrelate with the commercial objectives of the joint venture parties' separate VOD services, and it is also unclear whether the joint venture parties intend to continue to supply VOD content to Virgin Media and other VOD service providers."*¹

2.4 These concerns remain. First, despite the publication of the Transaction Description it is still unclear how Kangaroo will operate. In this regard, the Transaction Description and the Effects Paper exacerbate this lack of clarity as they make numerous statements on the intentions of JV Parties, rather than explicitly stating what will actually occur or what the terms of the joint venture actually are. For example, the JV Parties state:

*"It is intended that the majority of VOD content available on a temporary use basis (including almost all catch up and much archive material) will be free and advertisement supported (as opposed to DTR)."*² (Emphasis added.)

*"UKVOD intends to make available to consumers content from third parties, in addition to the content contributed by the Parties."*³ (Emphasis added.)

*"UKVOD intends to offer consumers a choice between, on the one hand, one-off viewing of a title on a free advertising-funded and/or DTR basis and, on the other hand, permanently owning a title through DTO."*⁴ (Emphasis added.)

*"The current UKVOD business plan forecasts that over 90 per cent of the anticipated transactions on the site will be free and advertising funded"*⁵ (Emphasis added.)

and

¹ Transcript, page 5.

² Transaction Description, paragraph 8.

³ Effects Paper, paragraph 2.1 (third bullet).

⁴ Effects Paper, paragraph 2.1 (fourth bullet).

⁵ Effects Paper, paragraph 5.3. See also paragraph 6.2.

*"Subject to the various carve outs, UKVOD will syndicate archive content contributed by the Parties to other sites and platforms.... Such deals may provide for distribution of the entire UKVOD service or sub-licensing of substantial representative samples of its content."*⁶ (Emphasis added.)

- 2.5 Second, the JV Parties describe the potential operation of the Kangaroo as being subject to certain exclusivity provisions,⁷ which are not explained in either the Transaction Description nor the Effects Paper. Without a full understanding of such exclusivity provisions, it is difficult to understand the scope for the JV Parties to syndicate rights to Virgin Media.
- 2.6 Third, it remains unclear to Virgin Media how the JV Parties' description of the transaction (and their intended behaviour) will be reconciled with their clear incentive to act in other ways. In this connection, it is not apparent to Virgin Media why, for example, the JV Parties will continue to compete with each other, and third parties, for the acquisition of VOD content rights (particularly if those rights are sold separately to linear rights).⁸

Counterfactual

- 2.7 Virgin Media agrees with the JV Parties' observation on the applicability of the CC's Merger Reference Guidelines which state that:

*"in applying the substantial lessening of competition test, the counterfactual will be the situation which is expected to arise in the absence of the merger under consideration. "In many cases", this will relate to the existing, pre-merger, competitive conditions. However, in "certain circumstances" the Commission will need to consider other factors that "may be expected"."*⁹

- 2.8 Virgin Media observes that nascent markets exhibiting significant growth and innovation, such as the VOD service and content markets in the UK, are precisely the types of markets where it would be inappropriate to assess a proposed transaction only against the existing, pre-merger competitive conditions.
- 2.9 Virgin Media also agrees with the JV Parties' observation that when determining the counterfactual, it would be appropriate to take account of possible market changes where *"there was a reasonable expectation that they would arise in the near future"*¹⁰. In this connection, as a customer of, and potential competitor to, BBCWW, Virgin Media expects that BBCWW would, absent Kangaroo, launch its own retail VOD service. This is particularly so given that BBCWW's competitors in the supply of VOD content rights already have reasonably well-developed, vertically integrated, retail VOD services and it is in BBCWW's interest to match the competitive offerings of its competitors. Accordingly, Virgin Media rejects the JV Parties' argument that given the *"significant uncertainty about whether it would enter the market and about the likely scope of its activities, ... it would be wrong to assume that [BBCWW] will be a standalone competitor offering a broad and comprehensive range of content."*¹¹
- 2.10 In the Effects Paper the JV Parties also argue that, in relation the independent ITV and Channel 4 archive content services, *"[t]here is no basis for an assumption that either [JV] Party would develop their retail archive offering to the same extent as would be developed*

⁶ Effects Paper, paragraph 9.3.

⁷ Effects Paper, paragraph 2.1 (last bullet).

⁸ Effects Paper, paragraph 1.6.

⁹ From the CC's Merger Reference Guidelines at paragraph 1.22 and quoted by the JV Parties in the Effects Paper, paragraph 3.8.

¹⁰ Effects Paper, paragraph 3.8.

¹¹ Effects Paper, paragraph 3.14.

on UKVOD".¹² In other words, the JV Parties appear to be suggesting that the Office of Fair Trading was wrong to consider the relevant counterfactual to be that ITV and Channel 4 would continue to offer independent archive content VOD services because those services would not provide an offering equivalent to that of Kangaroo. This represents a fundamental mischaracterisation of the standard counterfactual analysis, under which the relevant consideration is the extent to which competition will be lessened by the proposed transaction relative to the relevant counterfactual. The benefits of the proposed transaction relative to the counterfactual must be assessed separately.

Benefits of the Kangaroo JV

- 2.11 The JV Parties have repeated their claim that Kangaroo will result in significant benefits to consumers.¹³ As a preliminary point, Virgin Media refers to its earlier observations that:
- (a) most of the claimed benefits of the Kangaroo JV arise out of the creation of a single VOD supplier that will have significant market power, in particular as a result of control of attractive UK TV VOD content;¹⁴
 - (b) the benefits claimed by the JV Parties do not require the creation of Kangaroo; these benefits would accrue in any event if the JV Parties' content were to be wholesaled to downstream VOD service providers;¹⁵ and
 - (c) the CC should be wary about accepting the JV Parties' claims of hypothetical future consumer benefits, in particular given that under the counterfactual significant benefits are already being delivered to consumers and may be expected to continue to be delivered to consumers. This high level of innovation is a direct result of a large number of VOD content providers and VOD service providers competing to establish and provide a market leading service. Absent the Kangaroo JV, Virgin Media expects that this innovation and competition would continue unabated, may even intensify, leading to continuing consumer benefits.¹⁶
- 2.12 In relation to the specific arguments set out by the JV Parties in the Effects Paper as to the benefits of the Kangaroo JV, Virgin Media would make the following observations.
- 2.13 First, the benefits of a "one-stop shop" are significantly overstated by the JV Parties. For example, the JV Parties claim that Kangaroo will enable viewers to more easily find content.¹⁷ However, there are virtually no search or switching costs for consumers in comparing and using the VOD services provided on different web sites/platforms¹⁸. In this regard, search engines (such as Google) enable archived and catch-up VOD content to be located between websites quickly and easily. This means that there are no obvious search or switching cost saving benefits to customers from having a library of VOD content on a single website.
- 2.14 Second, the JV Parties appear to argue that the demand-side network effects of Kangaroo (i.e. that there is an increasing value to users as more content is added to Kangaroo, which in turn will stimulate higher demand and a broader range of content)¹⁹ are a direct

¹² Effects Paper, paragraph 3.12

¹³ Effects Paper, paragraphs 3.15 to 3.26.

¹⁴ Virgin Media's Main Submission to the CC dated 24 July 2008 ("**Main Submission**"), paragraph 7.11.

¹⁵ Virgin Media Oral Hearing 12 September 2008, comments by Malcolm Wall at Transcript, pages 5 to 6.

¹⁶ Main Submission, paragraph 7.14.

¹⁷ Effects Paper, paragraph 3.16.

¹⁸ This is acknowledged by the JV Parties in the Effects Paper, Annex 4, paragraph 1.1 (sixth bullet): "*customer switching is easy over the internet*".

¹⁹ See, for example, Effects Paper, paragraph 3.20.

consequence of the Kangaroo JV, implying that such network effects would only arise as a result of Kangaroo. However, the same positive feedback loop applies to all VOD service providers, including Virgin Media, so long as VOD service providers have access to attractive VOD content, such as that from the JV Parties. Access to attractive VOD content from the JV Parties would stimulate competition between VOD service providers which would in turn lead to increased quality, innovation and choice, and reductions in prices.

- 2.15 Third, there are no obvious economies of scale to suggest that there are material cost saving benefits to Kangaroo, which would not otherwise arise from the JV Parties providing VOD services and content individually. The JV Parties suggest that they will benefit from economies of scale in relation to digitisation, transcoding/content preparation, rights clearance and content storage/hosting costs.²⁰ However, it is not obvious how these claimed economies of scale arise from the Kangaroo JV, nor is the magnitude of such cost savings clear. In particular, these costs are largely variable costs (as opposed to fixed costs which are relevant to an assessment of the economies of scale) as they would be incurred in relation to each individual piece of content added to the service (for example digitisation, rights clearance and transcoding/content preparation costs). Further, even if there were cost savings to Kangaroo from achieving economies of scale, the reduction in competition which arises from the transaction means that any such cost saving benefits are unlikely to be passed on to consumers.
- 2.16 Fourth, in paragraph 3.23 (third bullet) the JV Parties state that *"it is unlikely that, absent a joint venture similar to Kangaroo, a third party would be able to replicate the output and effect of UKVOD, through entering into syndication deals with the three Parties"*. Quite apart from the fact that this observation suggests that no other VOD service will be able to compete effectively with the Kangaroo JV (thereby suggesting that Kangaroo will have market power), the transaction costs, execution risks etc. described by the JV Parties are evident in all markets. A strategy of vertical integration to address those costs and risks will not result in a better outcome for consumers where, as in this case, it will lead to substantial market power. This is because a lack of competition will mean that none of the alleged benefits will be passed on to consumers.
- 2.17 Fifth, it is not clear, in the context of the CC's assessment, for what purpose the JV Parties are making their claims that the Kangaroo JV will be pro-competitive and/or give rise to consumer benefits. The CC's guidance on merger references identifies two circumstances in which efficiencies/benefits might be taken into account:
- (a) first where they lead to an increase in rivalry such that there is no substantial lessening of competition;²¹ and
 - (b) when considering remedies the CC may, in exceptional circumstances, have regard to the effects of any action on any relevant customer benefit arising from the relevant merger situation concerned.²²
- 2.18 The JV Parties do not appear to have conducted their assessment of the efficiencies and/or benefits arising from the Kangaroo JV by reference to either (a) or (b) above. It is certainly not clear from the Effects Paper that the observations on consumer benefits are made in the context of either. Nevertheless, irrespective of the intentions of the JV Parties, it is clear that such benefits and efficiencies as are claimed by the JV Parties will not satisfy the relevant conditions in either case.

²⁰ Effects Paper, paragraph 3.19.

²¹ Merger references: Competition Commission guidelines at paragraphs 3.26 and 3.27.

²² Merger references: Competition Commission guidelines at paragraphs 4.34 to 4.45.

- 2.19 Turning first to the circumstances in which efficiencies may be taken into account by the CC by applying the SLC test, the CC will need to form an expectation:
- (a) that the claimed efficiencies result within a short period of time;
 - (b) that the claimed efficiencies result as a direct consequence of the merger; and
 - (c) that the efficiencies will increase rivalry amongst the remaining firms in the market.²³
- 2.20 Without dealing with each of these criteria in detail, it is clear that neither the second nor the third condition will be met. In particular, as indicated above, Virgin Media does not consider that any of the efficiencies/consumer benefits raised by the JV Parties are dependent on the creation of Kangaroo, and nor does Virgin Media consider that there are any circumstances in which the creation of the Kangaroo JV will increase rivalry amongst remaining firms in the market. Quite to the contrary, if the Kangaroo JV is permitted to proceed, it is very likely to attain a position of market power which will not be constrained by the remaining firms in the market.
- 2.21 As regards the circumstances in which customer benefits can be taken into account by the CC in considering remedies, the Enterprise Act 2002 provides that a benefit is only a relevant customer benefit if the CC believes that:
- (a) the benefit may be expected to accrue within a reasonable period as a result of the creation of a relevant merger situation concerned; and
 - (b) the benefit is unlikely to accrue without the creation of that situation or a similar lessening of competition.²⁴
- 2.22 In each case the burden is upon the merging parties to provide evidence that any claimed benefit does in fact fall within the meaning of a relevant customer benefit.
- 2.23 Virgin Media considers that the JV Parties have failed completely to make any case that the customer benefits or efficiencies to which they point in the Effects Paper satisfy the relevant criteria. In particular, the JV Parties have failed to demonstrate that any of the relevant customer benefits would be unlikely to accrue absent the Kangaroo JV.
- 2.24 In conclusion, most of the benefits claimed by the JV Parties to arise from Kangaroo are either illusory or do not require the creation of the Kangaroo JV to be delivered. Such benefits as may arise will be a consequence of the creation of a single VOD supplier that will have significant market power and cannot, therefore, be expected to be passed onto consumers. Those limited benefits do not, therefore, outweigh the clear SLC arising from Kangaroo. In short, the CC should be extremely wary about accepting the JV Parties' claims of hypothetical future consumer benefits, in particular given that significant benefits are already being delivered to consumers and may be expected to continue to be delivered to consumers under the counterfactual.

Other Observations

- 2.25 Many of the comments made by the JV Parties support arguments made by Virgin Media to both the Office of Fair Trading and the CC.
- 2.26 First, the JV Parties acknowledge the importance of having a range of attractive content in order to have a viable VOD service. For example, the JV Parties acknowledge that:

²³ Merger references: Competition Commission guidelines at paragraph 3.27.

²⁴ See section 30(3) of the Enterprise Act 2002.

"None of the Parties alone have a sufficient range of material to provide the scope of content that would be available on UKVOD thus making it difficult to credibly market an archive based proposition".^{25 26}

2.27 This is consistent with Virgin Media's views. Virgin Media has repeatedly argued that a range of attractive content is essential to its VOD service and that the JV Parties are each other's closest competitors in the supply of such UK TV VOD content. Specifically, Virgin Media has previously demonstrated that content from the JV Parties anchors its VOD service (see Virgin Media's Main Submission, paragraph 3.27) and that this content is necessary for an attractive and viable VOD service (see, for example, Main Submission, paragraph 4.66).

2.28 Second, related to this point, the JV Parties make statements which imply that the JV Parties will have market power as a result of Kangaroo. For example, the JV Parties refer to the advantages of having access to catch-up content and the ability to promote a wide range of UK archive content. The JV Parties go on to state:

*"No third party can be reasonably expected to attract more users with a propensity to view archive content and therefore be in a position to make available as much archive content as UKVOD."*²⁷

2.29 This is also consistent with Virgin Media's views. In this connection, Virgin Media reiterates that Kangaroo's stranglehold over key content will result in Kangaroo having significant market power over the syndication of such VOD content.²⁸ In addition, as a result of Kangaroo's market power over the syndication of such VOD content rights, the Kangaroo JV will have both the ability and incentive to engage in input foreclosure²⁹.

2.30 Third, the JV Parties have concluded that a viable and competitive VOD proposition must focus on *"providing a 'one stop shop' for a range of material that has appeared on UK television"*.³⁰ It is implicit in this statement that the JV Parties are acknowledging that UK television viewing drives VOD service viewing. This is consistent with Virgin Media's view. Virgin Media has repeatedly argued that linear viewing of the most popular UK TV channels drives VOD viewing.³¹

2.31 Fourth, the JV Parties explicitly acknowledge that Kangaroo will result in a reduction of horizontal competition in relation to the retail provision of VOD services. In this regard, the JV Parties state:

*"Any reduction in horizontal rivalry between the Parties in relation to transactional content, on any market definition, would therefore only be very modest and, in any event, would be outweighed by the benefits to consumers from UKVOD."*³²

²⁵ Effects Paper, paragraph 3.23 (first bullet).

²⁶ Virgin Media also notes that the JV Parties mischaracterise the scope of Kangaroo in this quote. It is clear from the Effects Paper (see, for example, paragraph 2.1 (second bullet)) and the Transaction Description (see, for example, paragraph 6) that Kangaroo will also include "current and recent" material, including catch-up content in some form. This is supported by comments by Kangaroo CEO Ashley Highfield who recently stated: *"We envisage that a lot of traffic will come through the door from catch-up television, then we will take them on a journey through the back catalogue and paid content."* See Robert Andrews @Mipcom:Kangaroo Plans to Offer US shows, Movies; Closed Beta Due For Christmas Paid Content: UK, 15 October 2008 ("**Paid Content: UK Article**").

²⁷ Effects Paper, paragraph 3.24.

²⁸ Main Submission, paragraphs 4.54 to 4.67.

²⁹ Main Submission, paragraphs 6.1 to 6.18.

³⁰ Effects Paper, paragraph 3.23 (second bullet).

³¹ See, for example, Main Submission, paragraphs 4.13 and 4.37.

³² Effects Paper, paragraph 7.2.

and

"For the businesses that are going into the joint venture...UKVOD will be providing the service and the Parties will have no or only limited relevant market activities".³³

2.32 The JV Parties have sought to address this loss of horizontal rivalry by relying on claimed "benefits". However, as reiterated by Virgin Media above (see from paragraph 2.11), these benefits are by no means certain and, in any event, do not require the creation of Kangaroo in order to be delivered.

2.33 The JV Parties have also sought to address underlying competition concerns with a series of statements of future intentions as regards the conduct of Kangaroo, none of which are certain or provable. For example, the JV Parties have sought to placate the concerns about Kangaroo having a stranglehold on key content by claiming that Kangaroo, or the JV Parties individually, will supply competing downstream retailers with VOD content. In this connection, it is very clear that there will be no obligation on Kangaroo or the JV Parties to supply this content. Rather, it is merely stated that:

"It is envisaged that the UKVOD service will be distributed so that it is also available on pay TV platforms."³⁴ (Emphasis added.)

"The UKVOD business plan assumes that it will actively seek syndication agreements. It is envisaged that UKVOD will be able to syndicate its whole service (or a substantial representative sample) to closed platforms and, after a period of 12 months to allow for the establishing or the website, to open services."³⁵ (Emphasis added.)

and

"The UKVOD business model assumes that it will seek syndication and sub-licensing agreements with third party platforms for archive content."³⁶ (Emphasis added.)

2.34 These statements on the intentions, assumptions and business plans of the JV Parties provide no comfort to Virgin Media about the future behaviour of Kangaroo and the individual JV Parties. As the CC is well aware, business plans can change and, even if these statements do represent the current intentions of the JV Parties, there is no guarantee that these intentions will not change. Indeed, in Virgin Media's view, it is highly likely that the business plans and commercial incentives of the JV Parties and the Kangaroo JV will inevitably change over time.

2.35 In short, the CC cannot rely on short term statements of intention (even if accurate) to address the competition concerns arising from the combination of the three most important suppliers of VOD content in the UK.

3. MARKET DEFINITION

3.1 The JV Parties claim that the Market Definition Paper provides additional evidence related to market definition for both the wholesale and retail VOD markets. The new evidence provided by the JV Parties includes the following: an analysis of consumers' viewing patterns on UK linear TV; an analysis of the DVD market; and a consumer survey on viewer preferences.

³³ Effects Paper, Annex 4, paragraph 1.4 (second bullet).

³⁴ Transaction Description, paragraph 3.

³⁵ Transaction Description, paragraph 20(e).

³⁶ Effects Paper, paragraph 2.1, last bullet.

3.2 A detailed consideration of the Market Definition Paper is attached at Annex 1. However, in summary, Virgin Media considers that the additional memorandum raises no new arguments which have not previously been made. Further, the purported new analysis, much of which has been excised from the Market Definition Paper, does not appear to provide any cogent new evidence to suggest that the market definitions for the wholesale and retail supply of VOD services should be any different to those set out in Virgin Media's Main Submission.

4. **SYNDICATION OF VOD CONTENT**

4.1 In its Main Submission Virgin Media raised two separate categories of competition concerns in relation to the syndication of VOD TV content by the Kangaroo JV and by the JV Parties:

- (a) a horizontal concern that the Kangaroo JV has removed the prospect of horizontal competition between the JV Parties in the supply of TV VOD rights to third party VOD service suppliers. This would be liable to cause third party VOD service suppliers to accept considerably worse terms (both price and non-price) for the supply of VOD content than would previously have been the case,³⁷ and
- (b) the vertical concern that the JV Parties would, as a consequence of the Kangaroo JV, have both the ability and incentive to engage in input foreclosure [**CONFIDENTIAL**].³⁸

4.2 In each case, the Kangaroo JV is expected to result in adverse effects on consumers.³⁹ In this regard, Virgin Media notes that it is not alone in expressing such concerns regarding the anti-competitive effects of the transaction.⁴⁰

4.3 The JV Parties have attempted to address the concerns expressed by Virgin Media and numerous other third parties in their further representations. However, Virgin Media does not consider that the JV Parties have provided any new credible evidence to suggest that such competition concerns will not materialise. The observations made by the JV Parties are addressed in turn below.

Loss of horizontal competition in syndication of rights

4.4 Notwithstanding the fact that the Effects Paper is nearly 73 pages long (including annexes) the JV Parties fail to address directly why the loss of horizontal competition between the JV Parties in the syndication of VOD content will not allow the Kangaroo JV or the JV Parties to increase prices.

4.5 The majority of the observations made by the JV Parties in the Effects Paper in relation to syndication of VOD rights seek to address the question of whether the Kangaroo JV will have the ability and incentive to engage in input foreclosure (i.e. the vertical issue, which is addressed below). The only comments made by the JV Parties that are relevant to the horizontal question of whether the Kangaroo JV will have market power over the syndication of VOD content rights are that:

- (a) the retail VOD platforms and services to which the Kangaroo JV could syndicate its content are large and powerful enterprises in their own right (i.e. the JV Parties suggest that countervailing buyer power will be sufficient to offset the horizontal

³⁷ See, for example, paragraphs 5.8 to 5.13 of the Main Submission.

³⁸ [**CONFIDENTIAL**].

³⁹ See, for example, paragraph 5.12 in relation to the loss of horizontal competition and paragraphs 6.19 to 6.20 of the Main Submission in relation to vertical concerns.

⁴⁰ The following companies/bodies, for example, also raised such concerns: PACT, Joost, Tiscali and Sky.

market power of the Kangaroo JV in relation to the syndication of VOD rights);⁴¹ and

- (b) the platforms and services to which the Kangaroo JV might syndicate its VOD content have access to content from other producers (i.e. retail VOD platforms have various "outside options" for VOD content other than to rely on the JV Parties).⁴²

Each observation is addressed in turn below.

Countervailing buyer power

4.6 The JV Parties appear to be suggesting that the loss of horizontal competition between the JV Parties in the syndication of VOD rights will be counterbalanced by the purchasing power on the part of their principal customers. As Virgin Media is one of the most significant actual and potential purchasers of VOD content in the UK, Virgin Media considers that this suggestion is entirely without foundation.

4.7 As emphasised by the UK's Office of Fair Trading's substantive assessment merger guidelines and the European Commission's guidelines on the assessment of horizontal mergers, countervailing buyer power in relation to the syndication of VOD rights will typically depend upon the ability of buyers to:

- (a) reduce, or credibly threaten to reduce, their purchases of VOD content from the Kangaroo JV by switching, or credibly threatening to switch to rival suppliers of VOD content;
- (b) threaten to enter the market for the syndication of VOD rights themselves or sponsor entry by others (such as by offering a new entrant a long term contract); and/or
- (c) otherwise impose costs on the Kangaroo JV even where buyers have no choice but to take the supplier's products.

In this regard, Virgin Media considers that none of the factors relevant to the assessment of countervailing buyer power apply in this case.

4.8 **[CONFIDENTIAL]**. In this regard **[CONFIDENTIAL]**, Virgin Media's direct experience is entirely at odds with the estimate of the JV Parties that the Kangaroo JV's syndication market share will be well under 25 per cent.⁴³ In particular:

- (a) BBCWW and Channel 4 content accounts for **[CONFIDENTIAL]** per cent of all views of TV VOD content⁴⁴ on Virgin Media's VOD service, **[CONFIDENTIAL]** per cent of all non-iPlayer views of catch-up TV VOD content, and **[CONFIDENTIAL]** per cent of all views of archive TV VOD content (excluding movies and music).⁴⁵ In other words, in practice, the syndication market share of the Kangaroo JV is likely to be **[CONFIDENTIAL]** that claimed by the JV Parties;
- (b) it is simply not correct for the JV Parties to assert that their content will not represent the first or second best choices for sites and platforms. As set out in the Main Submission:

⁴¹ See paragraph 9.4, fourth bullet of the Effects Paper.

⁴² See paragraph 9.4, fourth bullet and paragraph 9.5 of the Effects Paper.

⁴³ See Annex 5, paragraph 1.5, second bullet of the Effects Paper.

⁴⁴ Including catch-up, excluding movies and music.

⁴⁵ See, for example paragraph 6.6 of the Main Submission.

- (i) [CONFIDENTIAL];⁴⁶
- (ii) [CONFIDENTIAL];⁴⁷ and
- (iii) [CONFIDENTIAL].⁴⁸

4.9 [CONFIDENTIAL].⁴⁹ [CONFIDENTIAL].

4.10 As set out in Virgin Media's response to the CC's VOD supplier questionnaire of 24 July 2008 (the "**VOD Supplier Response**") [CONFIDENTIAL]. The JV Parties are, in practice, each others' closest competitors in the wholesale supply of TV VOD content, and the loss of this competitive dynamic will have a direct impact [CONFIDENTIAL].⁵⁰

4.11 [CONFIDENTIAL].

4.12 In this context, it is irrelevant that there are no significant switching costs if a site or platform wishes to change or increase the number of content suppliers from which it sources content.⁵¹ This is because switching costs only become relevant to the extent that there are alternative sources from which to obtain VOD content which will be substitutable in the eyes of customers for that of the Kangaroo JV and the JV Parties and which will continue to allow rival VOD service retailers to offer an attractive VOD service. For the reasons summarised below⁵², this is not the case.

4.13 In relation to the other factors relevant to the assessment of countervailing buyer power, it is implausible to suggest that Virgin Media could either enter or sponsor entry in the market for the syndication of VOD rights, nor is it plausible to suggest that Virgin Media could constrain/punish the JV Parties in other ways.

4.14 [CONFIDENTIAL].

Lack of availability of alternative content

4.15 The JV Parties have observed that the Kangaroo JV will not be the only, or major, supplier of content to other sites and platforms. The JV Parties suggest that this means that the availability of VOD content from third parties will constrain the ability of the Kangaroo JV to increase prices (or adversely affect terms of supply) post-merger. In this regard, Virgin Media considers that the JV Parties have materially overstated the availability of content from other suppliers and that, in practice, the availability of such content will not constrain the pricing power of the Kangaroo JV.

4.16 As indicated above, the JV Parties (even without ITV) account for an [CONFIDENTIAL] proportion of viewing of VOD content on the Virgin Media cable platform. Further, there are, in practice, no viable alternative sources of content [CONFIDENTIAL]. In summary:

- (a) [CONFIDENTIAL]. In this context, Virgin Media rejects the observations of the JV Parties in the Effects Paper that Virgin Media's VOD service would be successful without content from the Kangaroo JV and JV Parties.⁵³ On the basis of the

⁴⁶ [CONFIDENTIAL].

⁴⁷ [CONFIDENTIAL].

⁴⁸ [CONFIDENTIAL].

⁴⁹ [CONFIDENTIAL].

⁵⁰ See, further, paragraphs 21.1 and 21.2 of the VOD Supplier Response and paragraphs 5.8 to 5.13 of the Main Submission.

⁵¹ See Effects Paper, Annex 5, paragraph 1.5 (fourth bullet).

⁵² Paragraphs 4.15 to 4.18.

⁵³ See, for example, Effects Paper, paragraph 9.13.

evidence submitted to the CC,⁵⁴ there can be no doubt that the VOD content of the JV Parties is the anchor around which Virgin Media's VOD service is built [**CONFIDENTIAL**];

- (b) there is insufficient attractive US originated content to replace the content of the JV Parties. Again, in this context, Virgin Media rejects the assertion of the JV Parties that US content is viewed as more desirable than UK archive content.⁵⁵ In practice, as the range of evidence presented by Virgin Media to the CC⁵⁶ has shown, [**CONFIDENTIAL**], whilst US content complements the UK content, it is not an effective substitute either in the eyes of the consumer or from the perspective of Virgin Media;⁵⁷
- (c) [**CONFIDENTIAL**];⁵⁸
- (d) film and short-form content are not substitutable for the type and range of VOD content provided by the JV Parties; and
- (e) whilst the availability of BBC's iPlayer catch-up service on Virgin Media's platform might mitigate, to a limited extent, the impact of the loss of content from the JV Parties, Virgin Media considers that catch-up VOD services and archive VOD services fulfil different customer requirements.⁵⁹

4.17 On the basis of the above, Virgin Media has no doubt that in circumstances in which the JV Parties were permitted jointly to syndicate rights to UK TV VOD content, the existence of alternative sources of content would be wholly insufficient to constrain the market power of the Kangaroo JV. Even in relation to the syndication of VOD rights outside the scope of the Kangaroo JV, Virgin Media considers that the Kangaroo JV changes the competitive dynamic between the JV Parties, and that the Kangaroo JV raises serious concerns that it will provide a forum for the exchange of confidential information between the JV Parties in relation to the syndication of VOD rights outside the Kangaroo JV.

4.18 In conclusion, nowhere in the Effects Paper do the JV Parties directly seek to address the impact of the loss of horizontal competition between the JV Parties in relation to the syndication of UK TV VOD rights to rival VOD service retailers (in the event that the Kangaroo JV and the JV Parties are prepared, in practice, to syndicate such rights to third parties). Accordingly, Virgin Media continues to be strongly of the view that in the event that the Kangaroo JV was permitted to proceed, third party VOD service suppliers would be forced to accept considerably worse terms (both price and non-price) for the supply of VOD content by the JV Parties.

Vertical concerns - input foreclosure

4.19 The JV Parties argue that there is no prospect of the creation of UKVOD resulting in them engaging in input foreclosure for the following reasons:

- (a) the existence of competition in the syndication of VOD rights (i.e. there are a number of alternative VOD content suppliers);

⁵⁴ See, for example, Main Submission, paragraphs 3.26 to 3.27 and 4.62.

⁵⁵ Effects Paper, paragraph 9.11.

⁵⁶ See, for example, Main Submission paragraphs 3.26 to 3.27 and 4.62.

⁵⁷ See, for example, paragraphs 4.6 to 4.12 of the Main Submission.

⁵⁸ [**CONFIDENTIAL**].

⁵⁹ See paragraph 6.6 of the Main Submission.

- (b) Kangaroo will have strong incentives to supply material to a range of other sites and platforms (and the JV Parties have the right to require the Kangaroo JV to do so);
- (c) syndication of catch-up content (with the exception of DTO⁶⁰ rights) is outside the scope of the Kangaroo JV and the Kangaroo JV does not materially change the incentives to syndicate such content; and
- (d) UK content is not essential for other VOD platforms.⁶¹

Virgin Media disputes each of these assertions and addresses each in turn below.

The existence of competition in the syndication of VOD content

- 4.20 As regards the scope for input foreclosure concerns to arise in relation to the syndication of VOD content to third parties, the existence of competition at an upstream level is relevant to the competitive assessment. In this regard, the JV Parties argue that there is no risk of the Kangaroo JV engaging in input foreclosure because there are a number of alternative suppliers of VOD content.
- 4.21 For the reasons set out in paragraphs 4.15 to 4.18 above, Virgin Media continues to be strongly of the view that the JV Parties are by far and away the most important actual and potential suppliers of UK TV VOD content. In this context, the main driver for VOD take-up is the content broadcast on the most popular linear TV channels in the UK. The JV Parties account for the overwhelming majority of the VOD rights to such content, which is clearly demonstrated by the popularity of such content on the Virgin Media platform.
- 4.22 In short, the JV Parties are the three most important actual and potential suppliers of TV VOD content in the UK and they are each other's closest competitors in the supply of that VOD content. In practice, therefore, there are no viable alternative suppliers of VOD content (either individually or in aggregate) that would be able to replicate the value and quality of the content of the JV Parties in the event that the Kangaroo JV were to either refuse to syndicate VOD content to rival VOD service providers, or do so only on uneconomic terms.
- 4.23 In conclusion, there is no prospect of competition from alternative VOD content suppliers limiting the ability of the Kangaroo JV and the JV Parties successfully to engage in input foreclosure [**CONFIDENTIAL**].

Incentives of the Kangaroo JV to syndicate VOD content

- 4.24 The JV Parties claim that the Kangaroo JV will have strong incentives to syndicate VOD content to other platforms and services. Virgin Media rejects this assertion. Virgin Media set out in detail in paragraphs 6.10 to 6.18 of its Main Submission why it considered that the Kangaroo JV and the JV Parties would have an incentive to engage in input foreclosure. Without repeating each of those observations, Virgin Media sets out below a number of observations on the claims of the JV Parties.
- 4.25 [**CONFIDENTIAL**].⁶²
- 4.26 Second, Virgin Media observed that where a particular service is in its infancy and is expected to grow significantly there is a greater incentive for a vertically integrated operator to seek to win customer share as quickly as possible and thereby entrench its position in the future. The fact that this incentive exists, and the fact that the JV Parties

⁶⁰ Download to own.

⁶¹ See paragraph 9.1 of the Effects Paper.

⁶² [**CONFIDENTIAL**].

recognise it exists, is clearly flagged in footnote 49 to paragraph 9.3 of the Effects Paper. In that footnote the JV Parties indicate that the Kangaroo JV will not be able to syndicate content to open VOD services for a period of 12 months "*in order to build a sufficient degree of profile for the UKVOD service*". This clearly demonstrates that a strategy of withholding content from rival service providers is expected by the JV Parties to drive customers to the Kangaroo JV and to enable the Kangaroo JV to grow its retail subscriber base. In short, this observation on the part of the JV Parties is a clear admission that the Kangaroo JV has the incentive to engage in input foreclosure.

4.27 Third, as regards archive content, the JV Parties argue⁶³ that as consumers have a preference for viewing VOD over TV sets, the reach of the Kangaroo JV service can be increased considerably by making either the relevant content or the Kangaroo JV service available to TV platform VOD services. Virgin Media considers that the JV Parties have materially overstated the impact of this factor on the incentive of the JV Parties to syndicate VOD content to rival VOD service providers:

- (a) as set out in paragraphs 4.29 to 4.32 of Virgin Media's Main Submission, Virgin Media considers that the TV platform VOD service offered over its cable platform provides a technically superior and richer customer experience than that offered by internet VOD service providers. However, as a consequence of current developments and technology which enable content delivered by broadband to be viewed on a television, there is already a very significant degree of convergence between VOD content delivered via broadband and VOD content viewed over TV. In practice, in the very near future all VOD content however delivered will be capable of being viewed on a television set;
- (b) a number of public statements have been made by the JV Parties to the effect that it is the intention of the JV Parties to offer the Kangaroo JV service over TV platforms. By way of example, at the press launch of Freesat, the free digital satellite joint venture between the BBC and ITV, Mark Thompson, the BBC Director General, indicated the plans for Freesat include offering access to on-demand programming via broadband TV services including Kangaroo.⁶⁴ In addition, Virgin Media understands that the JV Parties are in discussions in relation to plans to offer the Kangaroo service over the Freeview (DTT) platform. As the Freeview (DTT) platform has very considerably greater reach than that of Virgin Media this would considerably reduce any limited incentive for the Kangaroo JV to access Virgin Media's TV VOD customers; and
- (c) the points raised above clearly demonstrate that any incentive to access existing TV VOD customers (such as those of Virgin Media) will only be short term. In other words, to the limited extent that there is currently an incentive on the part of the Kangaroo JV to access those customers, this incentive is likely to reduce very significantly in a very short period of time. At that point there will be nothing to prevent Kangaroo, having established itself, from ceasing to syndicate content, or services, to rival VOD service providers. In other words, the market power of the Kangaroo JV will be enduring whereas the incentive to syndicate content to third parties is very likely to reduce over time.

4.28 Fourth, as set out in Virgin Media's further observations on Project Kangaroo of 28 October 2008 ("**Further Observations**"), Ofcom's Pay TV Investigation Second Consultation Document made it very clear that where a vertically integrated operator controls key content (as will be the case for the Kangaroo JV), access to which is crucial to the ability of rival downstream retailers to offer attractive service (as is the case in relation to the content owned by the JV Parties), the vertically integrated operator will have the incentive and ability either to refuse to supply that content to competing

⁶³ See paragraph 9.4, first bullet of the Effects Paper.

⁶⁴ See paragraph 6.14 of the Main Submission.

retailers, or to offer it on uneconomic terms. Those incentives need to be considered both in the short and long term. In other words, the vertically integrated operator will have an incentive to forego wholesale revenues in the short term in order to deliver a long term strategic outcome.

- 4.29 In summary, Virgin Media continues to be of the view that the Kangaroo JV will have a very strong incentive to engage in input foreclosure as regards the archive content which will form part of the Kangaroo JV. This is explicitly recognised by the JV Parties (see paragraph 9.3, Footnote 49 of the Effects Paper). (The incentive to engage in input foreclosure in relation to catch-up material, which is purportedly outside the scope of the Kangaroo JV is addressed below). Further, even if were the case that in the short term the Kangaroo JV may have some limited incentives to syndicate content to enlisting TV platforms, that incentive is likely to reduce very materially and very quickly. In this context, it should be emphasised that the CC must look beyond the short term when assessing the potential impact on competition of the Kangaroo JV.

Syndication of catch-up content is outside the scope of the Kangaroo JV

- 4.30 The JV Parties argue that because the syndication of catch-up content is outside the scope of the Kangaroo JV, the Kangaroo JV does not materially change the incentive for the JV Parties to syndicate such content. As a matter of simple factual and economic logic, this statement is incorrect.
- 4.31 Prior to the creation of the Kangaroo JV, the individual JV Parties had the choice of exploiting VOD rights themselves and/or making them available to third party VOD service retailers for exploitation. The creation of the Kangaroo JV has materially changed that dynamic as it has provided an alternative vehicle for the JV Parties to exploit the value of their VOD content (a vehicle in which each of the JV Parties has a clear economic interest).
- 4.32 Prior to the creation of the Kangaroo JV, the incentives of each of the JV Parties to syndicate rights depended largely on a trade-off between: (i) the additional revenue available from syndicating catch-up rights to third parties and (ii) any resulting loss of revenue (or other benefits) obtained from viewers watching the content on rival VOD services. Subsequent to the creation of the Kangaroo JV, the trade-off is different. Each of the JV Parties must, when deciding whether to syndicate VOD catch-up rights, consider the trade-off between the following:
- (a) the additional revenue available from syndicating catch-up rights to third parties;
 - (b) the loss of revenue (or other benefits) obtained from fewer viewers watching the content on rival VOD services; and
 - (c) the loss of revenue (or other benefits) resulting from fewer viewers switching to watch their content (and other content) on the Kangaroo JV.
- 4.33 The loss of revenue to the Kangaroo JV from the JV Parties independently syndicating VOD rights is potentially large, particularly in circumstances where advertising revenue depends upon viewer numbers. In very simple terms, following the creation of the Kangaroo JV, each of the JV Parties must now have regard to the impact of their decisions in relation to syndicating content to third parties on the revenues and success of the Kangaroo JV. Prior to the creation of the Kangaroo JV, this was not a consideration.
- 4.34 Further, as set out in the European Commission's non-horizontal merger guidelines, a vertical merger may give rise to competition concerns if the merged entity is able to "*gain access to commercially sensitive information regarding the upstream or downstream activities of rivals*".⁶⁵ In this regard, the Kangaroo JV provides a forum by which the JV

⁶⁵ Paragraph 78 of the European Commission's guidelines on the assessment of non-horizontal mergers.

Parties will be able to discuss the syndication of VOD content rights, which potentially raises serious concerns regarding the flow of confidential information regarding competing VOD service providers and the prices which will be charged for the syndication of VOD content rights by the individual JV Parties.

- 4.35 In summary, it is disingenuous for the JV Parties to attempt to suggest that because the syndication of catch-up content lies outside the Kangaroo JV, the Kangaroo JV does not materially change the incentives to syndicate such content.⁶⁶

UK content is essential for other VOD platforms

- 4.36 The JV Parties assert that there is no risk of input foreclosure arising from the Kangaroo JV because UK content is not essential for other VOD platforms. As set out repeatedly in Virgin Media's submissions to the CC (and summarised in paragraphs 4.15 to 4.18 above) this is simply not true. The UK VOD content of the JV Parties [**CONFIDENTIAL**] to Virgin Media in order to enable it to continue to provide an attractive VOD service.
- 4.37 That aside, all of the observations made by the JV Parties as to the necessity of their content for rival service providers are made against the background of the current state of the market (i.e. a market in which the Kangaroo JV is yet to offer a "one-stop shop" for VOD content). In circumstances in which the Kangaroo JV has been given permission to proceed and is offering the anticipated "one-stop shop" for VOD content, it will become even more essential for rival VOD services to have access to the content of the JV Parties in order for them to be able to compete with the Kangaroo JV for customers.
- 4.38 In conclusion, it is just not credible for the JV Parties to claim, as they do, in paragraph 9.14 of the Effects Paper, that if the Kangaroo JV were not to syndicate content to third parties, it would have little impact on the ability of third party platforms to offer attractive content to consumers. The Effects Paper and the Market Definition Paper provide no additional evidence or arguments to address Virgin Media's very material concerns, as expressed in its Main Submission and subsequent submissions, that the creation of the Kangaroo JV may be expected to give rise to very material horizontal and vertical concerns in relation to the syndication of UK VOD TV content.

5. THE RETAIL PROVISION OF VOD SERVICES

- 5.1 This section considers, in turn, the horizontal competition concerns resulting from the Kangaroo JV in relation to the retail provision of VOD services.
- 5.2 The JV Parties seek to demonstrate that the Kangaroo JV will not result in horizontal competition concerns in relation to the retail provision of VOD services by arguing that:
- (a) 90 percent of transactions will be free to consumers;⁶⁷
 - (b) the JV Parties and Kangaroo are at a competitive disadvantage vis-à-vis these other VOD service providers;⁶⁸ and
 - (c) Kangaroo will not have a large market share and that there are a lot of other retail VOD service providers competing with the JV Parties who will continue to compete with Kangaroo.⁶⁹

⁶⁶ As an additional point, it is difficult to see how the involvement of each of the JV Parties in the Kangaroo JV will not lead to an increase in transparency between the JV Parties as to the price of content (whether it be catch-up or archive) which is syndicated to rival VOD service providers.

⁶⁷ See, for example, Effects Paper, paragraph 6.2.

⁶⁸ See, for example, Effects Paper, paragraph 5.5 to 5.18.

⁶⁹ See, for example, Effects Paper, paragraph 5.11.

Each claim is addressed below.

Content will be made available for free

- 5.3 The decision on the part of the Kangaroo JV to make a large proportion of content available to consumers for free is purely a business model choice, which exists because of the two-sided nature of the VOD market. There would be nothing to stop the Kangaroo JV from modifying its business model to reflect market changes. For example, the Kangaroo JV might change its business model in circumstances in which an advertising-funded business model ceases to be viable (e.g. due to a drop in advertising rates as a result of the deterioration in advertising market conditions) or because, having established itself as a "one-stop shop" and achieved market power in relation to the retail supply of VOD services, the Kangaroo JV considers that it has greater ability to generate revenue from viewers. In other words, given that the Kangaroo JV already expects 10 per cent of content to be paid-for by viewers, it would be simple for the Kangaroo JV to adjust the mix of advertising and subscription funding depending on varying market conditions.

Claimed advantages of other platforms

- 5.4 The JV Parties specifically argue that competing VOD service providers have a number of advantages over the JV Parties and Kangaroo. In this regard, the JV Parties claim that the rationale of the Kangaroo JV is to:

*"create a customer proposition that can compete in the VOD market against powerful competitors who are able to leverage significant existing assets that the broadcasters do not possess (e.g. an established closed platform customer base, an installed base of proprietary hardware devices, an established internet retail presence, global reach)."*⁷⁰

- 5.5 Before discussing the specific "advantages" the JV Parties claim that competing VOD service providers benefit from, it is worth noting that the BBC was able to launch its highly successful iPlayer services despite not benefiting from these so-called "advantages". Against this background, Virgin Media discusses some of the claimed "advantages" as presented by the JV Parties below.

- 5.6 First, the JV Parties claim that closed VOD platforms and games consoles have a strong retail market advantage because they enable viewers to watch VOD content on the television, for which consumers have demonstrated a strong preference.⁷¹ In this regard, Virgin Media has previously stated that although it considers its TV-based VOD service to be a richer and technically superior service to an Internet-based VOD service, Internet-based VOD services are becoming more popular (for example, the BBC's iPlayer).⁷² Further, technological developments are expected to enable Internet-based VOD services to be viewed on a television⁷³. Accordingly, *"it is clear that to the extent that there could ever have been a material distinction drawn between the VOD services made available over a broadband connection and those made available over TV, that distinction has in practice already become meaningless."*⁷⁴ As such the "strong retail market advantage" that the JV Parties identified, to the extent it ever existed, has been eroded, and will continue to be eroded, by technological and market developments.

⁷⁰ Effects Paper, paragraph 3.15. See also paragraph 5.15.

⁷¹ Effects Paper, paragraphs 5.7 to 5.8.

⁷² Main Submission, paragraph 4.29.

⁷³ Main Submission, paragraph 4.30.

⁷⁴ Main Submission, paragraph 4.31.

- 5.7 Second, the JV Parties claim that personal video recorders ("**PVR**") are a further advantage enjoyed by closed platform VOD service providers.⁷⁵ As stated in the Main Submission⁷⁶, Virgin Media does not consider that PVRs compete in the same market as the provision of retail VOD services. Further, PVRs are not essential to attracting and retaining VOD viewers.
- 5.8 Third, the JV Parties argue that access to a range of premium sports, movies and adult content is important in relation to the success of a VOD service⁷⁷. This is simply not correct. To date, VOD services have taken off on the back of attractive TV VOD content such as UK dramas that are first shown on linear TV. Further, sports rights are generally not provided on a VOD basis and, for the reasons discussed in the Main Submission⁷⁸, movie VOD content is generally not substitutable for TV VOD content and therefore should not be considered to compete in the same market.
- 5.9 Fourth, the JV Parties claim that other VOD service providers such as Amazon and iTunes benefit from a strong internet retail base.⁷⁹ Although a well known brand and internet presence may be of some advantage, the JV Parties are the best known brands as regards the provision of UK TV content and cannot be expected to have any difficulty in creating an on-line presence. In addition, the JV Parties envisage (at least currently) that the vast majority of their content will be provided on free or advertisement funded basis. This being the case, it is not clear why a strong internet retail base is a clear advantage.
- 5.10 Fifth, the JV Parties argue that VOD service retailers such as Apple, Microsoft and Sony have the ability to strike global content deals and that this gives them a competitive advantage. In Virgin Media's experience, demand for content varies materially from jurisdiction to jurisdiction and that existing UK VOD customers have a very strong preference for UK content. Accordingly, the JV Parties have materially overstated the advantage in being able to strike global content deals.
- 5.11 However, even if these claimed advantages of other platforms do exist to some degree, it is apparent that all these advantages are worthless unless the VOD service provider in question has access to attractive, desirable, content on sustainable economic terms. As mentioned above, the JV Parties hold the rights to the vast majority of the most attractive UK TV VOD rights and, without access to that content on economic terms, Virgin Media would be unable to continue to offer an attractive VOD service.
- 5.12 As a consequence, the JV Parties could easily mitigate against the claimed advantages of other VOD service providers [**CONFIDENTIAL**]⁸⁰ [**CONFIDENTIAL**]. Indeed, the greater the advantages that the Kangaroo JV perceives operate to the benefit of other VOD service providers, the greater the incentive for the Kangaroo JV to engage in input foreclosure.
- 5.13 In summary, Virgin Media considers that the advantages claimed by the JV Parties of other VOD service suppliers are largely illusory. However, to the extent that they do exist, they depend on access to attractive content. Accordingly, the control by the Kangaroo JV and the JV Parties over the majority of attractive UK TV VOD content would allow the JV Parties to nullify the claimed advantages of other VOD services by engaging in an input foreclosure strategy.

Existing competition

⁷⁵ Effects Paper, paragraph 5.9.

⁷⁶ Paragraphs 4.43 to 4.47.

⁷⁷ See, Effects Paper, paragraph 5.17 (third bullet).

⁷⁸ Paragraphs 4.16 to 4.24

⁷⁹ Effects Paper, paragraph 5.17 (sixth bullet).

⁸⁰ [**CONFIDENTIAL**].

- 5.14 In relation to the constraint imposed by other VOD service providers, the JV Parties have significantly understated the market share of Kangaroo, and overstated the competitive constraint from other VOD service providers.
- 5.15 It is erroneous to claim that Kangaroo will not have a large market share in relation to retail VOD services.⁸¹ In this connection, the JV Parties have relied on an inappropriately wide market definition in order to dilute the market share of Kangaroo. As set out in Section 3 above and detailed from paragraph 5.20 below, the JV Parties have included many services and competitors which do not actually compete in the retail provision of VOD services (such as DVDs, PRVs, games consoles, music and films).
- 5.16 Virgin Media also notes that the DVD proxy for market shares as adopted by the JV Parties in paragraphs 7.37 to 7.42 of the Effects Paper is fundamentally flawed. The DVD proxy includes content which is outside of the relevant market definition, such as movies and US content. Further, consumers are likely to have different preferences in relation to buying DVDs compared to viewing VOD content. For example, DVDs are significantly more expensive than VOD content and therefore consumers may prefer to purchase DVDs that they feel they will watch numerous times. In contrast, VOD content is either free or relatively inexpensive and therefore consumers may be enticed to taste a wider range of content, including content that they would not buy on DVD. Also, Virgin Media's direct experience demonstrates that linear TV viewing drives VOD viewing.⁸² This suggests that linear viewing is a better proxy for market shares than DVD sales.⁸³
- 5.17 The JV Parties then argue that "*[e]ven if only TV VOD is considered the share of the transactional market will be less than 25 percent – below the level normally considered sufficient to raise competition concerns.*"⁸⁴ In this regard, transactional VOD only comprises a proportion of TV VOD viewing. The JV Parties have, therefore, ignored the large amount of catch-up and archive TV VOD content that the JV Parties will supply on a free basis.
- 5.18 In addition, Kangaroo CEO Mr Highfield recently acknowledged the ability of Kangaroo to use its strong position in linear TV and associated catch-up to drive viewers to transactional content on the Kangaroo service:
- "We envisage that a lot of traffic will come through the door from catch-up television, then we will take them on a journey through the back catalogue and paid content."*⁸⁵
- 5.19 The vast majority of competing VOD service providers, including Virgin Media, will not be able to direct viewers to transactional content in such a seamless manner. Accordingly, Kangaroo will have a very considerable advantage in attracting viewers to its transaction content.
- 5.20 Lastly, the JV Parties have overstated the competitive constraint imposed by the businesses listed in paragraph 5.11 and Annex 2 of the Effects Paper. In this connection, many of the competing VOD service providers identified by the JV Parties in paragraph 5.11 do not actually compete in the market for the provision of retail VOD services, or only compete in a peripheral manner. For example:

⁸¹ Effects Paper, Annex 4, paragraph 1.1 (first bullet).

⁸² This is acknowledged by the JV Parties in the Effects Paper, Annex 4, paragraph 1.1 (seventh bullet): "*VOD is largely a secondary content market and capacity growth is generated by production for film and linear free-to-air television.*"

⁸³ See also Main Submission, paragraph 4.13.

⁸⁴ Effects Paper, Annex 4, paragraph 1.1 (first bullet).

⁸⁵ Paid Content: UK Article.

- (a) Sky: the JV Parties identify Sky as a major competitor on the basis of its Sky+ PVR and Sky Anytime push VOD service.⁸⁶ The JV Parties have significantly overstated the competitive constraint imposed by Sky in relation to true VOD. As noted in Virgin Media's Main Submission, PVRs do not compete in the same market as the provision of true retail VOD services.⁸⁷
- (b) Apple: The Apple iTunes service is focussed on music (which is outside the scope of the relevant market) and has only more recently expanded into other content, in particular movie content (which is also outside of the scope of the relevant market).
- (c) Games consoles: Games consoles in themselves do not provide a VOD service to viewers. Rather games consoles are an apparatus via which viewers can connect information downloaded online directly to television sets. These games consoles rely on VOD content from VOD content suppliers such as the JV Parties in order to make available VOD content to consumers. Accordingly, the JV Parties mischaracterise the extent to which these consoles compete with the JV Parties and Kangaroo in the Effects Paper.⁸⁸
- (d) LOVEFiLM: This is essentially a movie download service. Movie VOD services are in a separate market to TV VOD content services.
- (e) Tesco: As stated by the JV Parties, the Tesco service currently relates to music only⁸⁹, which does not fall within the market for TV VOD content services.
- (f) Etailers and physical retailers: The JV Parties state that these retailers sell DVDs over the internet and can be expected to offer DTO in the future. First, DVDs do not compete in the same market as TV VOD content services. Further, it is expected that a significant proportion of the DTO business would relate to movies, which do not fall within the market for TV VOD content services.
- (g) Orange and O2: these telecommunication companies have only announced VOD plans, and the timetable for launch is very vague.⁹⁰
- (h) Babelgum: The JV Parties have admitted that Babelgum is a movie focussed service, which therefore falls outside of the scope of the relevant market.
- (i) Joost: The JV Parties specifically refer to Joost "*having recently announced the expansion of its relationship with ALL3MEDIA to provide addition [sic] UK content*"⁹¹. Virgin Media seriously doubts the ability of Joost to acquire sufficient UK content from All3MEDIA to compete with the attractive UK content that the Kangaroo JV will be able to supply. **[CONFIDENTIAL]**.⁹² In this connection, Joost has made it very clear to the CC that lack of access to the JV Parties' content severely limits its ability to compete in the UK.⁹³

⁸⁶ Effects Paper, paragraph 5.11(b).

⁸⁷ Main Submission, paragraph 4.45.

⁸⁸ See, for example, Effects Paper, paragraph 5.8.

⁸⁹ Effects Paper, paragraph 5.11(j).

⁹⁰ In this regard, Orange have recently announced that they have delayed their plans to launch any TV service. See, for example: <http://www.broadbandtvnews.com/?p=10439>.

⁹¹ Effects Paper, paragraph 5.11(i).

⁹² **[CONFIDENTIAL]**.

⁹³ See Joost submission to the CC of 25 July 2008 (section 2).

(j) Youtube: Youtube predominantly offers short-form content, which is outside of the scope of the relevant market.⁹⁴

5.21 The limitations on the ability of the above businesses to compete with the JV Parties and Kangaroo in relation to VOD services also apply to the long list of relatively insignificant potential competitors set out in Annex 2 of the Effects Paper.

5.22 In conclusion, in considering the impact on competition on the retailing of VOD content and services, the JV Parties have very considerably overstated the competitive constraint that will be imposed on the Kangaroo JV by a combination of (i) consumer unwillingness to pay for VOD content; (ii) the perceived advantages from which other VOD service platforms benefit; and (iii) the existence of other retail competitors. Moreover, the JV Parties have very materially understated the likely market position of the Kangaroo JV. Accordingly, there is a very real risk that if the proposed Kangaroo JV were to be permitted to proceed, it would give rise to an SLC in the retail supply of TV VOD services.

⁹⁴ Main Submission, paragraphs 4.14 to 4.15.

ANNEX 1

RESPONSE TO MARKET DEFINITION PAPER

1. INTRODUCTION

- 1.1 The JV Parties claim that the Market Definition Paper provides additional evidence related to market definition for both the wholesale and retail VOD markets. The new evidence provided by the JV Parties includes the following: an analysis of consumers' viewing patterns on UK linear TV (referred to as "**BARB analysis**"); an analysis of the DVD market; and a consumer survey on viewer preferences.
- 1.2 Virgin Media considers that the additional memorandum raises no new arguments which the JV Parties have not previously made. Further, the purported new evidence, much of which has been excised from the memorandum, does not appear to provide any cogent new evidence to suggest that the market definitions for the wholesale and retail supply of VOD services are any different to those set out in Virgin Media's Main Submission.

2. MARKET FOR THE RETAIL SUPPLY OF VOD SERVICES

- 2.1 The JV Parties claim in the Market Definition Paper that the additional evidence shows that:
- (a) a significant proportion of consumers are reluctant to pay for VOD content;
 - (b) consumers are willing to substitute between a range of different types of content including US and UK content, TV and films, and short-form and long-form content; and
 - (c) consumers are willing to substitute between a variety of delivery technologies and platforms.
- 2.2 Each of these points is addressed further below.

Consumers are reluctant to pay for VOD content

- 2.3 The JV Parties indicate in their memorandum that *"it is anticipated that over 90 per cent (by usage) of content on UKVOD will be advertising-funded and free to consumers. This is because there is overwhelming evidence that consumers are not willing to pay for VOD content."*¹
- 2.4 Clearly, whilst it is always the case that consumers prefer lower prices to higher prices, the fact that the Kangaroo JV proposes to supply 90 per cent of VOD services free to viewers is purely a choice on the part of the JV Parties as to the appropriate business model in what is a two-sided market. As set out in paragraphs 3.20 to 3.25 of the Main Submission, Virgin Media's VOD service currently involves a mix of different pricing models. For example, Catch-up TV is free to all customers, TV Choice and Music On Demand is available without an additional charge to Virgin Media's top tier subscription customers, although there is an additional supplementary charge to other customers, and More On Demand is a mix of free and PPV content. Given the improvements in technology and the rapid growth in Virgin Media's VOD service since its launch in 2005, it is implausible to suggest that viewers are not willing to pay for VOD content when the available evidence shows that customers are currently paying for VOD services.
- 2.5 While the JV Parties indicate in paragraph 3.7 that *"evidence drawn from two separate consumers surveys supports the view that consumers are unwilling to pay for VOD content"*, they have chosen to excise the results of the survey. Clearly, this limits the

¹ Paragraph 3.5.

extent to which Virgin Media and other third parties are able to comment on the accuracy and reliability of the evidence on which the JV Parties are basing their conclusions.

- 2.6 Further, the Kangaroo JV's choice of advertising-funded business model does not address the fact that advertisers will potentially pay higher prices as a result of the lack of competition between the JV Parties which will arise as a result of the Kangaroo JV. Similarly, if the advertising-funded business model does not work, or the Kangaroo JV decides to adjust its business model to include a mix of subscription and advertising funding (the Kangaroo JV already expects 10 per cent of content to be paid-for by viewers), the lack of competition between the JV Parties means that consumers and advertisers would potentially pay higher prices than they otherwise would absent the JV. The fact that the Kangaroo JV has currently chosen one business model over another does not preclude it from adjusting the business model in future once market power has been obtained.

Consumers are willing to substitute between a range of different types of content

UK and US content

- 2.7 The JV Parties state that "*new evidence presented in this paper demonstrates that Consumers are expected to view both UK and US VOD content (based on BARB and DVD analysis); and "Consumers will substitute between a VOD service with UK and US content".*"²
- 2.8 As set out in paragraphs 4.5 to 4.12 of the Main submission, Virgin Media does not consider UK and US originated content to be close substitutes. Although US content is provided by Virgin Media on its VOD service³, this is because, as a service provider, Virgin Media wishes to offer as full a range of attractive content to its customers as is possible so as to increase the attractiveness of the overall VOD service offering. In other words, Virgin Media considers US-originated content to be complementary to the UK-originated content provided by the JV Parties, and not a close substitute.
- 2.9 In relation to the additional BARB and DVD analysis provided by the JV Parties, as much of the analysis has been excised from the Market Definition Paper, Virgin Media is unable to comment in any detail. However, the JV Parties conclusion from the BARB analysis appears to be at odds to the evidence submitted by Virgin Media. As set out in paragraph 4.9 of the Main Submission, much of the most popular VOD content on Virgin Media's VOD service relates to UK-originated content originally broadcast by the JV Parties on the most widely viewed linear channels. Accordingly, the CC should exercise caution over the additional analysis submitted by the JV Parties as it is not consistent with the viewing data drawn from Virgin Media's VOD service.
- 2.10 In relation to the additional DVD analysis submitted by the JV Parties, Virgin Media disagrees that DVD sales of television content could be used as a proxy for evidence of substitution between UK and US television content. This is for the reasons set out in paragraph 4.13 of the Main Submission.
- 2.11 Although it will certainly be the case that some consumers view both UK and US VOD content, this does not address the relevant question for the purpose of assessing market definition as to whether consumers would switch between UK and US VOD content in response to a 5-10 per cent relative increase in prices. The JV Parties indicate that the

² Paragraph 3.10.

³ There is almost no US-originated content on the catch-up VOD services available on the Virgin Media platform. There is no US originated content available on the BBC's iPlayer or on 4OD (Channel 4's catch-up service). The only material US originated content available on Virgin Media's VOD catch-up service is Star Trek (which is supplied by Virgin 1).

consumer survey which they commissioned demonstrates that consumers would switch between DTR⁴ UK and US TV archive content delivered online. Although it is not possible for Virgin Media to comment directly on the results of the consumer survey which have been excised from the memorandum, it is noteworthy that the JV Parties purported conclusion only relates to DTR archive content and not to catch-up or DTO content.

- 2.12 Further, Virgin Media would encourage the CC to exercise caution over the results of the consumer survey as the JV Parties have indicated that the methodology used included "*conjoint analysis to better understand the preferences that consumers have for different types of content and different modes of delivery*".⁵ Conjoint analyses (and stated preference surveys in general) have a number of very important limitations. In particular, when consumers have to choose between a number of trade-off options, it is easy for respondents to become confused and resort to simplification strategies, which makes the results wholly unreliable. Further, designing conjoint studies can be difficult and the results can be very sensitive to the trade-off options selected and the values attached to the different options.
- 2.13 It is noteworthy that the JV Parties justify their use of conjoint analysis by stating in footnote 10 that "[t]o ask consumers directly about their preferences, for example, for US or UK content, (*"Would you switch to US VOD content if the price of UK VOD content were to increase?"*) would likely result in unreliable consumer responses". However, the JV Parties fail to acknowledge that such stated intentions surveys have the benefit of being simple and easily understandable by respondents, which means that the results will often be more reliable than the results of more complicated survey techniques. In this regard, Virgin Media would observe that the CC has usually commissioned stated intentions surveys (instead of the complex conjoint analysis) in its previous merger investigations in order to obtain robust and reliable information.⁶

Films and television content

- 2.14 The JV Parties indicate that the "*New evidence presented in this paper demonstrates that:*
- *Consumers are expected to view both TV and Film content (based on BARB and DVD market analysis); and*
 - *Consumers will substitute between a VOD service with TV content and a VOD service with Film content"*⁷
- 2.15 As set out in detail in paragraphs 4.16-4.24 of the Main submission, Virgin Media considers that TV VOD content and movie VOD content are generally not substitutable and therefore should not be considered to compete in the same market. The contradiction in the parties' arguments is also clearly evident from the fact that they say on the one hand that viewers are not willing to pay for VOD content, yet on the other hand argue that film content (which is nearly all paid-for VOD content) is a constraint on TV VOD content. As mentioned in paragraph 4.19 of Virgin Media's Main Submission, the fact that movie and TV VOD content are generally made available on a different charging basis shows that customers of VOD movies demonstrate an additional willingness to pay compared to customers of TV VOD content.
- 2.16 As the new evidence provided by the JV Parties has been excised from the Market Definition Paper, it is not possible for Virgin Media to provide any detailed comments on

⁴ Download to rent.

⁵ Paragraph 3.14.

⁶ E.g. Woolworths/Bertram (2007), Greif/Blagden (2007), Stagecoach/Scottish Citylink (2006), Greater Western Passenger Railway Franchise (2006), National Express Group/Thameslink Greater Northern Rail Franchise (2005) etc.

⁷ Paragraph 3.20.

the results. However, analogous points apply to those mentioned above regarding the reliability of the new evidence (i.e. the BARB data is not consistent with the evidence submitted by Virgin Media, the DVD analysis does not provide a reliable proxy of evidence of substitution between film and TV VOD content, and caution should be exercised over the results of the consumer survey). Accordingly, Virgin Media has not been presented with any additional evidence to suggest that it, or the CC, should depart from the views expressed in its previous submission that film and TV VOD content should not be considered within the same market.

Long form content and short form content.

- 2.17 The JV Parties maintain that long form and short form content are substitutable, although the additional evidence referred to in the memorandum to support this proposition has been excised. Nevertheless, Virgin Media does not consider that it is credible that the JV Parties have been able to provide robust economic evidence to show that consumers (or VOD suppliers) would switch between long form and short form VOD content in response to a 5-10 per cent relative increase in price.
- 2.18 As set out in paragraphs 4.14-4.15 of the Main submission, Virgin Media does not consider that short form VOD content is substitutable for traditional long form content (such as TV programmes etc.) either from the customer's perspective or from the perspective of Virgin Media as a VOD service provider. In this regard, Virgin Media agrees with the OFT's conclusion that *"the evidence available does not persuade the OFT that a hypothetical monopolist of long-form VOD content would be constrained by consumer switching to short-form content"*.⁸

c) Consumers are willing to substitute between a variety of delivery technologies and platforms

The interaction between internet VOD and TV-platform VOD.

- 2.19 The JV Parties suggest that *"Closed VOD Platforms (i.e. VOD through a television set) are the most popular means of accessing VOD because consumers can replicate the "lean back" experience of watching linear television"*⁹ and that *"[a] consumer survey conducted in January 2008 by Wiggan Entertainment Media Research indicated that consumers have a strong preference for viewing VOD on TV platforms"*.¹⁰ The JV Parties suggest that *"this clearly gives a strong retail market advantage to closed VOD platforms and games consoles which allow consumers to view content on a TV"*.¹¹
- 2.20 As set out in paragraphs 4.29 to 4.32 of the Main Submission, Virgin Media considers that the TV platform VOD service offered over its cable platform provides a technically superior and richer customer experience than that offered by internet VOD service providers. However, as a consequence of current developments in technology which enable content delivered by broadband to be viewed on a television, there is already a very significant degree of convergence between VOD content delivered via broadband and VOD content viewed over TV. In practice, in the very near future all VOD content, however delivered, would be capable of being viewed on a television set.
- 2.21 Therefore, to the extent that there could ever have been a material distinction drawn between the VOD services made available over a broadband connection and those made available over TV, that distinction has in practice already become meaningless. It is also

⁸ Paragraph 37.

⁹ Paragraph 3.28

¹⁰ Paragraph 3.29

¹¹ Paragraph 5.8 of the Parties Joint Position Paper on the Effects of the Transaction on Competition.

simply not credible for the JV Parties to suggest that TV VOD services have a material advantage over internet VOD services in light of the convergence.

"VOD delivered by Peer-to-peer (P2P) is a constraint on other VOD services"

- 2.22 Virgin Media considers that the JV Parties' claim that "*customers will substitute away from legal online VOD services to Peer-to-peer services*"¹² to be deeply implausible. The sharing of TV VOD content on peer-to-peer websites is most likely to be unlawful, the range of content will be limited and of poor quality, and there is the risk that such content will be withdrawn from the site due to its illegal nature. Accordingly, it is extremely unlikely that a sufficient number of customers will switch from the type and range of VOD content provided by the JV Parties to the unlawful content delivered via peer-to-peer networks in response to a 5-10 per cent increase in price.

"PVRs (personal video recorders) provide consumers with a strong alternative to VOD"

- 2.23 The JV Parties maintain that PVRs provide consumers with a strong alternative to VOD. Virgin Media addressed the points previously made by the JV Parties and set out the reasons why it considered that PVRs and VOD should not be considered to be in the same market in paragraphs 4.43 to 4.47 of the Main Submission.
- 2.24 The additional evidence provided by the JV Parties in its memorandum is inconclusive. For example, the information supplied in Table 1 of the submission simply consists of a comparison of VOD and PVR functionality. In this regard, the OFT's substantive assessment guidelines on mergers states that "*market definition focuses on the empirical question of substitutability from the point of view both customers and competing suppliers. Demand-side substitution examines the extent to which customers could and would switch among substitute products in response to a change in their relative prices.*"¹³ (Emphasis added.) The analysis provided by the JV Parties on the attributes and functionality of PVRs and VOD fails to consider how consumers would react to a relative change in the price of VOD services, which is the relevant question for assessing market definition. Similarly, the BARB analysis which the JV Parties refer to in paragraphs 3.39 to 3.40 of the memorandum (i.e. "*that consumers do use and value the ability to time-shift their viewing*"¹⁴ and that "*PVR users have a very similar profile in terms of content preferences to likely users of UKVOD*"¹⁵) also fails to consider how consumers would respond to a relative change in the price of VOD services.
- 2.25 Accordingly, Virgin Media does not consider that the additional evidence provided by the JV Parties provides any further analysis to suggest that PVRs are a constraint on VOD services.

"DVDs are a substitute for transactional VOD"

- 2.26 The JV Parties maintain that DVDs are a substitute for VOD services. However, the only additional evidence provided by the JV Parties in the memorandum to support this claim appears to be a single example from the consumer survey, which the JV Parties have excised.
- 2.27 Virgin Media set out the reasons why it does not consider DVD rental or retail sales of DVDs to be a substitute in paragraphs 4.48 to 4.51 of the Main Submission. Given the

¹² Paragraph 3.32

¹³ Paragraph 3.13. Mergers - Substantive Assessment Guidance, OFT 516, May 2003.

¹⁴ Paragraph 3.39

¹⁵ Paragraph 3.40

lack of additional evidence provided by the JV Parties, there is no reason for Virgin Media to change its view that DVDs do not compete with VOD services.

The overall impact of substitution to all alternative VOD services

- 2.28 Virgin Media disagrees with the JV Parties overall conclusion that the *"evidence presented in this paper demonstrates that there are a large number of VOD characteristics that will drive consumers' choice and substitution behaviour."*¹⁶ Much of the purported new evidence, most of which has been excised from the memorandum, does not appear to provide any reliable new evidence to suggest that the market definition for the retail supply of VOD services is any different to that set out in the Main Submission.
- 2.29 The JV Parties even acknowledge themselves that the *"evidence presented in this paper does not allow one directly to test the question whether a sufficient number of consumers would be able to switch away from a hypothetical monopolist of UK TV archive content attempting to raise price."*¹⁷ Accordingly, it would take a large leap of faith by the CC to accept the JV Parties suggested approach to market definition when the JV Parties have not provided any cogent information which explores the extent to which consumers would switch between different types of content and different delivery mechanisms in response to a relative change in prices.
- 2.30 Finally, in paragraphs 3.52 of the Market Definition Paper, the JV Parties rather curiously set out reasons why the results of the consumer survey which they commissioned should not be used to estimate price elasticities of demand. This seems to be a rather contradictory statement given that the JV Parties have relied upon the consumer survey as evidence to show that consumers switch between different types of content (particularly between UK and US originated content, and between TV and film content). Clearly, such comments raise significant doubts over the quality and reliability of the survey which the JV Parties commissioned.

3. MARKET FOR THE WHOLESALE SUPPLY OF VOD SERVICES

- 3.1 In relation to the wholesale supply of VOD services, the JV Parties continue to argue that *"the substitutes to UK TV archive content at the wholesale level are largely the same as those at the retail level i.e. the wholesale supply of UK TV archive content is part of a broader market for the wholesale supply of other VOD services which include for example, US television content, film, catch up and VOD delivered through a PVR"*.¹⁸ Accordingly, the JV Parties have not provided any further evidence on the wholesale supply of VOD services in addition to the limited additional evidence referred to above in relation to the retail supply of VOD services.
- 3.2 As set out in the Main Submission, the JV Parties own and broadcast content representing a very high share of viewing in the UK. Moreover the JV Parties account for [CONFIDENTIAL] proportion of VOD TV content viewed on the cable platform. Regardless of the precise scope of the market definition for the wholesale provision of the content in the UK, Virgin Media considers that the JV Parties are each other's closest competitors for a wide range of content supplied on a VOD basis.

¹⁶ Paragraph 3.50

¹⁷ Paragraph 3.51.

¹⁸ Paragraph 4.2.