

**REFERENCE RELATING TO THE ANTICIPATED JOINT VENTURE BETWEEN
BBC WORLDWIDE LIMITED, CHANNEL FOUR TELEVISION CORPORATION
AND ITV PLC**

Summary of provisional findings

1. On 30 June 2008, the Office of Fair Trading (OFT) referred the anticipated joint venture (JV) between the British Broadcasting Corporation (BBC) through BBC Worldwide Limited (BBCW), Channel Four Television Corporation (C4C) and ITV plc (ITV) relating to the video on demand (VOD) sector to the Competition Commission (CC) for investigation and report. The reference was made under section 33(1) of the Enterprise Act 2002 (the Act). Following an extension of the original 24-week inquiry period under section 39(4) of the Act, we are required to publish our final report by 8 February 2009.
2. VOD covers a range of technologies which allow the consumer to select audiovisual content for immediate or subsequent viewing, rather than being restricted to the 'linear' TV schedule put together by the broadcasters. The VOD supply chain starts with programme production or the acquisition of rights to exploit content for VOD purposes. UK broadcasters have three main sources for their audiovisual content: in-house production; commissioning from third party production companies; and the licensing of rights to exploit existing content. Rights owners may provide a VOD service directly to consumers or may wholesale content to retailers, who will deliver VOD to viewers. The viewer can access content over the Internet without subscription (typically referred to as open VOD) or in a variety of ways with a subscription or using dedicated hardware or connections (typically referred to as closed VOD). Closed VOD services can often be viewed on a TV set.

3. VOD services are new and are growing quickly, and business models vary. It is useful to distinguish, in particular, between free-to-air (FTA) advertising funded; subscription funded; and pay-per-view funded models. Content may be watched immediately ('streamed'); downloaded temporarily as a time-limited file (download to rent (DTR)); or downloaded permanently (download to own (DTO)).
4. The BBC is the longest established national TV channel operator in the UK. It is a public corporation operating under its own charter, which was renewed on 1 January 2007. The BBC launched the BBC iPlayer on 25 December 2007 as part of its public service activities. This offers a catch-up service via the Internet for programmes for up to 7 days after transmission (or longer for continuing series).
5. BBCW is a wholly-owned subsidiary of the BBC. Its day-to-day operations are conducted on an arm's length basis from the BBC. BBCW engages in a wide range of commercial activities in the audiovisual sector both in the UK and overseas, mainly involving the commercial exploitation of the BBC's content. It provides the UKTV suite of nine channels in conjunction with Virgin Media. BBCW is also involved in the sale of DVDs through 2 entertain. BBCW does not currently have a retail VOD presence in the UK market but licenses content to a variety of other VOD services.
6. C4C is a statutory corporation which was created by Act of Parliament in 1982. Its particular public service remit is to offer distinctive programming that the market might otherwise not provide. It is funded primarily from TV advertising revenues. C4C was the first of the parties to launch a VOD service. 4OD was launched in late 2006 on cable and broadband, offering a selection of C4C's programming on an on-demand basis via the 4OD application. 4OD has, over time, become predominantly free to viewers. Programmes can be streamed or downloaded on a DTR or DTO basis. Channel4.com offers primarily catch-up for C4C linear programming and

material to complement linear programming. C4C licenses content to a variety of other VOD services.

7. ITV (and its predecessors) has been in operation for more than 50 years. It is the UK's largest commercial FTA broadcaster. ITV.com, ITV's website, allows consumers to access a wide range of ITV material, including 30-day catch-up and some archive material, on a streamed basis over the Internet. It is primarily funded by online advertising and was the first predominantly free streamed video service in the UK. Some ITV content is licensed to other VOD services.
8. On 27 November 2007, the parties signed a Short Form Agreement setting out the key terms of the transaction. They also formed a limited liability partnership (UKVOD LLP) under an interim agreement. On 29 September 2008, the parties submitted to us detailed documentation setting out the updated transaction.
9. Under the terms of the agreements, UKVOD will supply VOD content to any consumer with a PC and to third party VOD retailers in the UK. Each party will hold an equal stake in the limited liability partnership, will be entitled to appoint two directors to the board, and will contribute certain VOD business activities. Subject to specified exemptions, UKVOD will be each party's principal route to market for their archive VOD content. They expect the vast majority of views to be of free, advertising-funded material.
10. Each party will make available a minimum number of hours of content to UKVOD for a minimum period including, for C4C and ITV, both archive and catch-up VOD rights. UKVOD will select content from ITV and C4C. Initial selection of BBC content for UKVOD will be made via BBCW.

11. Of the parties' existing consumer-facing VOD operations, ITV.com and Channel4.com will continue and will, in particular, provide catch-up material, focusing on content that complements their primary broadcasting business. C4C's 4OD service will cease. BBC iPlayer is a public service activity of the BBC operated separately from BBCW's commercial activities and does not form part of the BBC's contribution to the JV.
12. It is envisaged that UKVOD will be able to syndicate the whole, or substantially the whole UKVOD service (or sub-license substantial representative samples of it) to closed VOD services and, after a period of 12 months to allow for the establishment of the UKVOD website, to open VOD services. This ability will be largely exclusive to UKVOD for archive VOD content. ITV and C4C will retain the ability to wholesale rights to catch-up content separately from UKVOD.
13. The parties told us that the purpose of the JV was to create a customer proposition that could compete in the VOD market against powerful competitors who were able to leverage significant existing assets that the broadcasters did not possess. To achieve this, the parties intended to create a 'one-stop-shop' that would provide consumers with the convenience of being able to access both popular content and niche content on a single service, providing the consumer with 'a sophisticated and comprehensive user experience'. The parties said that they were also seeking to maintain control of their content, in order to avoid the 'disintermediation' faced by music companies due to the success of, for example, iTunes. They also told us that the JV would limit individual risk in an uncertain, nascent, VOD sector.
14. The parties said that, as catch-up content would still be available on ITV and C4C's own websites and on BBC iPlayer, the key element of UKVOD's proposition was to promote a wide range of UK archive content. However, archive content could not be

offered in isolation. The parties told us that catch-up content was the driver for viewers consuming archive content.

15. We reached a provisional view that, in the absence of the transaction, each of BBCW, ITV and C4C would pursue its own commercial interests, either alone or in partnership with a third party, to exploit its archive VOD content rights. Such rights would be likely to form part of a retail VOD service, either in a direct-to-consumer offering or through wholesale distribution or both. We did not find it necessary to come to a conclusion as to which route to market was the most likely to be pursued by each party.
16. We provisionally concluded that two or more enterprises would cease to be distinct and that the share of supply test was met, and therefore that a relevant merger situation would be created.
17. We provisionally concluded that the markets for the retail supply of VOD services and the wholesale licensing of content for VOD exploitation should be defined by reference to the supply of VOD content and should include long-form VOD content delivered by both open and closed services. We decided that catch-up and archive content should be treated as part of the same markets. The markets should exclude film VOD, short-form and user-generated content, DVDs and the use of personal video recorders (PVRs), and the supply of linear broadcast TV. We also viewed non-UK content as an imperfect substitute for UK content, particularly for certain genres of programmes and/or if it had not previously been broadcast on linear TV. We provisionally concluded that the geographic market should be no wider than the UK.
18. We looked at levels of competition in the retail supply of VOD services. We reached the provisional view that, absent the JV, the parties were, or would be in the future,

each other's closest competitors for a wide range of content supplied on a VOD basis and that third party VOD retailers offered a weaker competitive constraint. Third party VOD retailers rely on content from one or more of the parties to offer any substantial volume of UK TV VOD content to their customers. We found that the parties had a substantial share of VOD content, particularly of hours of UK TV archive VOD content. Given our finding that non-UK VOD content was, in general, an imperfect substitute for the parties' VOD content, we did not find that VOD retailers offering non-UK content acted as an effective competitive constraint on the parties.

19. We also looked at levels of competition in the wholesale supply of VOD content rights. We examined the syndication deals between the parties as wholesalers and third party VOD retailers as customers. We found that the most quoted source of bargaining strength was the degree of importance attached to the content under negotiation. In addition, the ability to switch, or threaten to switch, between suppliers was an important aspect of bargaining power. We found that, in general, the parties had greater bargaining strength than the VOD retailers to whom they supplied content.
20. Nevertheless, we were told by several third parties that it might be sufficient for them to have access to content from two of the three parties. We saw some evidence of a competitive process in which VOD retailers played one party off against another. Several existing and potential VOD retailers also told us of the importance of being able to offer both catch-up and archive content.
21. We looked at whether, in the absence of UK VOD content from the parties, third party VOD retailers would have access to sufficient UK content to allow them to compete closely with the parties. We found that the ability to acquire VOD rights was often closely associated with holding or acquiring linear TV rights and that the linear

broadcaster of that content was in an advantageous position when negotiating for VOD rights to it. According to our estimates, third party producers were able to offer, in total, only a small fraction of the volume of VOD content available from the parties. We thought it unlikely that third party VOD retailers would be able to acquire sufficient non-UK content to offer an effective competitive constraint to the parties.

22. We therefore provisionally concluded that there were no sources of sufficient scale to provide credible alternatives to the parties' content, making it difficult for wholesale customers to switch, or threaten to switch, away from the parties as suppliers should they be unable to agree satisfactory terms. This indicated to us that, absent the JV, the parties would be in a strong position in the wholesale market.
23. We looked at entry and expansion in the VOD markets. We found that there were a wide range of existing and likely future VOD services being offered in the UK. However, it was clear to us that, in order to compete with UKVOD, any VOD retailer would need to have access to a wide range of both catch-up and archive UK content. We found it unlikely that a VOD retailer would be able to access sufficient UK VOD content to provide a VOD service which competed effectively with the parties.
24. We considered the impact of the JV on competition in the relevant VOD markets. We formed the provisional view that the JV was likely to result in a loss of rivalry in the supply of VOD content at the wholesale level. The parties were each other's closest competitors for a wide range of content supplied on a VOD basis, and other suppliers would not be in a position to offer content which would allow third party VOD retailers to act as an effective competitive constraint to UKVOD.
25. We considered the extent to which UKVOD was likely to have the incentive to enter into syndication deals in the future. We thought it unlikely that UKVOD would have a

strong incentive to enter into future syndication deals, particularly to open VOD services, which might undermine its own retail operation. If UKVOD were to enter into syndication deals, we thought it likely that these would be on terms that would make it difficult for a third party VOD retailer to offer an effective competitive constraint to the UKVOD service. We also considered whether ITV and C4C would have an incentive to syndicate catch-up content to third party VOD retailers to which UKVOD would not choose to syndicate. We thought it more likely that, if they did enter into syndication deals with third parties, these would be on terms that would be less favourable than would otherwise have been the case.

26. We identified two ways in which a loss of rivalry at the wholesale level might affect viewers. First, third party VOD retailers purchasing VOD content from the parties might pass on a price increase, or other adverse change in terms, to consumers. Second, the parties may find it in their interest to engage in strategies that would limit the ability of any rival service to undermine the JV, by, for example, attempting, partially or completely, to foreclose access to content or otherwise increasing the cost of this content to their rivals, or by limiting the manner in which the content could be exploited. We thought it possible that, at some point in the future, they would choose to do so.

27. We formed the provisional view that the JV was also likely to result in a loss of rivalry at the retail level. The parties were, or would be in the future, each other's closest competitors for a wide range of content supplied on a VOD basis and third party VOD retailers would not act as an effective competitive constraint. This loss of rivalry between them would enable the parties to offer less attractive terms to customers, resulting in viewers paying higher prices for some content, paying for a higher proportion of content, and/or receiving lower quality or less innovative offers. The loss of rivalry and the concentration of content in one entity could also reduce the

opportunities for future initiatives or developments by third parties of alternatives to the JV.

28. We provisionally concluded that the JV would be likely to lead to a loss of rivalry between the parties, amounting to a substantial lessening of competition (SLC) in the supply of UK TV VOD content at the wholesale and retail levels. We also provisionally concluded that the JV would be unlikely to result in an SLC in the online UK advertising market or in the market for content acquisition in the UK.

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