ACQUISITION BY BRITISH SKY BROADCASTING GROUP PLC OF 17.9 PER CENT OF THE SHARES IN ITV PLC

Report sent to Secretary of State (BERR) 14 December 2007
The Department for Business, Enterprise and Regulatory Reform (BERR) has excluded from this published version of the report information which it considers should be excluded having regard to the three considerations set out in section 244 of the Enterprise Act 2002 (specified information: considerations relevant to disclosure). The omissions are indicated by ☐.

The versions of this report published on the BERR website on 20 December 2007, and reproduced on the CC website, gave the name of the company acquiring the 17.9 per cent stake in ITV plc as British Sky Broadcasting plc. The correct, full title of the acquiring company is British Sky Broadcasting Group plc. This corrected version of the report, with the full company name given on the title pages, paragraph 1 of the summary and in footnote 160, was posted on the BERR and CC websites on 11 January 2008.
# Acquisition by British Sky Broadcasting Group plc of 17.9 per cent of the shares in ITV plc

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Glossary
Summary

1. On 24 May 2007 the Secretary of State for Trade and Industry, now the Secretary of State for Business, Enterprise and Regulatory Reform, referred the acquisition by British Sky Broadcasting Group plc (BSkyB) of 17.9 per cent of the shares in ITV plc (ITV) to the Competition Commission (CC) for investigation and report. The reference was made under section 45(2) of the Enterprise Act 2002 (the Act). This followed the Secretary of State’s intervention notice dated 26 February 2007 and the reports of the Office of Fair Trading (OFT) and the Office of Communications (Ofcom) to the Secretary of State of 27 April 2007 under sections 44 and 44A of the Act respectively. Following an extension to our timetable, we are required to report to the Secretary of State by 2 January 2008. This was the first reference to be made under Chapter 2 of Part 3 of the Act (Public Interest Cases).

2. The media sector includes film, radio and television production and broadcasting; aspects of telecommunications; advertising; publishing (including newspapers); and the retailing of audio-visual appliances and DVDs. We focused primarily on television, although we recognized the importance of the broader media sector, particularly in our discussion of plurality issues.

3. The industry is characterized by significant and rapid changes in technology and consumer demand. For many years, viewers received three terrestrial channels: BBC1, BBC2 and ITV. Channel Four Television Corporation (Channel 4) was launched in 1982 and Channel 5 Broadcasting Limited (Five) in 1997. Multi-channel television using satellite or cable technologies was introduced in the early 1980s, offering many more television channels to viewers. Digital technology started to be introduced in the late 1990s. The digital terrestrial television (DTT) free-to-air (FTA) platform was relaunched under the ‘Freeview’ brand in October 2002 and has since grown very rapidly. By the end of June 2007, there were 9.1 million DTT-only homes, around 8.1 million satellite subscription homes, and 3.4 million cable subscription homes. The analogue service is being phased out region by region across the UK between 2008 and 2012.

4. There are two basic business models available to television broadcasters: FTA and pay-TV. The major analogue FTA television services are BBC1, BBC2, ITV1, Channel 4 and Five. DTT is available through a set-top box and carries around 40 FTA channels. Around 200 channels are available FTA to owners of BSkyB satellite dishes through the ‘Freesat from Sky’ service. The British Broadcasting Corporation (BBC), together with some commercial broadcasters including ITV, has also announced that it intends to launch a ‘Freesat’ service. Commercial broadcasters of FTA services rely primarily on advertising and sponsorship for their funding.

5. Pay-TV retailers include BSkyB, Virgin Media Inc (Virgin Media) and the newer entrants such as BT Vision, Tiscali SpA (Tiscali) and Top Up TV Ltd (Top Up TV). Pay-TV retailers typically offer alternative packages of ‘basic’ channels, with ‘premium’ channels (such as sports or movie channels) offered singly or in small packages, usually as an optional extra. Pay-TV is available on DTT, digital satellite (DSat), cable, and the newer platforms (broadband and mobile). Pay-TV retailers rely primarily on subscription fees for their funding; subscribers pay monthly fees to view encrypted channels.

6. BSkyB is a leading broadcaster of sports, movies, entertainment and news. It was formed in 1990 from the merger of Sky Television plc and British Satellite
Broadcasting Limited. BSkyB’s largest shareholder is News UK Nominees Ltd (ultimately owned by News Corporation) which owns 39.1 per cent of BSkyB.

7. BSkyB acquires programming to broadcast on its own channels and supplies channels on a wholesale basis to other broadcasters. It also retails channels (both its own and those of third parties) to subscribers. BSkyB currently makes three of its channels available FTA via the UK DTT platform as part of the branded Freeview offering and has a 20 per cent stake in DTV Services Limited (DTVSL). BSkyB also produces a limited amount of its own content. Around three-quarters of BSkyB’s revenue is derived from subscriptions. Advertising makes up a small proportion of its revenues.

8. ITV (and its predecessors) has been the UK’s largest commercial broadcaster for more than 50 years. ITV was created from the merger of Carlton Communications plc (Carlton) and Granada plc (Granada) in February 2004 and is quoted on the London Stock Exchange. It is a producer of content through ITV Productions and a broadcaster of FTA content. It also has a 40 per cent stake in Independent Television News Limited (ITN) and a 20 per cent stake in DTVSL. Around three-quarters of its revenue is derived from advertising.

9. On 17 November 2006 BSkyB announced that it had bought 696 million shares in ITV, amounting to 17.9 per cent of ITV’s issued share capital. BSkyB paid 135p per share, a total of £940 million, for its stake. We formed the view that BSkyB, through its acquisition of a stake in ITV, was looking to preserve its options as regards the future of ITV. We thought it unlikely that BSkyB would have chosen to invest in ITV purely as an investment vehicle.

10. We looked at whether BSkyB had acquired the ability materially to influence the policy of ITV. We took the policy of a company in this context to mean the management of its business, in particular in relation to its competitive conduct, including the strategic direction of a company and its ability to define and achieve its objectives. In assessing whether BSkyB had acquired material influence as a result of the acquisition, we did not take into account the possibility of a BSkyB director being appointed to the ITV board, nor of BSkyB increasing its shareholding subject to remaining within the 20 per cent limit imposed by the provisions of the Communications Act 2003 (CA 2003).

11. We found that the size of BSkyB’s holding both in absolute and relative terms was such that on the basis of past voting patterns it would be able to block special resolutions proposed by ITV’s management. BSkyB’s ability to block a special resolution would limit ITV’s strategic options, for example its ability to raise funds. BSkyB’s importance and stature as an industry player, together with its position as the largest shareholder, would give additional weight to its views, increasing its ability to influence other ITV shareholders.

12. We concluded that BSkyB had acquired the ability materially to influence the policy of ITV which gives rise to common control for the purposes of section 26 of the Act. The turnover test under section 23(1) of the Act was satisfied. We concluded that a relevant merger situation had been created.

Assessment of competitive effects

13. We concluded that, had the acquisition not occurred, we would expect ITV to remain independent. We therefore assessed the competitive effects of the acquisition against an independent ITV.
14. We concluded that the appropriate framework for analysing any loss of competition arising from the acquisition was a UK market for all-TV which included both pay-TV and FTA services. The all-TV market is highly differentiated and dynamic and we conducted our analysis of the impact of the acquisition by assessing not only the impact on the market as a whole under current competitive conditions, but also possible future competition in pay-TV.

15. We looked at the strength of the existing and future constraints on BSkyB in the market for all-TV, assessing the constraint from other pay-TV operators and from the FTA offer in the absence of the acquisition. We found that within pay-TV, services provided over cable and DSat platforms were close competitors. Although services provided over the IPTV platform offered a certain level of competitive constraint within an all-TV market, it was not clear to us that these players would be able to acquire significant market share within the foreseeable future.

16. We found that FTA services posed a constraint to BSkyB’s prices and that the BBC and ITV were both key to the strength of the FTA offer. Channel 4 and Five also made a significant contribution. BSkyB’s business model relied on the ability to persuade consumers to pay for the content available in its packages, rather than opt for freely-available services. We concluded that, given the competitive constraint of the FTA offer on BSkyB’s services, and the importance of ITV within the FTA offer, BSkyB would have the incentive to influence ITV’s strategy in such a way as to minimize the constraint it offered to BSkyB. We did not find that entry or expansion would be likely to constrain the parties and hence mitigate BSkyB’s incentive to influence ITV’s strategy.

17. We looked at the impact of the acquisition on current competition. ITV’s strategy update, published on 12 September 2007, focused on a three- to five-year plan for content-led growth funded through gains in efficiency and the disposal of remaining non-core assets. Nevertheless, given the dynamic environment in which ITV operates, we found it likely that the board would need to make major investments requiring external funding over the next two to three years. A non-pre-emptive rights issue would be the only feasible or efficient funding mechanism for some investments. BSkyB’s ability to block a special resolution would limit ITV’s ability to raise funds, ruling out some strategic options and affecting its ability to compete in the market for all-TV.

18. We thought it likely that BSkyB would exercise its ability to influence ITV’s strategy so as substantially to lessen competition. We identified several examples of the ways in which, in practice, this might occur:

   (a) BSkyB could seek to influence ITV’s strategy in relation to content production and commissioning. Given its interests as a competitor and despite its interests as a shareholder, we believed that BSkyB would have the incentive to reduce ITV’s investment in content in order to reduce the competitive constraint of FTA on BSkyB. Further, ITV could seek to acquire rights to existing content (such as sports rights) in order to improve the quality of its offer. If ITV sought to raise additional finance to support such an acquisition, either alone or as part of a joint bid, BSkyB would have an incentive to seek to disrupt this.

   (b) BSkyB could seek to influence investment by ITV in high-definition television (HDTV) or in other services requiring additional spectrum. Ofcom’s current proposals to upgrade the DTT platform over the next few years to allow up to four HDTV channels for Public Service Broadcasters (PSBs) did not, in our view, rule
out ITV’s participation in any auction. BSkyB would have an incentive to seek to use its expertise and experience to influence ITV’s other shareholders in relation to any attempt by ITV to raise funds to participate in any auction for additional spectrum.

(c) BSkyB could attempt to influence the course of any future transactions involving ITV to weaken the constraint that FTA services would otherwise provide. It might, for example, disrupt an acquisition of ITV that might otherwise strengthen ITV’s competitive position, or encourage the acquisition of ITV by another buyer who might act in BSkyB’s interests.

19. We concluded that, as a result of the acquisition, there was likely to be a substantial lessening of competition (SLC) arising from a loss of rivalry between ITV and BSkyB in the all-TV market. This may be expected to result in a reduction in the quality of the offer, a reduction in innovation, or an increase in the price of audiovisual services in the all-TV market, compared with the levels that there would otherwise have been absent the acquisition.

20. We looked at the possible impact of the acquisition on future competition. We did not expect ITV to develop a pay-TV offer, or strengthen a competitor’s existing offer. We concluded that there was unlikely to be an SLC arising from a loss of potential rivalry from a pay-TV offer developed or strengthened by ITV.

Advertising

21. We concluded that the effects of the acquisition could be assessed within a UK market for television advertising.

22. Third parties raised a number of concerns in this market. However, the Contracts Rights Renewal remedy (CRR) currently prevents ITV from raising prices for sales of advertising on ITV1, and we saw no evidence to suggest that the parties would be able to raise prices for advertising on their other channels. We also found that the nature of the influence obtained by BSkyB as a result of the acquisition would be unlikely to facilitate the types of anti-competitive behaviour described by third parties.

23. We concluded that the acquisition was unlikely to result in an SLC arising from a loss of rivalry between ITV and BSkyB in the UK market for television advertising.

National television news programme supply

24. We concluded that the effects of the acquisition could be assessed within a UK market for the wholesale provision of television news.

25. We looked at the impact of the acquisition on the wholesale supply of news programming resulting from the indirect link between BSkyB and ITN (in which ITV has a 40 per cent stake). Channel 4 was the most concerned about its future news provision, in part because of its high-quality specification for its news services.

26. We considered the potential mechanisms through which competition could be reduced between Sky News and ITN. We thought it unlikely that the ownership link between BSkyB and ITV would lead Sky News to compete less aggressively with ITN or to influence ITV to weaken ITN given, in particular, the size of BSkyB’s stake in ITV, the non-strategic nature of wholesale news provision and the fact that no relevant contracts will come up for renewal before 2010. Nor did we expect the acquisition to increase the likelihood of coordination between ITN and Sky News.
27. We concluded that the acquisition was unlikely to result in an SLC arising from a loss of rivalry in the wholesale provision of national television news.

Conclusions on the SLC test

28. We therefore concluded that BSkyB’s acquisition of a 17.9 per cent stake in ITV was likely to result in an SLC arising from a loss of rivalry between ITV and BSkyB in the all-TV market.

Plurality

29. We considered the issues raised by the admissible public interest consideration specified by the Secretary of State in the intervention notice dated 26 February 2007 and incorporated in our terms of reference, namely ‘the need, in relation to every different audience in the United Kingdom or in a particular area or locality of the United Kingdom, for there to be a sufficient plurality of persons with control of the media enterprises serving that audience’. This public interest consideration is set out in section 58(2C)(a) of the Act.

30. We took the concept of plurality of persons with control of media enterprises to refer both to the range and number of persons with control of media enterprises. We concluded that a plurality of control within the media is a matter of public interest because it may affect the range of information and views provided to different audiences. We thought it important to draw a distinction between the plurality of persons with control of media enterprises and the implications of that plurality for the range of information and views made available to audiences. We also thought that it was appropriate to distinguish between the range of information and views that are provided across separate independent media groups (external plurality) and the range that are provided within individual media groups (internal plurality).

31. We note that the regulation of media enterprises in relation to plurality and impartiality are distinct. Impartiality relates to the fair and balanced treatment of differing viewpoints in relation to particular news stories but does not address the relative prominence given to each story. We concluded that it was a matter of public interest that decisions about the relative importance of different news stories should be made by a range of independent people and reflect diverse perspectives.

32. We looked qualitatively at sufficiency, and the change in plurality that arose as a result of the acquisition, in relation to both internal and external plurality.

33. We considered how to define relevant audiences. We focused on national news and referred to the range of information and views communicated to audiences through the news as the ‘plurality of news’.

34. We found that the regulatory framework, while relevant to the plurality of news and, hence, the statutory public interest assessment, did not on its own ensure a sufficiency of plurality of news.

35. We looked at the existing levels of plurality for national television and cross-media news audiences absent the acquisition. We noted the following indicators of plurality of news:

(a) The five main channel providers (BBC, ITV, BSkyB, Channel 4 and Five) account for at least 97.5 per cent of total television news viewing. The BBC is by some margin the most widely viewed channel provider for news, followed by ITV.
(b) Television news programme supply is more concentrated still. There are three main providers of news programming, BBC, ITN and Sky News, providing news programming to all of the five main channel providers.

(c) Looking across media, television is most likely to be regarded by people as their main source of news, with newspapers and radio considered to be the next most important sources. While the Internet is growing rapidly, people still largely rely on traditional sources of news and traditional news providers.

(d) Content analysis of television news reveals less diversity than a simple tally of news providers might suggest.

36. We noted that ITV was a significant channel provider for television news and that BSkyB, whilst smaller, was still significant. ITV was the most widely-viewed alternative to the BBC, with BSkyB one of three smaller players in news provision (together with Channel 4 and Five). The parties' links to related companies—in particular ITV's links to ITN and BSkyB's links to News International and News Corporation—further increased the potential significance of their contribution to the plurality of news. In television news, existing regulatory mechanisms reduced the scope for influence over editorial decisions by owners of television channels which broadcast news. There were fewer regulatory restrictions on newspapers.

37. We looked at how the acquisition might affect the plurality of news in terms of direct editorial influence or commercial influence. We noted that both BSkyB and ITV said that the editorial content of ITV news would be unlikely to be a matter of strategic importance. We found that there was a strong commitment to editorial independence across television news broadcasting which would lead to editors resisting any intervention from the board or from shareholders to set the news agenda. We also noted that there were a number of internal and regulatory constraints in the production of television news which were likely to limit any possible single minority shareholder influence on editorial decisions.

38. We concluded that there was insufficient evidence to suggest that the acquisition of a stake of this nature would give BSkyB or its parent companies the ability or incentive to exert editorial influence over ITV's news output.

39. We thought it likely that ITV was able to exert commercial influence over ITN. We noted that ITN would provide ITV with news programming until 2012. ITV’s commercial influence over ITN could, in principle, extend beyond ITV’s news output. In particular, if ITN were unable to function as an effective independent supplier of news content in competition to Sky News, this could reduce the ability of other channels, such as Channel 4, to provide an independent news voice.

40. However, while we thought it likely that BSkyB would have an incentive to favour Sky News over ITN, it was not clear to us that the acquisition would significantly alter BSkyB’s ability to influence ITV to do so. We therefore concluded that the acquisition of a 17.9 per cent stake in ITV did not give BSkyB the ability to exert significant commercial influence over ITV’s news output or more widely over ITN.

Conclusions on plurality

41. Given the extent of the influence conferred on BSkyB by its acquisition of a 17.9 per cent shareholding in ITV, we concluded that the regulatory mechanisms, combined with a strong culture of editorial independence within television news production, were likely to be effective in preventing any prejudice to the independence of ITV news. We did not therefore expect BSkyB’s ability materially to influence ITV to have
an adverse effect on the plurality of news relative to the position absent the acquisition. We therefore concluded that the acquisition would not materially affect the sufficiency of plurality of persons with control of media enterprises servicing audiences for news.

42. We concluded that the acquisition may not be expected to operate against the public interest, having regard only to the relevant public interest consideration.

Conclusions on public interest

43. We concluded that BSkyB’s acquisition of a 17.9 per cent stake in ITV may not be expected to operate against the public interest having regard to the media public interest consideration. However, we also concluded that it was likely to result in an SLC based on our assessment of the competitive effects of the acquisition. In these circumstances, we concluded that, overall, the acquisition may be expected to operate against the public interest.

Remedies

44. In the Notice of possible remedies (the Notice) we invited views on three remedy options:

(a) divestiture of the whole of BSkyB’s shareholding in ITV;

(b) divestiture of such part of BSkyB’s shareholding in ITV that it would cease to have material influence over ITV; and

(c) behavioural remedies to accompany partial divestiture remedies.

45. BSkyB proposed two further possible remedies:

(a) placing the entirety of BSkyB’s voting rights in ITV in a voting trust; and

(b) an undertaking by BSkyB not to exercise the entirety of its voting rights in ITV.

46. We found that the full divestiture of BSkyB’s shareholding in ITV would be effective in remedying the SLC and the consequent adverse effects on the public interest as it would restore the situation prior to the acquisition.

47. We concluded that a divestment of shares to below 7.5 per cent would be effective in remedying the SLC and the consequent adverse effects on the public interest. We recognized that this assessment was not solely a matter of calculation or quantitative analysis, but was in part a matter of judgement. However, we were confident that, below this level, there would be no realistic prospect that BSkyB would be able to exercise material influence in the ways that we had identified. ITV would therefore be able to design and implement its strategy unfettered by a competitor. For the avoidance of doubt, we thought it appropriate that, in addition to a partial divestiture remedy, BSkyB should give undertakings that it would neither seek nor accept Board representation.

48. We had significant concerns regarding the likely effectiveness of the voting trust mechanism as put forward by BSkyB when compared with a divestiture remedy. In particular we were not satisfied that effective mechanisms could be put in place to provide the necessary oversight and enforcement of the remedy. We therefore concluded that BSkyB’s proposal to cede all its voting rights to a voting trust would
not address effectively the SLC and the consequent adverse effects on the public interest. We also concluded that BSkyB’s proposal not to exercise the entirety of its voting rights would not address effectively the SLC and the consequent adverse effects on the public interest.

49. We therefore concluded that two remedy options would be effective in addressing the SLC and the consequent adverse effects on the public interest expected following the acquisition by BSkyB of a 17.9 per cent shareholding in ITV:

(a) divestiture of the whole of BSkyB’s shareholding in ITV; and

(b) divestiture by BSkyB of such part of its shareholding that it would hold less than 7.5 per cent of ITV’s issued ordinary shares, combined with an undertaking not to seek or accept ITV Board representation.

50. We found that, of the two effective remedies that we had identified, partial divestiture was the least intrusive, as it required BSkyB to divest a smaller proportion of its shareholding in ITV. We therefore thought it the more proportionate. We saw no reason to modify our remedy in the light of any relevant customer benefits.

51. We were satisfied that partial divestiture to a level below 7.5 per cent was in practical terms likely to be as effective a remedy as full divestiture, because it removed any realistic prospect that BSkyB would be able materially to influence ITV’s strategy. It was more proportionate than full divestiture because it was less intrusive. We were therefore satisfied that partial divestiture by BSkyB of its shareholding in ITV down to a level below 7.5 per cent was as comprehensive a solution as was reasonable and practicable to the SLC and any adverse effects resulting from it. We recommended that the Secretary of State should take action to implement this remedy. We also recommended that the Secretary of State sought undertakings from BSkyB that it would not seek or accept representation on ITV’s Board.

52. We recommended that the divestiture should take place within [ ] of undertakings being agreed, accompanied by undertakings from BSkyB to the Secretary of State that it would not vote the part of its stake in ITV to be divested during the divestiture period. If a longer period were allowed, we would recommend that a divestiture trustee be put in place and that the Secretary of State approve the trustee and its mandate. In either event, undertakings should be sought from BSkyB not to sell the shares to an associated person.
Findings

1. The reference

1.1 On 24 May 2007 the Secretary of State for Trade and Industry, now the Secretary of State for Business, Enterprise and Regulatory Reform, referred the acquisition by BSkyB of 17.9 per cent of the shares in ITV to the CC for investigation and report. The reference was made under section 45(2) of the Act. This followed the Secretary of State’s intervention notice dated 26 February 2007 and the reports of the OFT and Ofcom to the Secretary of State of 27 April 2007 under sections 44 and 44A of the Act respectively.¹ Our terms of reference are set out in Appendix A. Following an extension to our timetable, we are required to report to the Secretary of State by 2 January 2008.

1.2 In accordance with our terms of reference, if we find that a relevant merger situation has been created, we must decide whether it may be expected to result in an SLC, and whether, taking account only of any SLC and the media public interest consideration concerned, the creation of the relevant merger situation operates, or may be expected to operate, against the public interest. The media public interest consideration specified by the Secretary of State in the intervention notice was the need, in relation to every different audience, for there to be a sufficiency of plurality of persons with control of the media enterprises serving that audience.

1.3 This is the first reference to be made under Chapter 2 of Part 3 of the Act, which provides for a public interest regime under which mergers which appear to give rise to specified public interest considerations can be examined. In public interest cases it is the Secretary of State who has discretion to make a reference to the CC; the questions which the CC is required to answer include a consideration of the public interest having regard to any specified public interest consideration; and the CC delivers its report to the Secretary of State, who has discretion to decide on remedial action. Our findings as to whether a relevant merger situation has been created and, if so, whether it may be expected to give rise to an SLC, must be accepted by the Secretary of State but he is the ultimate decision-maker both on the public interest and on any remedial action. The Secretary of State must make and publish his decision within 30 days of receiving the CC’s report and must also publish the CC’s report.

1.4 The Secretary of State may decide to make no finding at all on the reference if he decides that there is no public interest consideration which is relevant to a consideration of the relevant merger situation concerned. Should the Secretary of State make no finding at all, the CC will proceed as though the reference had been made under section 22 of the Act instead of section 45.

1.5 This document, together with its appendices, constitutes our final report. We are required to deliver our final report to the Secretary of State under section 50 of the Act. Further information, including non-sensitive versions of written submissions, summaries of third-party arguments and views and our provisional findings published on 4 October 2007, can be found on our website.² We refer to these documents as appropriate.

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¹ Ofcom has reporting and related investigatory duties where an intervention notice has been served. These ensure that the Secretary of State receives Ofcom’s advice on any media public interest consideration mentioned in the intervention notice as well as Ofcom’s summary of the relevant representations that it received in relation to such media public interest consideration.

² [www.competition-commission.org.uk](http://www.competition-commission.org.uk)
2. Industry background and the companies

2.1 In this section we outline the major features of the industry; the relevant provisions of the regulatory regime; the television supply chain and the provision of television news; and the companies that are the subject of this inquiry. This provides the context for our subsequent assessment of the competitive effects and plurality issues associated with the acquisition.

Industry overview

2.2 The media sector is very broad and includes film, radio and television production and broadcasting; aspects of telecommunications (including the transmission of programmes via cable, broadcasting, satellite and the Internet); advertising; publishing (including newspapers in print and online); and the retailing of audio-visual appliances and DVDs. We focus primarily on the television supply chain, although we recognize the importance of the broader media sector, particularly in our discussion of plurality issues (see Section 5).

2.3 The industry is characterized by significant and rapid changes in technology and consumer demand. For many years, viewers received three terrestrial channels: BBC1, BBC2 and ITV (now ITV1). Channel 4 was launched in 1982 and Five in 1997. Multi-channel television using satellite or cable technologies was introduced in the early 1980s, offering many more television channels to viewers.

2.4 Traditionally television was broadcast using an analogue signal. However, digital technology started to be introduced in the late 1990s, using spectrum capacity more efficiently (and hence leaving spectrum capacity spare for alternative uses) and facilitating better picture quality. BSkyB introduced a digital satellite service in October 1998, DTT services (including ONdigital’s pay services) were launched in November 1998 and the first digital cable services were launched in 1999. Following the failure of ONdigital’s DTT service, the DTT free-to-view platform was relaunched under the ‘Freeview’ brand in October 2002. DTT take up has grown very rapidly since the launch of Freeview. By the end of June 2007, there were 9.1 million DTT-only homes, around 8.1 million satellite subscription homes, and 3.4 million cable subscription homes. The analogue service is being phased out region by region across the UK between 2008 and 2012.

2.5 It is estimated that around 5 million households have still to convert to digital before switch-off in 2012. There are also a large number of analogue television sets in households where the main television set is already digital. Digitization is facilitating the convergence of the television, telecommunications and Internet sectors, and leading to the development of a range of new services and delivery platforms including, for example, mobile television and HDTV.

2.6 On 13 December 2007, Ofcom announced that it would take a market-led approach to the allocation of the spectrum capacity released after analogue television signals are switched off. It would auction most of the digital dividend in 2009, offering

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4 The analogue television signal was switched to digital in Whitehaven/Copeland in autumn 2007, partly in order to test the logistics of the wider digital switchover scheme.
5 There are estimated to be 19.5 million households with at least one television set requiring conversion to digital before analogue switch-off. Source: Continental Research, Digital TV Report, Autumn 2006.
6 On 19 December 2006, Ofcom published its Digital Dividend Review for public consultation, setting out proposals for the most effective use of this spectrum. It announced its conclusions on 13 December 2007. In addition, on 21 November 2007 Ofcom announced its proposals for an upgrade of DTT that would create the capacity for up to four HD channels on Freeview without using additional spectrum. The consultation document asks PSBs to set out how they would use the upgraded capacity. The
licences that allow users to decide the technology and service, and that can be traded after use. It said that this would create the maximum flexibility for different services and would allow the use of the spectrum to change over time. This may have important implications for the future television landscape, depending on the balance between use of new capacity for television and non-television services (such as wireless broadband and mobile telephony).

Regulatory regime

2.7 We looked at the role of the industry regulator, Ofcom; the regulatory requirements applicable to PSBs; and the main regulatory requirements in six key areas: ownership and control; programme content; commissioning content; advertising; multiplexing and electronic programme guides. Further background relating to the regulatory regime is set out in Appendix B.

Ofcom

2.8 CA 2003 established Ofcom as the independent regulator and competition authority for the UK communications industries with responsibilities across television, radio, telecommunications and wireless. Ofcom's principal duty in carrying out its functions is to further the interests of citizens in relation to communications matters and to further the interests of consumers where appropriate by promoting competition. Section 3 of CA 2003 divides Ofcom's duties into six areas: regulating (through codes and licence provisions) the optimal use of the spectrum; the availability of a wide range of electronic communications services; a wide range of television and radio services of high quality and wide appeal; plurality in the provision of broadcasting; adequate protection for audiences against offensive or harmful material; and adequate protection for audiences against unfairness or the unwarranted infringement of privacy.

2.9 Licensees are obliged to comply with codes established by Ofcom via their licence conditions. There are codes on television access services, broadcasting, cross-promotion, sports and other listed events, EPGs and rules on the amount and distribution of advertising. If a licensee is found to be in breach of a condition of its licence, Ofcom may, among other sanctions available to it, issue a direction requiring compliance with the relevant licence condition and may impose a fine. Ofcom also has the power to revoke the licence where the broadcaster is in breach of its licence if no other remedies are considered appropriate and it is necessary in the public interest to do so.

Public service broadcasters

2.10 The BBC is established by a Royal Charter and funded by a licence fee. The current Charter, which came into force on 1 January 2007, runs until the end of 2016. Under the terms of the Charter the BBC is governed by the BBC Trust, which sets the strategic direction of the BBC and has a clear duty to represent the interests of the licence fee payers. The Trust sets policies and priorities; issues service licences; and holds the Executive Board (which has the operational responsibility for the BBC)

consultation closes at the end of January 2008. Ofcom aims to have new services available on the DTT platform by late 2009/early 2010.

The BBC Trust must set Purpose Remits for each of the BBC's Public Purposes. These define the Trust's priorities for the Executive Board and explain how it will judge the Executive's performance against them. The six Public Purposes include, for example, sustaining citizenship and civil society, promoting education and learning and stimulating creativity and cultural excellence.
to account. An Agreement between the BBC and the Secretary of State for Culture, Media and Sport, which accompanies the Charter, recognizes the BBC’s editorial independence and sets out its public service remit in detail.\(^8\)

2.11 Channel 3, 4 and 5 licensees also have public service remits arising from the conditions attached to their licences as PSBs (see Appendix B for further details). Channel 3 licensees (ITV holds 11 of the 15 licences) and Five (the Channel 5 licensee) must provide ‘a range of high quality and diverse programming’. In addition, some changes in programme policy require Ofcom’s consent. Channel 4 has a similar remit to provide ‘a broad range of high quality and diverse programming’ which, in particular, demonstrates innovation, appeals to the tastes of a culturally diverse society, has educative value and exhibits a distinctive character. Section 295 CA 2003 also requires Channel 4 not to be involved, except to such extent as Ofcom may allow, in the making of programmes to be broadcast on Channel 4.

**Ownership and control**

2.12 Section 350 and Schedule 14 CA 2003 relax certain former restrictions on licence holding and establish new rules relating to the ownership of cross-media services. Schedule 14 CA 2003 places restrictions on participation in companies holding Channel 3 licences (such as ITV). No person may hold more than a 20 per cent share in such a company if they are the owner of national newspapers with more than a 20 per cent share of the total national market. CA 2003 removed this restriction in relation to Five. Section 351 CA 2003 requires Ofcom to carry out a review of the effects or likely effects on a Channel 3 licensee’s programming if there has been a ‘relevant change of control’.\(^9\) Section 281 CA 2003 provides that a person cannot become the appointed news provider for a Channel 3 licensee if the ownership restrictions in CA 2003 would have been contravened if that person had held a Channel 3 licence.

**Programme content**

2.13 The Broadcasting Act 1996 as amended and section 319 CA 2003 require Ofcom to draw up a code for television and radio, covering standards in programmes, sponsorship, fairness and privacy (the Broadcasting Code). Broadcasters are required by the terms of their Ofcom licence to observe the Broadcasting Code. It imposes requirements in relation to the accuracy and due impartial presentation of news, editorializing in relation to matters of political and industrial controversy and balance in terms of presentation. It also gives effect to a number of the requirements of the Television Without Frontiers Directive (TVWF Directive) and was drafted in the light of the Human Rights Act 1998. The Broadcasting Code applies to services licensed by Ofcom, services funded by the licence fee and provided by the BBC and to Sianel Pedwar Cymru (S4C).

2.14 Sections 299 to 302 CA 2003 regulate the broadcasting of sporting and other events of national interest (listed events). These provisions ensure that no UK broadcaster can obtain the rights to broadcast live and on an exclusive basis certain sporting or other events of national interest designated by the Secretary of State, without first

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8 Articles 43 to 63 of the Agreement deal with matters such as content standards, accuracy and impartiality, the Fairness Code, quotas for independent productions and international obligations.

9 A relevant change of control means a change in the persons having control over a body holding the licence to provide a Channel 3 service or any body which is connected with a body holding such a licence and is involved, or is likely to become involved, in the service provided under that licence. The programming matters which would need to be considered include the extent to which time is allocated to different types of programming such as news and current affairs, regional production, and the quality and range of programming.
having offered those rights to a broadcaster in another category or, if no such other broadcaster acquires those rights, without the prior written consent of Ofcom. The effect of these rules is that a number of leading sports events cannot be shown exclusively live on pay-TV in the UK.\textsuperscript{10}

\textit{Commissioning content}

2.15 All licensed broadcasters must comply with articles 4 and 5 of the TVWF Directive which imposes quotas for ‘European works’ and 10 per cent of transmission time or programme budget for independent producers. In addition, section 277 CA 2003 requires all public service channels to ensure that in each calendar year, no less than 25 per cent of the total amount of time allocated to the broadcasting of qualifying programmes\textsuperscript{11} is allocated to a range and diversity of independent productions. Section 285 CA 2003 requires Ofcom to ensure that the regulatory regime for every licensed public service channel includes conditions requiring the broadcaster to put in place a code of practice in relation to its dealings with independent producers.

2.16 With regard to sports rights, in June 2001 the European Commission launched an investigation into the joint selling arrangements put in place by the football clubs in the Premier League for the exploitation in the UK of media rights to Premier League matches. The European Commission adopted a decision in March 2006 that the FA Premier League must sell the rights to broadcast live premier league matches in six separate ‘balanced packages’.\textsuperscript{12} No single broadcaster could be awarded all six; each package must be sold to the highest stand-alone bidder; and more rights must be available on different distribution platforms. These commitments are effective until 2013, covering two three-year periods.

\textit{Advertising}

2.17 Under section 322 CA 2003, all licence holders must comply with Ofcom’s directions on the maximum time to be given to advertisements in any given time period, the minimum interval between two periods of advertisements and the number of advertising slots in any programme, hour or day. The CRR, set up following the merger of Carlton and Granada in 2003, ensures, in particular, that, for the duration of the undertakings,\textsuperscript{13} ITV1’s advertising customers have the right to renew the terms of their 2003 contracts and to reduce the proportion of their ITV1 advertising spend contracted in line with reductions in ITV1’s share of commercial impacts\textsuperscript{14} (see paragraph 4.150). On 6 September 2007 the OFT announced that it would conduct a review of the CRR starting in January 2008.\textsuperscript{15}

\textsuperscript{10}There are two categories of listed events. Group A events must be shown on BBC1, BBC2, ITV1 or Channel 4. These include the Olympic Games, the FA Cup Final and the Wimbledon Tennis Finals. Group B events cannot be broadcast live on an exclusive basis unless adequate provision has been made for secondary coverage (eg broadcast highlights).

\textsuperscript{11}Article 2 of The Broadcasting (Independent Productions) Order 1991 (SI 1991/1408, as amended) defines ‘qualifying programmes’ in terms of who produces them, their costs and their content. In particular, they do not include programmes which consist wholly or mainly of news, or programmes constituting part of a series of programmes which consist wholly or mainly of news and which are presented live.

\textsuperscript{12}Case COMP/C-2/38.173—Joint selling of the media rights to the FA Premier League, 22 March 2006.

\textsuperscript{13}The CRR undertakings were accepted by the Secretary of State in November 2003 following an adverse finding by the CC in relation to the proposed merger.

\textsuperscript{14}One impact represents one viewer who sees a particular advertisement once.

\textsuperscript{15}The OFT’s initial review will be conducted in partnership with Ofcom. The OFT has a duty under the Act to keep undertakings under review and to give the CC such advice as the OFT considers appropriate in relation to any changes to the undertakings. It is for the CC to decide whether and, if so, what changes should be made.
**Multiplexing**

2.18 The regulatory framework for DTT is set out in Part 1 of the Broadcasting Act 1996 (as amended by CA 2003). This provided initially for the availability of six frequency channels or ‘multiplexes’ each able to carry at least three television channels together with some additional data services. ‘Multiplexing’ facilitates the digital broadcasting of several services in a single frequency channel. Multiplex licensing is currently performed by Ofcom. (See Appendix B for a diagram showing the multiplex providers and their respective owners, together with the channels which sit on each multiplex as at July 2007.)

**Electronic Programme Guides**

2.19 Ofcom’s Code on Electronic Programme Guides (EPGs) requires all providers of EPGs licensed under the Broadcasting Acts to give public service channels such degree of prominence as Ofcom considers appropriate.\(^\text{16}\) BSkyB is subject to these requirements.

**Television industry**

**Television supply chain**

2.20 Figure 1 shows the television supply chain, including content acquisition and production; content distribution; and retailing of content and equipment.

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\(^{16}\)The EPG Code also requires that undue prominence is not given to connected channels on an EPG, that an objective policy for allocating listings on the EPG is maintained and published, and that any agreement with broadcasters for the provision of an EPG service is made on fair, reasonable and non-discriminatory terms.
2.21 Content covers a wide range of genres and is derived from a variety of sources. Some broadcasters, including ITV, have large in-house production capabilities; there are many independent UK production companies;\textsuperscript{17} broadcasters obtain the rights to show, for example, US-produced series, movies, or sports events; and there are also libraries of existing programmes available for licensed use by other broadcasters. UK television channels spent an estimated £4.7 billion on programmes in 2004, of which £2.6 billion was spent on first-run original programmes.\textsuperscript{18}

2.22 In order to provide viewers with linear (i.e. scheduled) television services, two main wholesale inputs are required: television channels and technical services. Television channels consist of a linear stream of content ready for distribution. Channel providers, licensed by Ofcom, combine different types of content into a complete schedule (see Appendix B). Channels may be sold on a wholesale basis to retailers operating on different platforms (e.g. BSkyB provides channels to Virgin Media cable viewers) or may be supplied in-house for a downstream retail business (e.g. BSkyB providing channels for its DSat service).

2.23 A channel provider must also acquire transmission capacity so that its channels can be distributed to viewers. Various alternative transmission technologies (platforms) are available, including analogue terrestrial, DTT, DSat, digital cable (cable),\textsuperscript{19}

\textsuperscript{17}The independent production sector comprises nine large groups (with a turnover of over £50 million each); around 20 mid-size to large companies (£10–£50 million turnover); over 100 mid-size growing businesses (£1–£10 million turnover) and several hundred companies with a turnover of below £1 million. Source: PACT, 2007 Production Census.

\textsuperscript{18}Ofcom: Television Production Sector Review, 20 September 2005.

\textsuperscript{19}At end-March 2007 around 310,000 subscribers remained on analogue cable, but these services are being phased out. Source: Ofcom Digital Progress Report, 20 June 2007.
broadband television and mobile television. These are described in more detail in Appendix B. In addition to the provision of transmission capacity, various technical services may be required, including, for example, encoding and compression, conditional access, access control (AC), and EPGs.20

2.24 Retailers supply branded channels to viewers using channels produced in-house or bought on a wholesale basis. Other retailer activities include marketing, collection of fees, and the sale of equipment such as digital set-top boxes, viewing cards and satellite dishes. Many retailers also offer other services such as broadband Internet connection, fixed telephony and mobile telephony services, either as part of a bundled offer or on a stand-alone basis.

2.25 The major FTA broadcasters are the BBC and the commercial broadcasters with public service obligations: ITV, Channel 4 and Five. There are a large number of pay-TV retailers, some of whom are also content providers. The pay-TV retailers include BSkyB, Virgin Media and the newer entrants such as BT Vision, Tiscali and Top Up TV. We discuss each of these in more detail in paragraphs 4.39 to 4.54.

2.26 There are two basic business models available to television broadcasters: FTA and pay-TV. The analogue FTA television services are BBC1, BBC2, ITV1, Channel 4 and Five.21 Digital FTA services are available on DTT and DSat, both of which require the purchase of reception equipment.22 DTT is available through a set-top box and carries around 40 FTA channels. The FTA services available on DTT are marketed under the Freeview brand.23 Around 200 channels are available FTA to owners of BSkyB satellite dishes through the ‘Freesat from Sky’ service.24 The BBC, together with some commercial broadcasters including ITV, has also announced that it intends launching a ‘Freesat’ service by spring 2008 to provide an alternative FTA satellite platform with near universal coverage. Commercial broadcasters of FTA services rely primarily on advertising and sponsorship for their funding.

2.27 Pay-TV retailers typically offer alternative packages of ‘basic’ channels, with ‘premium’ channels (such as sports or movie channels) offered singly or in small packages, usually as an optional extra. Pay-TV is available on DTT, DSat, cable, and the newer platforms (broadband and mobile). Pay-TV retailers rely primarily on subscription fees for their funding; subscribers pay monthly fees to view encrypted channels. They also earn one-off fees for particular programmes (pay-per-view).25 Other sources of revenue for pay-TV broadcasters include advertising funding and sponsorship.

2.28 Current service and technical developments include the offer of bundled services (eg BSkyB’s ‘See, Speak, Surf’ offering of television, broadband and fixed-line telephony); VoD which allows viewers to watch programmes or movies when they want to, selecting from an array of alternative content; HDTV (offering significant improvements in picture quality); and a range of services including personal video recorders (PVRs). New distribution platforms include mobile television and

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20 Conditional access involves the encryption of channels and the de-encryption by authorized viewers using a decoder (usually part of a set-top box) and viewing card. AC services allow broadcasters to offer interactivity features such as the ‘red button’ function on a television’s remote control. An EPG allows viewers to navigate to channels by, for example, example, time, title and channel, to view scheduling, and to read programme synopsis information.
21 In addition, there is the Welsh language version of Channel 4, S4C.
22 FTA digital services are also available on cable from Virgin Media, if subscribing to a Virgin Media telephone package.
23 Set-top boxes retail from around £10. Up to one-third of consumers may also need to upgrade their aerial to receive DTT (but this will reduce to around 10 per cent once the power of the DTT signal is increased after digital switchover). Source: Parliamentary Office of Science and Technology, Analogue to Digital TV Switchover, June 2006.
24 Consumers pay around £150 for the installation of a satellite receiver and dish.
25 Both FTA broadcasters and pay-TV retailers also earn revenue from goods sold on shopping channels and from phone-ins.
broadband television, where audiovisual content is distributed over the Internet, either in the form of a conventional television channel in a ‘closed’ system like cable (IPTV) or in an ‘open’ system where the viewer goes to a website and views or downloads audiovisual content (television-over-the-Internet). These are discussed in more detail in paragraphs 4.67 to 4.70 and in Appendix B.

**Provision of television news**

2.29 Many features of news provision (for example, distribution platforms) are as for any other form of content. However, making television news programmes is a specialized activity, bringing together newsgathering and programme production. Newsgathering involves the reporting of news events and the transmission of reports back to the programme makers’ central production facilities and can be carried out in-house or subcontracted to other news providers or to news agencies such as Reuters. Programme production involves turning the material gathered into broadcast material. This will involve journalistic judgements about which stories to prioritize on a particular day, along with the presentation, recording and broadcast of the programme and final editing of the stories.

2.30 While much of the news content that is broadcast on a particular day will have been generated for that purpose, news programmes also draw on archives of historic news reporting. Non-news programmes (eg documentaries) may also wish to draw on historic footage. Where news is provided by a third party programme provider, the ownership of the rights to news content is subject to commercial negotiation between the news provider and the channel owner.

2.31 Television news is provided to viewers in two main ways:

(a) In specific news programmes or bulletins on general channels, as part of a broader schedule of programming. This is the approach taken on the analogue terrestrial channels and on some digital-only channels, such as More 4 (one of Channel 4’s family of channels).

(b) On dedicated news channels. The two major dedicated news channels are BBC News 24 and Sky News. In addition, some digital-only channels, such as Al Jazeera and CNN, are dedicated news channels.

2.32 Many viewers still make an ‘appointment to view’ the main scheduled news bulletins, which review the day’s events and may also include some more in-depth ‘current affairs’ style content. Dedicated news channels, on the other hand, have a particular advantage in reporting ‘breaking news’, covering major stories as they happen.

*The main parties*

2.33 Paragraphs 2.34 to 2.46 set out relevant background material on the main parties, BSkyB and ITV. Further details of their financial positions are set out in Appendix C.
BSkyB is a leading broadcaster of sports, movies, entertainment and news. It was formed in 1990 from the merger of Sky Television plc and British Satellite Broadcasting Limited.

BSkyB acquires programming to broadcast on its own channels and supplies channels on a wholesale basis to other retailers. It also retails channels (both its own and those of third parties) to subscribers. BSkyB currently makes three of its channels available FTA via the UK DTT platform as part of the branded Freeview offering\(^{29}\) and has a 20 per cent stake in DTVSL. BSkyB also produces its own content. BSkyB’s other activities include the provision of conditional access, AC and EPG services to broadcasters and interactive service providers on the DSat platform; selling advertising time and online advertising; operating interactive services on the DSat platform; providing fixed-odds betting services; and offering its DSat residential subscribers telephony and broadband services.

In 2006, BSkyB launched Sky HD, its HDTV service. BSkyB also provides certain live channels via mobile and broadband. In 2006, BSkyB completed the acquisition of the broadband provider Easynet. At 30 June 2007, the coverage of BSkyB’s broadband network was around 70 per cent of UK homes.

BSkyB principally delivers channels to DSat subscribers in the UK and Republic of Ireland. As at 30 June 2007, BSkyB had approximately 8.6 million subscribers.\(^{30}\) In the year ended 30 June 2007, BSkyB reported an operating profit of £815 million on turnover of £4.6 billion. Around three-quarters of BSkyB’s revenue is derived from subscriptions. Advertising makes up a small proportion of its revenues. Over half of BSkyB’s programming costs relate to sports, with movies and third party content each representing approximately 20 per cent. BSkyB’s market capitalization was £12.0 billion as at 31 October 2007.\(^{31}\)

BSkyB’s ordinary shares are quoted on the London Stock Exchange.\(^{32}\) BSkyB’s largest shareholder is News UK Nominees Ltd which owns 39.1 per cent of BSkyB, with News UK Nominees Ltd’s voting rights capped at 37.19 per cent.\(^{33}\) News UK Nominees Ltd is ultimately owned by News Corporation. As at the end of October 2007, five other shareholders had a shareholding in BSkyB of over 3 per cent.\(^{34}\)

Mr Rupert Murdoch is the founder and, since 1999, Chairman of BSkyB. His son, Mr James Murdoch, has been a director of BSkyB since February 2003, and CEO since November 2003. Mr Rupert Murdoch has been CEO of News Corporation since 1979 and Chairman since 1991. In addition to Mr Rupert Murdoch, three executive or non-executive directors of News Corporation are also directors of BSkyB.\(^{35}\)

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\(^{29}\) In February 2007 BSkyB announced plans to replace these channels (Sky Sports News, Sky News and Sky Three) with a new pay-TV service. On 4 October, Ofcom published its public consultation on BSkyB’s new service, to be called Picnic, which will include broadband and telephony as well as digital television services. Ofcom referred to potential competition concerns regarding pay-TV services on DTT and possibly across other digital platforms. The closing date for Ofcom’s consultation is 14 December 2007.

\(^{30}\) Including approximately 500,000 in the Republic of Ireland.

\(^{31}\) Source: Datastream.

\(^{32}\) BSkyB also has American Depositary Receipts listed on the New York Stock Exchange.

\(^{33}\) BSkyB, BSkyB Holdco Inc, News Corporation and News UK Nominees Limited reached a voting agreement on 21 September 2005 which caps the voting rights attaching to News UK Nominees Limited’s shares at 37.19 per cent.

\(^{34}\) Templeton Global Advisors Limited, Brandes Investment Partners (Brandes), The Capital Group Companies, Janus Capital Management and Legal & General Group.

\(^{35}\) On 7 December 2007, it was announced that, with immediate effect, Mr Rupert Murdoch had decided to step down as Chairman and as a Director of BSkyB. He is succeeded as Non-Executive Chairman by Mr James Murdoch who is leaving his
2.40 News Corporation is a diversified entertainment company with global activities, quoted on the New York Stock Exchange. As of 30 June 2007, it had total assets of approximately US$62 billion and total annual revenues of approximately US$29 billion. Its principal shareholders as at 17 August 2007 were The Murdoch Family Trust (30.1 per cent), Liberty Media Corporation (19.1 per cent) and HRH Prince Alwaleed Bin Talal Bin Abdulaziz AlSaud (5.7 per cent).  

ITV

2.41 ITV (and its predecessors) has been the UK’s largest commercial broadcaster for more than 50 years. It is a broadcaster of FTA content. ITV was created (as ITV plc) from the merger of Carlton and Granada in February 2004.

2.42 The ITV Network is made up of the 15 regional Channel 3 licences, providing television to viewers across the UK on the ITV1-branded channel. Eleven of the licences in England and Wales are owned by ITV. The individual Channel 3 licences broadcast many of the same programmes simultaneously with some regional variations.

2.43 ITV’s operations include:

(a) production of content: through ITV Productions, ITV’s in-house production unit;

(b) broadcasting: commissioning and scheduling programmes on all the ITV channels. ITV also owns 75 per cent of GMTV, the holder of the Channel 3 breakfast time licence; and

(c) managing the relationship with viewers.

In addition, ITV has a 40 per cent stake in ITN and a 20 per cent stake in DTVSL. ITV also owns Multiplex A as well as part of Multiplex 2 (see paragraph 2.18).

2.44 In the year ended 31 December 2006, ITV made an operating profit of £375 million on a turnover of £2.18 billion. Around three-quarters of its revenue was derived from advertising. Its market capitalization was £3.8 billion as at 31 October 2007.

2.45 Trading in ITV’s shares began on the London Stock Exchange on 2 February 2004. BSkyB currently owns 17.9 per cent of ITV’s shares. As at the end of October 2007, four other shareholders had a shareholding in ITV of over 3 per cent.

2.46 Mr Michael Grade was appointed as Executive Chairman of ITV on 28 November 2006, taking up his appointment on 8 January 2007. This followed the departure of Sir Peter Burt (previously ITV’s Chairman) and of Mr Charles Allen (previously ITV’s CEO).
3. The acquisition

**History of the acquisition**

3.1 ITV told us that approaches had been made to acquire the whole of ITV in the last five years:

(a) 

(b) 

(c) Virgin Media, in November 2006, made a cash and share offer amounting to the equivalent of 122p per ITV share.

3.2 BSkyB said that it had held internal discussions regarding the possibility of acquiring a stake in ITV.

3.3 On 17 November 2006 BSkyB announced that it had bought 696 million shares in ITV, amounting to 17.9 per cent of ITV’s issued share capital. BSkyB paid 135p per share, a total of £940 million, for its stake. This represented a 17 per cent premium to the share price on that day and a 28 per cent premium to ITV’s share price prior to the Virgin Media bid. ITV’s share price at the close of business on 31 October 2007 was 99.1p.

3.4 The acquisition took place without any prior consultation of ITV.

3.5 Following the sale, a number of the shareholders who sold to BSkyB rebought shares in ITV in the open market at a lower price.

**Rationale for the acquisition**

3.6 We considered evidence from a number of sources on BSkyB’s rationale for acquiring a stake in ITV. This included BSkyB’s public and confidential statements and third party evidence.

3.7 BSkyB’s Chief Operating Officer, Mike Darcey, gave evidence on 8 May 2007 to the House of Commons Culture, Media and Sport Committee on Public Service Media content. In this he said that ‘[BSkyB’s] motivation was really not so much that [ITV] might end up with Virgin [Media] but that it might end up somewhere’. He also said that BSkyB believed that ITV ‘was at a low ebb, that it would turnaround and that someone would do well out of that’. This is in line with BSkyB’s press release at the time of the acquisition which said that ITV ‘holds substantial potential for long-term value creation’.

3.8 BSkyB said that its rationale for the acquisition was:

3.9 BSkyB said that it had considered ways to increase its effective holding from the 17.9 per cent it had acquired up to the legal maximum of 20 per cent. However,

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41 ITV share price was 106p as at 8 November 2006.
42 [X]
43 [XX]
we note that BSkyB has not chosen to increase its share in any way since the acquisition in November 2006.  

3.10 We considered two possible rationales for BSkyB’s acquisition of a stake in ITV:

(a) to preserve BSkyB’s options as regards the future of ITV; and

(b) to invest in ITV as an undervalued asset.

3.11

3.12

3.13

3.14

3.15 The most immediate way in which the acquisition preserved BSkyB’s options was by impeding the acquisition of ITV by Virgin Media. This acquisition was structured as a scheme of arrangement. BSkyB’s financial adviser stated that. The acquisition of BSkyB’s stake would also enable it to block the squeeze out of minority shareholders under a takeover offer (see paragraph 3.53).

3.16 ITV said that it could not comment on the rationale for the acquisition. It said, however, that the acquisition was widely reported in the press as a means for BSkyB to block pre-emptively any takeover offer for ITV by Virgin Media. It also said that the acquisition took place at a time when ITV had already received an indicative approach from Virgin Media, and it was widely anticipated in the press that Virgin Media was preparing to submit a revised formal offer.

3.17 Third parties told us that the primary motive for BSkyB in obtaining its stake in ITV was to block the Virgin Media bid:

(a) Virgin Media said that the primary motive for BSkyB in acquiring its shareholding in ITV was to act as a blocking stake to any potential third party bid. Virgin Media said that it was not credible that a company would spend £940 million, paying a 28 per cent premium to the market price, in order to obtain a purely passive financial investment.

(b) The BBC noted that, although it did not have a view as to why BSkyB acquired the stake, the argument most reported at the time was that ‘[BSkyB] were there so that others could not be’.

(c) Channel 4 noted the close proximity of BSkyB’s share acquisition and NTL’s interest in acquiring ITV. In its view, there was prior evidence of News Corporation taking a minority stake in a competitor company in order to secure a position of influence over the long-term ownership of that competitor. One example was News Corporation’s acquisition of shares in Fairfax, in Australia. In response to a question as to why News Corporation decided to spend

44We note that, from 26 June 2007, this would have been prohibited as a result of undertakings put in place by the Secretary of State (see paragraph 3.38).

45This could be achieved with a stake of less than 10 per cent, but would not necessarily give the acquirer the ability to acquire the entire issued share capital.
$360 million on the stake in Fairfax, Mr Rupert Murdoch said "just to make it difficult for anybody to take it over".47

(d) Commentary in the press and in equity research suggested that the rationale for the transaction was to block Virgin Media's attempt to acquire ITV.48

3.18 View on rationale

Based on the evidence set out in paragraphs 3.7 to 3.18, we formed the view that BSkyB, through its acquisition of a stake in ITV, was looking to preserve its options as regards the future of ITV. We thought it unlikely that BSkyB would have chosen to invest in ITV purely as an investment vehicle. Numerous other investment options would have been available to BSkyB and we received no evidence to suggest that other investment options had been considered.

Counterfactual

To consider the effect of the acquisition on competition and plurality, we compare the situation that we expect to arise following the acquisition to that which would be expected to prevail had the acquisition not occurred (the counterfactual).49

We looked at two possible counterfactuals:

(a) ITV remains independent, and its shareholder mix remains broadly similar to the situation prior to the acquisition; and

(b) another buyer (for example, Virgin Media) acquires all of ITV.

Independent ITV

All those who have expressed a view believe the appropriate counterfactual to be an independent ITV. ITV, whilst not disputing this counterfactual, suggests that we should also consider the alternative counterfactual that ITV is acquired by a third party.50 We note that, following a period of uncertainty over the leadership of ITV, Mr Michael Grade took up his appointment as Executive Chairman in January 2007 (see paragraph 2.46).

BSkyB said that the appropriate counterfactual in this case was the situation prevailing prior to the acquisition, and that taking account of other potential acquisitions of ITV (eg by Virgin Media) would be 'entirely speculative and inherently uncertain'. BSkyB told us it believed that there was no guarantee that a successful offer for ITV would have resulted from Virgin Media's approach, given ITV board's rejection of the offer.51

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47 'News aims to foil any tilts at Fairfax, says Murdoch' The Sydney Morning Herald, 16 November 2006. Quoted by Channel 4 (main submission, p2).
48 Examples include the brokers reports by Merrill Lynch dated 20 November 2006 'The one billion pound spoiler' and Dresdner Kleinwort on 29 November 2006.
49 See, for example, paragraph 1.22 of Merger References—Completion Commission Guidelines, CC2.
50 ITV main submission, paragraph 6.1. ITV also said that 'the posited counterfactual [an independent ITV] is not the only possible counterfactual in this case, as claimed by the OFT.
51 BSkyB main submission, part D, paragraph 4.2.
3.24 Third parties agreed that an independent ITV was the most appropriate counterfactual. Virgin Media, for example, said that the most appropriate counterfactual was an independent ITV free to pursue strategic alliances. It said that [35]. Channel 4 also agreed that an independent ITV was the appropriate counterfactual.

Acquisition by another party

3.25 ITV told us that ‘the acquisition occurred against the backdrop of an attempted takeover of ITV by Virgin Media …, [35]’. Given this background, we consider whether an ITV acquired by another company would be a more likely counterfactual.

3.26 ITV said that ‘a counterfactual in which ITV had partnered with a third party, and in which ITV benefited from the resulting opportunities (whether through increased investment or synergies) cannot be dismissed by the Commission’. However, ITV’s board minutes from 20 November 2006 make clear that [35].

3.27 We note, however, that neither ITV nor any third party has advocated the use of this alternative counterfactual. Nor did we receive any evidence to suggest that a plausible alternative bid for ITV was likely to be made in the foreseeable future.

Conclusions on counterfactual

3.28 We conclude that an independent ITV is the most likely counterfactual.

Jurisdiction

Introduction

3.29 Under our terms of reference (see Appendix A), the first question we have to decide is whether a relevant merger situation has been created. Under section 23 of the Act, a relevant merger situation is created if two or more enterprises have ceased to be distinct and if either the turnover test or the share of supply test is satisfied.

3.30 We looked at whether the acquisition has led to enterprises controlled by BSkyB and ITV ceasing to be distinct. Under section 26(1) of the Act, two or more enterprises cease to be distinct when ‘they are brought under common ownership or common control’. Under section 26(3):

A person or group of persons able, directly or indirectly, to control or materially to influence the policy of a body corporate, or the policy of any person in carrying on an enterprise but without having a controlling interest in that body corporate or in that enterprise, may, for the purposes of subsections (1) and (2), be treated as having control of it.

3.31 In this case, given the level of shareholding acquired by BSkyB, we considered whether BSkyB had acquired the lowest level of control, that is the ability, directly or

52ITV main submission, paragraph 6.2ff.
53ITV main submission, paragraph 6.2.
54BSkyB suggested that we should verify that the reference was made within the time limits set out in section 23(1)(a) of the Act. The OFT provided us with the relevant details and we are satisfied that the reference was made to us within the specified timeframe.
55Section 26(2) of the Act sets out the conditions for enterprises to be treated as under ‘common control’.
indirectly, materially to influence the policy of ITV (material influence). In our discussion of jurisdiction, we focus on whether the acquisition had given BSkyB the ability to exercise material influence. In our assessment of the competitive effects of the acquisition, we consider BSkyB’s incentive to influence ITV’s policy, together with some examples of the ways in which, in practice, any such influence might be exercised.

3.32 Whether a person has acquired material influence is primarily a question of fact and degree to be assessed on a case-by-case basis having regard to all relevant circumstances. In conducting our assessment, we noted previous decisions of the CC (and the Monopolies and Mergers Commission (MMC)) and the OFT under both the Act and the Fair Trading Act 1973. The *OFT Substantive Merger Guidance* notes that a shareholding giving voting rights of greater than 25 per cent is likely to be seen as presumptively conferring material influence. Additionally, the OFT may examine any case where there is shareholding of 15 per cent or more, to ascertain whether the holder might be able to materially influence company policy. The guidance also notes that, occasionally, it may be appropriate to examine shareholdings of less than 15 per cent to determine whether material influence exists. In practice there have only been a few cases where the MMC or the CC have been asked to examine holdings of less than 20 per cent.

3.33 We took the view that in assessing material influence in the context of the Act we should be concerned with the ability materially to influence policy relevant to the behaviour of ITV in the marketplace. The policy of a company in this context means the management of its business, in particular in relation to its competitive conduct, and thus includes the strategic direction of a company and its ability to define and achieve its objectives.

3.34 We considered whether the following factors might give rise to BSkyB having the ability materially to influence the policy of ITV:

(a) the absolute and relative size of BSkyB’s shareholding and the consequent, likely ability of BSkyB to block special resolutions; and

(b) the industry knowledge and standing of BSkyB which, combined with the absolute and relative size of its shareholding, might give it the ability to influence the strategy of the ITV board.

These are discussed in more detail in paragraphs 3.39 to 3.62.

3.35 We also considered several countervailing factors which might limit the impact of BSkyB’s shareholding:

(a) the provisions of CA 2003 which prevent BSkyB owning more than 20 per cent of ITV (see paragraph 2.12);

(b) the presence of other, significant, active shareholders who could collaborate to outvote BSkyB; and

(c) the absence of evidence of actual influence being exerted to date.

These are discussed in more detail in paragraphs 3.63 to 3.65.

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The definition of ‘control’ in the Act is virtually identical to the definition in the Fair Trading Act so that decisions of the CC and the MMC under the Fair Trading Act are relevant in considering the approach to identification of material influence.
Some third parties argued that BSkyB was likely to be able to secure board representation with its current level of shareholding. It is clear that BSkyB does not have the ability to secure the appointment of a director by the exercise of its voting rights. BSkyB also said that it did not intend to seek board representation or accept it if offered. ITV commented publicly that it would be very difficult to appoint a BSkyB director, given the potential conflicts of interest that would arise. However, ITV also said that a request from BSkyB for board representation could not be ruled out and that, in the event of a request, ITV would come under pressure to accede to any such request.

Although we thought it conceivable that ITV would come under pressure to appoint a BSkyB director to the board, we noted that any such director would risk being subject to conflicts of interest or a breach of competition rules arising through access to commercially sensitive information. We did not expect a BSkyB director to be appointed to the ITV board and we therefore did not take the possibility of such an appointment into account in assessing material influence.

We also noted that BSkyB could in future increase its shareholding, subject to remaining within the 20 per cent limit imposed by the provisions of CA 2003. However, we did not receive any evidence to enable us to form an expectation that this would occur, and hence did not take it into account in assessing material influence.

Factors which might give rise to material influence

Absolute and relative size of BSkyB shareholding and ability to block special resolutions

We note that at 17.9 per cent BSkyB’s shareholding is at the low end of the levels of holding which have, in the past, been found to confer material influence. However, BSkyB’s holding makes it the largest shareholder in ITV by some margin. As at the end of October 2007, BSkyB’s holding was more than twice that of the next largest shareholder, Brandes. Brandes had more than 5 per cent and three other shareholders held shareholdings of more than 3 per cent (see paragraph 2.45).

We assessed whether BSkyB had acquired the ability to block special resolutions proposed by ITV’s management. In previous decisions of the CC (and MMC) and OFT, the ability to block special resolutions has been regarded as a very strong indicator of material influence. Special resolutions must be passed by at least 75 per cent of those who vote on a resolution, in person or by proxy at a general

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57 Directors are normally selected by the board and their appointment (or removal) requires the approval of shareholders through an ordinary resolution.
58 In addition, we note that BSkyB gave undertakings to the Secretary of State for Trade and Industry that, with effect from 26 June 2007, it would not propose any person for election or appointment as a director of ITV, nor accept an invitation to nominate any person for such election, and would use its best endeavours to ensure that no person who is a director or employee of BSkyB or any of its subsidiaries become a director of ITV. These undertakings continue in force until the cessation of the intervention notice or final determination of the reference, whichever is the later. We consider this issue further in the context of our remedies (see paragraph 6.58).
59 In addition, BSkyB undertook to the Secretary of State for Trade and Industry not to dispose of the whole or any part of its shareholding in ITV.
60 There have often been other factors (such as the presence or ability to appoint a board representative) in addition to the ability to block special resolutions (for example, see The Government of Kuwait and The British Petroleum Company plc: a report on the merger situation, October 1988 (Cm 477), and General Utilities PLC and The Mid Kent Water Company: a report on the merger situation (Cm 1125)). In at least one case (see Southern Water plc and Mid-Sussex Water Company: a report on the merger situation, July 1990 (Cm 1126)), the existence of the ability to block special resolutions has been held of itself to be sufficient to determine the existence of influence. However, we note that in that case, Southern had a 25.1 per cent share of the voting share capital in Mid-Sussex, and so had the ability to block a special resolution regardless of the level of turnout.
meeting. The ability to control more than 25 per cent of the votes cast would give a shareholder the ability to block such a resolution.

3.41 Special resolutions are required to make changes to a company’s constitution and to carry out certain procedures which affect the rights of shareholders, including the buyback of shares and the waiver of pre-emption rights.\(^{61}\) The ability to block a waiver of pre-emption rights may be particularly important if the company is looking to raise funds quickly to finance a strategic acquisition, for example. A special resolution is not required for appointment or removal of directors, many acquisitions or disposals or most forms of fund-raising.

3.42 A scheme of arrangement also requires approval by a majority in number representing 75 per cent in value of those who vote at a meeting convened by the court for the purpose of considering the scheme.\(^{62}\) A scheme of arrangement may be one means of giving effect to a merger. A company able to block a special resolution will also be able to block a scheme of arrangement. For the purposes of this report, we use the term ‘special resolution’ to include a resolution approving a scheme of arrangement.

3.43 We looked at whether, should ITV need to raise funds, it would be likely to look for equity funding. ITV’s credit ratings are currently at the lower bounds of investment grade for both Standard & Poor’s and Moody’s. In July 2007, Standard & Poor’s said that ‘[ITV’s] flexibility to make significant and continued investments in programming or selected debt-financed acquisitions will be severely limited … unless it can significantly improve its operating performance’. ITV has consistently stated that it wishes to maintain its investment grade rating. We therefore reached the view that, despite the possible sources of funds outlined in BSkyB’s evidence (see Appendix C, paragraph 17), and ITV’s ability to raise funds through improved efficiency or the sale of non-core assets, ITV would be likely to need equity funding in order to pursue certain major strategic options in the next two to three years.

3.44 In response to our provisional findings, BSkyB provided us with a list of occasions on which ITV (and previously Carlton or Granada) had raised debt and equity over the past ten years. BSkyB said that none of these occasions had been for the express purpose of investment in content. We considered this evidence but it did not alter our view of ITV’s likely need for equity funding in the future.

3.45 Given that its holding is less than 25 per cent, BSkyB does not have the automatic ability to block special resolutions. Its ability to do so will depend on whether its shareholding exceeds 25 per cent of the shares voted at any particular general meeting. We analysed evidence of past voting behaviour at ITV general meetings, the behaviour of shareholders which it replaced and the share of votes which BSkyB would have represented based on voting records of ITV (see Appendix D). This analysis indicates that BSkyB alone would have been able to block a special resolution at all but one of the five general meetings held since the creation of ITV and would have been able to block a special resolution by voting with the other shareholders who voted against a special resolution at the remaining meeting.\(^{63}\) In addition, the analysis indicates that since BSkyB replaced shareholders who typically exercised their voting rights, its voting power in future general meetings is likely to be similar to the historical pattern.

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\(^{61}\)The waiving of pre-emption rights allows the issue of new shares as a way of raising funding through the issue of new shares, typically to financial institutions, without the need to make an offer to all shareholders.

\(^{62}\)A scheme of arrangement also requires court approval. If the scheme includes a reduction of capital, a separate special resolution is necessary.

\(^{63}\)In paragraphs 6.30 and 6.31 we discuss further the level of votes against that are normally cast at any general meeting, regardless of any influence by BSkyB.
3.46 We also thought that, in practice, BSkyB would not necessarily need to defeat a special resolution at a vote in order materially to influence a policy which would require a special resolution. BSkyB would have the opportunity to shape ITV’s thinking by influencing policy formulation at an earlier stage through, for example, meetings between shareholders and ITV. Further, we thought that ITV’s appetite for pursuing certain strategies at all would be reduced if it was aware that these strategies were likely to cause conflict with BSkyB.

3.47 If ITV perceived BSkyB to be likely to have 25 per cent of the vote, we would expect ITV to take into account any expected opposition from BSkyB in formulating its policy and in deciding whether to bring it forward. In these circumstances, BSkyB’s ability materially to influence policy might not turn on the precise percentage of the vote held.64

3.48 BSkyB said that past voting patterns were not the most reliable guide to future voting patterns and that its shareholding would not offer the ability to block special resolutions. It provided us with an analysis (the Lintstock Reports) which set out how, in its view, historical voting patterns should be adjusted to allow for an increase in turnout. The reasons for these adjustments as set out in the Lintstock Reports are:

(a) a trend towards increasing concentration of ownership in listed companies;

(b) a gradual upward trend in voting levels across FTSE 100 companies generally, derived in part from the increasing concentration in ownership; and

(c) the fact that issues which are contentious tend to elicit higher voting levels.

3.49 The Lintstock Reports suggest that a 7.3 per cent increase in turnout should be assumed across all FTSE companies. BSkyB noted that, at the one general meeting held since the acquisition,65 its shares represented less than 25 per cent (in fact, 24.9 per cent) of the shares voted at the meeting. This, in its view, demonstrated the trend towards increasing turnout identified by Lintstock.

3.50 In addition, based on the FTSE 100 average in 2005 and 2006, the Lintstock Reports suggest that discussion of contentious issues had raised turnout at shareholder meetings by 5 to 7 percentage points. BSkyB therefore said that turnout would be expected to be significantly higher than the historical average at any meeting where the ITV board was going to seek to force through a resolution in the face of opposition from BSkyB.

3.51 We sought evidence from other ITV shareholders about their voting record and history of involvement in ITV as shareholders. We established that since its inception, ITV has had a relatively active shareholder base which has turned out to vote at general meetings and that, in particular, the financial institutions which have the next largest holdings after BSkyB were active before, as well as after, the acquisition. BSkyB itself replaced active shareholders.

3.52 We thought that the most directly relevant evidence to turnout and likely future voting patterns was the record of historical turnout at ITV general meetings. Despite the evidence provided in the Lintstock reports, we could not form an expectation that the trends noted, either in terms of increasing turnout or higher turnouts for contentious

64In paragraphs 6.26 to 6.28, we consider how votes withheld at general meetings may affect BSkyB’s ability materially to influence ITV’s strategy. This issue is important in the context of remedies because we must be confident that any proposed remedy would be effective. However, we did not find it necessary to consider this as part of our discussion of material influence.

issues, would give rise to a significant change in voting patterns. Nor did we think that we should base any conclusion about material influence on the results of voting at a single general meeting.

3.53 The bid by Virgin Media was proceeding by scheme of arrangement and therefore required approval of at least 75 per cent of shareholders at a general meeting.

3.54 Virgin Media said that shareholders in ITV who were also shareholders in BSkyB or News Corporation might be likely to vote in line with BSkyB, which would give BSkyB a much higher share of the votes cast at any general meeting of ITV. We spoke to several of the larger shareholders with shares in both ITV and BSkyB. They told us that they held shares belonging to various institutions, primarily pension funds, each of which may only hold shares in one or other company. Voting tactically to support, for example, BSkyB rather than ITV, rather than necessarily in the interests of the individual investor, may therefore harm individual shareholders (for example those that hold only ITV shares) and would be a breach of the fund manager’s duty. We therefore did not place reliance on this line of argument in reaching our conclusions.

3.55 Having regard to expected voting patterns, we thought that BSkyB’s shareholding would give it the ability to block a special resolution and that this would enable BSkyB materially to influence the policy of ITV where that policy would require a special resolution. In addition, as set out in paragraph 3.46, BSkyB’s shareholding places it in a position materially to influence ITV’s policy at an earlier stage in policy formulation.

3.56 We also considered whether BSkyB’s ability to block a contested or ‘hostile’ takeover of ITV would give it the ability to affect ITV’s strategy. We did not think that this would be the case, since such a takeover would not form part of ITV’s strategy. However, we thought that the ability to block a takeover (whether hostile or friendly) could increase BSkyB’s ability to influence other shareholders (see paragraphs 3.58 to 3.62).

3.57 We noted that BSkyB would also have the ability to block a merger recommended by the ITV Board as part of its strategy for the business, for example through blocking a squeeze out (see paragraph 3.53) or a scheme of arrangement (see paragraph 3.42).

*BSkyB industry knowledge and standing combined with the size of its shareholding*

3.58 BSkyB is a highly successful player in the audiovisual services sector and has pioneered many important innovations. In previous decisions the MMC and CC have identified the additional weight which a shareholder active in the same market can carry. We considered whether BSkyB’s standing as an industry player was likely to contribute to the weight which its views would carry among other shareholders.

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66 We found, historically, that there was no evidence of a correlation between turnout at ITV general meetings and the type of resolutions put to the meeting. BSkyB said that this was not relevant because none of these resolutions could be considered to be ‘contentious’. We also noted a comment made by BSkyB’s advisers. [67]

67 A minority squeeze out as part of a takeover offer would require 90 per cent acceptance: control can be achieved by the acquisition of a lower percentage but this would not necessarily give the acquirer the ability to acquire the entire issued share capital.

68 See, for example, *The Peninsular and Oriental Steam Navigation Company and European Ferries Group PLC: a report on the merger situation*, December 1986 (Cmnd 31); *Stagecoach Holdings plc and Mainline Partnership Limited*, March 1995 (Cm 2782); *Anticipated acquisition by Robert Wiseman Dairies plc of the fresh milk business of Scottish Milk Dairies Limited (OFT advice)*; *Vivendi SA & British Sky Broadcasting Group plc: a report on the merger situation*, April 2000 (Cm 4691); and *Stora
3.59 Many of the other large shareholders in ITV are sophisticated financial institutions with in-house expertise in the media sector. Nevertheless, particularly in areas such as HDTV where BSkyB has played an innovative role, we would expect BSkyB’s views to be of particular interest to other shareholders. If BSkyB chose to oppose a course of action favoured by ITV’s board, it would be likely to have the ability to influence other shareholders due to the size of its shareholding combined with its industry knowledge and standing, thus enabling it to block a special resolution with others.

3.60 ITV told us that, in addition to the ability to block special resolutions, it anticipated that BSkyB would have material influence as a result of its ability to act as a ‘disruptive shareholder’. The incentives of most of ITV’s shareholders would be to maximize their returns from their shareholding in ITV. BSkyB, on the other hand, as a major competitor to ITV, might in some cases find that ITV management were pursuing a course of action which was not in BSkyB’s best interests. ITV told us that in addition to blocking special resolutions, whether or not related to the funding of a particular strategic action, a shareholder with a holding of the size of BSkyB’s could cause considerable disruption to the management of a company’s affairs by using its voting power to vote against ordinary resolutions, opposing the declared strategy of the ITV board in the press, within the media sector and in possible alliance with other shareholders.

3.61 Virgin Media supported this view, saying that ‘you listen to your major shareholders and you share your intentions with your major shareholders, and failure to do so … [is] at your own peril’. It told us that, in our provisional findings, we had understated the degree to which BSkyB could use its importance and stature as an industry player, together with its position as the largest shareholder, to influence the overall strategy and commercial direction of ITV. It gave us recent examples of activist minority shareholders having had a material impact on the strategy and direction of major companies, although we noted that these were examples of activist financial investors who would have been in a somewhat different position as an investor to a competitor such as BSkyB.

3.62 In summary, we found that BSkyB’s industry knowledge and standing, together with its position as the largest shareholder, would be likely to increase its ability to influence other shareholders, enabling it to block a special resolution with others. Although we recognized the argument that BSkyB would also be in a position to act as a disruptive shareholder more generally, we did not attach weight to this in reaching our conclusion. We could not form an expectation that BSkyB could expect to be able to exert sufficient influence to force through an ordinary resolution.

**Countervailing factors relevant to material influence**

*Cross-media ownership rules*

3.63 BSkyB is precluded from owning more than 20 per cent of ITV as a result of CA 2003 (see paragraph 2.12). BSkyB said that this placed it in a less strong position than a shareholder with a 17.9 per cent stake would normally have because it could not buy more shares to increase its leverage over ITV. We noted that the ability of BSkyB to further strengthen its position in ITV was restricted but we did not find that this reduced the impact of the existing shareholding.
**Countervailing influence of other shareholders**

3.64 BSkyB drew our attention to several other significant shareholders in ITV. Based on shareholdings at the end of October 2007, BSkyB could be outvoted by a coalition of as few as four of these acting together. We recognize that there are a number of financial investors with significant shareholdings in ITV and a history of active engagement with the company. Nevertheless, we concluded that there would be circumstances in which the other major shareholders would not, for example, be able to ensure that the board could secure a special resolution in the face of opposition from BSkyB.

**No evidence of actual influence**

3.65 BSkyB also said that there had been no example to date of BSkyB seeking to exert influence. Indeed it noted that it had not sought or been offered a shareholder meeting by ITV (although the Chief Executives of the two companies had met and spoken on other matters). We noted this but did not place weight on it. We would not expect to see evidence of influence being exerted whilst a transaction was under investigation. In any event, the test that we have to apply in deciding whether a relevant merger situation had been created is whether the ability to exert material influence has arisen, not whether, in practice, that ability has been exploited.

**Conclusions on material influence**

3.66 We found that the size of BSkyB’s holding both in absolute and relative terms was such that on the basis of past voting patterns it would be able to block special resolutions proposed by ITV’s management. BSkyB’s ability to block a special resolution would limit some of ITV’s strategic options, for example its ability to raise funds. BSkyB’s importance and stature as an industry player, together with its position as the largest shareholder, would give additional weight to its views, increasing its ability to influence other ITV shareholders. We did not find that any of the countervailing factors set out in paragraphs 3.63 to 3.65 offset BSkyB’s ability to exercise material influence.

3.67 Based on the evidence set out in paragraphs 3.39 to 3.65, we conclude that, as a result of the acquisition, BSkyB has acquired the ability materially to influence the policy of ITV. This ability gives rise to common control for the purposes of section 26 of the Act.

**Turnover**

3.68 ITV’s turnover in the financial year ended 31 December 2006 was £2.18 billion. Accordingly the turnover test under section 23(1) of the Act is satisfied and we are not required to consider the application of section 23(2).

**Conclusion on relevant merger situation**

3.69 We conclude that a relevant merger situation has been created.

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*We note that, in any case, BSkyB is bound for the period of the inquiry to respect the undertakings put in place by the then Department of Trade and Industry (see footnotes 58 and 59).*
4. Market definition and assessment of competitive effects

Overview

4.1 In this section of our report we analyse the competitive effects of the acquisition, taking into account our view of the counterfactual set out in paragraph 3.28. We looked in particular at:

(a) audiovisual services;
(b) advertising; and
(c) national television news programme supply.

4.2 In each area, we start by defining the market, in terms of both product and geography. We then discuss any underlying factors affecting existing and future levels of competition in the market, including, as appropriate, an outline of the major players in the market, estimated market shares and details of pricing structures. Next we assess the level of competition in the market absent the acquisition, before analysing the competitive effects of the acquisition and drawing our conclusions. Regardless of the rationale for BSkyB’s acquisition, we conduct our competitive assessment by considering how the nature of competition in the market may affect BSkyB’s incentives to influence ITV’s policy.

Audiovisual services

Market definition

Introduction

4.3 In order to define the market or markets for the audiovisual services provided by ITV and BSkyB, we adopt the conceptual approach of the SSNIP test as set out in our guidelines.71 This defines a market according to the ability of a hypothetical monopolist profitably to carry out a small but significant price increase, or otherwise reduce its competitive effort (in terms, for example, of the quality of its offer) over a narrow set of products. This analysis focuses on the substitutability of different products to end-users, and on supply-side substitution. In line with our usual practice, we have carried out our analysis at current prices and conditions of competition, regardless of whether these represent competitive price levels.

4.4 There are a number of market characteristics which affect our market definition. First, the parties operate in a two-sided market. This means that the companies serve two distinct sets of customers—viewers and advertisers—which are interdependent. Furthermore, as set out in Section 2, the parties operate different business models, with BSkyB deriving the majority of its revenue from subscription fees and ITV relying primarily on advertising revenue. The BBC operates a third business model, relying primarily on revenue from its licence fee (see paragraph 4.41).

4.5 Second, ITV and BSkyB compete for viewers within a differentiated product market. This differentiation can be seen in a range of dimensions, such as the amount, type and quality of content provided, the timeliness with which the content is provided (linear or on-demand), the provision of complementary services and equipment (such

as EPGs and PVRs), and whether services are available as part of a bundle with other services (for example, telephony and Internet access).

4.6 We note that observed price differences are not necessarily an indication of a lack of substitutability in any market. In two-sided markets suppliers can compete with one another at different price points, given the ability to generate revenue in two separate markets. For example, FTA services may compete directly for viewers with pay services, with higher viewing figures indirectly generating higher advertising revenues.

4.7 BSkyB noted that this context poses some difficulties in applying a standard SSNIP test and using specific quantitative data. Nevertheless, as set out in paragraph 4.3, we use the conceptual framework of the SSNIP test, relying as appropriate on a variety of qualitative and quantitative evidence to inform our market definition.

4.8 Although, as set out in paragraph 2.20, the provision of audiovisual services covers different stages in the supply chain, we find it helpful in this case to conduct market definition in terms of viewers’ ability to substitute between different retail offers. In our view, this allows us to focus our analysis on the main driver of revenue for all companies in the market—ultimately, competition for viewers—regardless of the specific business strategy they adopt. We distinguish between the different stages of the supply chain where appropriate in carrying out our competitive assessment.

Product market

4.9 We looked at the retail products provided by each of the parties. Both parties provide audiovisual content to viewers, but in each case the content is bundled and distributed in a different way:

(a) ITV creates television channels which are available to viewers FTA, whether or not the viewers subscribe to pay-TV. ITV does not have a direct relationship with a set of viewing customers.

(b) BSkyB has a direct relationship with its subscribers. Subscribers pay BSkyB a monthly fee in exchange for access to packages of channels. In order to receive these channels they must install equipment to receive and decode a satellite signal, including a satellite dish and set-top box.

4.10 BSkyB sells a range of channel packages. Prices for these packages range from £16 to £45.\textsuperscript{22} The pricing structure distinguishes between Sky Sports and Sky Movies channels (‘premium’ channels) and other channels (‘basic’ channels). Further details of BSkyB’s packages are set out in Appendix E.

4.11 BSkyB also provides a range of other services. For example, customers can choose a Sky+ box, which incorporates a PVR, or one that enables them to watch HDTV, as their set-top box. All households with a satellite dish and a BSkyB set-top box have automatic access to an EPG (see paragraph 2.23). As well as television-only packages, BSkyB supplies packages that include television, fixed telephone and broadband services, marketed under the ‘See, Speak, Surf’ banner.

4.12 BSkyB said that, in its view, the relevant market was broad, covering:

(a) FTA services;

\textsuperscript{22}Prior to 1 September 2007 the equivalent range of prices was £15 to £43.50.
(b) pay-TV packages (supplied by other retailers such as Virgin Media, BT Vision, Setanta and Tiscali);

(c) VoD services (from retailers such as Virgin Media, Top Up TV and BT Vision);

(d) Television-over-the-Internet services (including i-tunes, Joost, Babelgum and YouTube); and

(e) DVD sales and rentals.

4.13 ITV said that the inquiry should be framed in terms of a market for ‘all TV’, in order to capture the loss of rivalry between the BSkyB and ITV business models. It said that competition within the market was characterized by ‘both price competition and dynamic, innovation-based competition, as UK television markets move towards digital switchover’.\(^{73}\) It said that consumers would cease to subscribe to BSkyB if the channels it provided were not viewed sufficiently often to justify its subscription charges, and that competition between the parties occurred first and foremost for viewers.

4.14 Third party views of the market varied.\(^{74}\) Virgin Group, for example, suggested that the boundaries between FTA and pay-TV were becoming increasingly blurred, and that the acquisition could be analysed within a market for ‘the supply of television services generally’. The BBC said that it supported the OFT’s view that ‘an independent ITV free to strengthen its digital free to air offering offers a materially greater threat to BSkyB’s market power in premium pay-TV market’. Virgin Media said that ‘whilst there is a competitive dynamic between free multi-channel TV and pay-TV …. there is a separate pay-TV market within which BSkyB already exercises market power’. Setanta said that the FTA offer exerted some constraint over pay-TV but not sufficient to bring pay-TV prices to the competitive level. Both Setanta and Five said that whilst BSkyB faced strong competition from terrestrial channels on its general entertainment offer (which included channels such as Sky One), its premium offer faced less competition. On the other hand, Top Up TV did not think that BSkyB competed with Freeview to a significant extent, and Channel 4 said that ‘pay’ and ‘free’ represent largely distinct markets, with BSkyB ‘clearly the dominant player in terms of pay television platforms’.

4.15 In order to assess demand-side substitution, we looked at evidence of customer switching. We first looked at evidence of switching between pay-TV providers. Survey data from internal research carried out by BSkyB suggests that of those customers likely to switch to another provider within the next three months, at least \([\%]\) per cent would switch to another pay-TV provider (including \([\%]\) per cent to cable). For cable customers thinking of switching, \([\%]\) per cent would switch to another pay-TV provider (including \([\%]\) per cent to BSkyB).\(^{75}\) We have also seen evidence of competitive responses between pay-TV retailers to the bundled offers of other providers and note the existence of extensive marketing campaigns (see paragraph 4.66). This suggests to us that pay-TV packages are likely to be reasonable substitutes for one another. We therefore consider all pay-TV to be in the same relevant economic market.

4.16 We next looked at whether FTA services would provide a constraint to a monopolist of pay-TV attempting to raise prices or otherwise reduce its competitive efforts by a small but significant amount from current levels.

\(^{73}\)ITV Main Submission, paragraph 2.16.
\(^{74}\)See third party submissions and hearing summaries on CC website.
\(^{75}\)[\%]
4.17 As set out in paragraph 2.26, FTA services can be accessed in a variety of ways, some of which require one-off fees for equipment. The widespread availability of Freeview services and the opportunity to obtain around 200 channels FTA through a satellite dish, mean that most UK viewers have access to a free multi-channel service after purchasing the relevant equipment. These free services overlap with those received by pay-TV subscribers, and terrestrial channels constitute some of the most popular viewing on all platforms.

4.18 We looked at the evidence of competition between FTA and pay-TV (see paragraphs 4.73 to 4.83 and Appendix E). BSkyB said that ‘there is a chain of demand side substitution that links free to air services, basic only pay television packages and pay television packages that contain both premium and basic pay television channels’.

4.19 We note that all pay-TV packages offer content and services in addition to those which are available FTA. Certain pay-TV providers with the most similar offers are likely to be particularly close substitutes, for example BSkyB and Virgin Media, whose packages are most similar, and whose marketing clearly targets one another’s services (see paragraph 4.66).

4.20 In our view, it is likely that the FTA offer is a closer substitute to packages which include only basic channels than those which include basic and premium channels. As such, FTA services may be a relatively weaker constraint on those packages which include premium channels.

4.21 We looked at whether it might be appropriate to segment the market by distribution platform. As set out in paragraph 2.23, television services are available over a variety of platforms, including analogue terrestrial, DTT, DSat, cable, broadband and mobile television. A viewer who is watching a channel over a particular platform will not necessarily be able to distinguish the distribution platform. We therefore believe that it would be inappropriate to segment the market purely on the grounds that some packages are delivered over different platforms. However, some platforms may have an impact on the ability of retailers to deliver a particular content or to reach a high number of potential customers. Any impact on demand-side substitution will be considered in the context of the assessment of the competitive effects of the acquisition.

4.22 We looked at whether the product market should be defined more widely than FTA and pay-TV. One element of differentiation in the provision of audiovisual services is between traditional linear broadcasting and VoD. Many retailers offer both linear content and VoD. For example, viewers may watch a programme at the time it is broadcast or through a VoD catch-up service. Most content is suitable for both means of delivery to viewers (exceptions include content that it typically watched live, such as sport or news) and we consider that if a provider of audiovisual services possesses suitable content and sufficient capacity, it can choose the form of delivery that suits its commercial offer best. Therefore we believe that, for content suitable for VoD, there is sufficient demand- and supply-side substitution between VoD and linear broadcasting that VoD should form part of the same market.

4.23 We also looked at whether, as suggested by BSkyB, the market should be defined more broadly to cover audiovisual services delivered over the Internet (television-
over-the-Internet as distinct from IPTV services (see paragraph 2.28)). We note that this is growing in popularity. Several high-profile media companies have recently launched new television-over-the-Internet services (for example, the BBC’s iPlayer, ITV.com, Channel 4’s ‘4oD’ Internet service and BSkyB’s ‘Sky Anytime to PC’ VoD service). These services typically offer a catch-up/view-again VoD service. Other companies such as Joost, Babelgum and Google (YouTube) have also launched television-over-the-Internet services.

Research carried out in 2006 by Ofcom suggested that around 5 per cent of the adult population (8 per cent aged under 25) had watched video or television-over-the-Internet ‘in the last month or so’. There was also some evidence of substitution away from more traditional television viewing. The rapid increase in broadband connections facilitates viewing of television-over-the-Internet. Half of UK adults now live in households with a broadband Internet connection.

However, this content cannot yet be readily viewed on main television sets, suggesting that it may not be a good substitute for many viewers. Although devices are starting to come to market that facilitate this, they are not yet widespread and the quality of the service is dependent on the quality of the underlying broadband network. We understand, for example, that the picture quality of television-over-the-Internet services can often be inferior to that available on other digital platforms, and there can be delays while material is downloaded. Television-over-the-Internet is currently less well adapted than conventional broadcast technologies to situations where a large number of viewers attempt to watch content simultaneously, as they might in the case of primetime drama, soap operas or major sports events.

For these reasons, we believe that it is unlikely that a hypothetical monopolist of all television services would be constrained in lowering the competitiveness of its offer by a small but significant amount because of the existence of television-over-the-Internet services.

We also considered whether the market should include the sale or rental of DVDs. The content available on DVDs is the same as some content offered in the all-TV market (particularly in relation to movies and TV series). However, DVDs do not provide an alternative to much of the content broadcast on television including, for example, any live content. We do not believe that the sale or rental of DVDs is likely to constrain a hypothetical monopolist of all-TV services. In terms of demand substitution, we therefore formed the view that the market should not be widened to include television-over-the-Internet or the sale or rental of DVDs.

We looked at the possible impact of supply-side substitution on our market definition. Much recent entry to the UK television market has come from existing players in the telecommunications market such as BT, Tiscali and Orange Home UK plc (Orange; a wholly-owned subsidiary of France Telecom), which are looking to provide, or expand

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78 On 27 November 2007 ITV, BBC Worldwide and Channel 4 announced the launch of a joint service offering VoD (Kangaroo).
79 In addition, 4 per cent (7 per cent aged under 25) had watched television-over-the-Internet at the same time as they were broadcast on television (simulcast) at least twice in the past six months.
80 People who had recently watched video content or television programmes via the Internet were asked whether their usage of other services fell. While 42 per cent said that there was no effect on other activities, 18 per cent said that their viewing of FTA television services fell, and 12 per cent said the same for each of cable and satellite viewing. BBC iPlayer Market Impact Assessment: Consumer Survey, 2006.
82 For example, Apple has recently launched a product that allows users to transfer content from a computer to a television over their wireless network.
83 Particularly for content that is not downloaded in advance.
84 Because companies in the all-TV market have different business models, a hypothetical monopolist could relax its competitive effort in different ways. A company offering a FTA service, for example, might reduce the quality of its content, whereas a pay-TV retailer might also increase its subscription fees.
their provision of, audiovisual services using IPTV technology. Virgin Media is also active in both sectors. Recent entries suggest that a strong brand and a ready-made customer-base in the telecommunications sector can facilitate a move into television.

4.29 Third parties said that significant investment in terms of infrastructure and content would be needed for companies to switch to supplying audiovisual services to the UK market. Similar issues would apply to supply-side substitution by Internet-based companies such as Google and Yahoo. We therefore do not believe that new entrants could easily supply a competing service.

4.30 Our view, based on the evidence set out in paragraphs 4.9 to 4.29, is that FTA and pay services compete with one another within a market for ‘all-TV’, which includes VoD. The all-TV market is highly differentiated, however, and we conduct our analysis of the impact of the acquisition not only by assessing the impact on the market as a whole under current competitive conditions, but also by looking separately at possible future competition in pay-TV. Despite the dynamic nature of the industry, we conclude that, based on our view of likely future trends, the market should not be widened to encompass television-over-the-Internet services or DVD sales and rentals.

4.31 In response to our provisional findings, we received submissions from several third parties pointing to previous cases where the relevant market was found to be no wider than pay-TV services despite the existence of a constraint from FTA. They suggested that we should look at the possibility of defining a narrow market in this case. We believe that the relatively broad market that we defined in paragraph 4.30 is the appropriate framework for analysing any loss of competition arising from this acquisition. However, we note that this does not imply that the same market definition should necessarily be used to analyse other mergers in the industry or should necessarily apply in other competition cases.

Geographic market

4.32 ITV said that it offered its products and services primarily to a UK market. BSkyB considered that the geographic scope of the ‘supply of audiovisual programming to end users’ could be considered to be the UK.

4.33 We note that a number of channels owned by companies active outside the UK are supplied in the UK. However, shares of viewing are on aggregate dominated by UK-based companies.

4.34 ITV said that for technological reasons platforms available in the UK generally cannot provide services in other countries. Platforms which rely on physical infrastructure to transmit content to a viewer’s home, for example cable and IPTV, are clearly unable to reach wider audiences, and other platforms are subject to licensing regulation.

4.35 Consumers are not readily able to switch to television services from outside the UK, and language barriers would often prevent them from consuming such content (with a few notable exceptions, for example services from the USA).

4.36 We therefore conclude that the market should be no wider than the UK.

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85 It is possible that if BSkyB were to face stronger competition from pay-TV retailers, prices would fall to an extent that FTA services no longer presented a constraint. In this situation it would be appropriate to define a separate market for pay-TV.

86 The only exception is the supply of content, a substantial amount of which is exported to Germany, Australia and the USA.

87 BARB viewing shares for May 2006 provided by ITV are consistent with this.
Conclusion on market definition

4.37 We therefore conclude that the appropriate framework for analysing any loss of competition arising from the acquisition is a UK market for all-TV which includes both pay-TV and FTA services.

Underlying factors affecting competition

4.38 Before assessing the levels of competition in the market and the impact of the acquisition, we set out some key factors affecting competition. Paragraphs 4.39 to 4.54 give an overview of competitors to BSkyB and ITV; paragraphs 4.55 to 4.63 set out our views on market shares.

Overview of competitors

• The BBC

4.39 The BBC is the longest-established national television channel operator in the UK. It is constituted as a public corporation operating under its own charter (renewed on 1 January 2007). The Charter provides the BBC with a wide public remit, which includes the provision of a broad range of high-quality programming within its broadcasting schedule. It operates a number of digital public service television channels—BBC1, BBC2, BBC3, BBC4, CBBC, CBeebies, BBC News 24 and BBC Parliament—with BBC1 and BBC2 also available FTA on the analogue terrestrial platform. The BBC’s digital television channels are available FTA on DTT (as part of DTVSL’s Freeview package) and on DSat; and are also accessible to pay-TV viewers as part of the basic access packages offered by cable and IPTV operators. The BBC also has interests in a number of commercial television channels either wholly owned by BBC Worldwide or operated by joint ventures between BBC Worldwide and other media companies such as Flextech Television (Virgin Media) and Discovery Communications Inc.

4.40 The BBC is one of the largest purchasers of independent productions and its in-house production arm is the largest UK programme maker (the programme budget of BBC1 was £1.0 billion in 2006/07). The BBC is also the largest provider of national television and radio news. The BBC’s other television interests include:

(a) control of two of the six DTT multiplexes and a 20 per cent share in DTVSL;

(b) a new FTA DSat service, ‘Freesat’, planned for launch by spring 2008;

(c) HDTV services—the BBC launched a dedicated HD channel on the DSat and cable platforms on 1 December 2007. It also completed a successful six-month trial of HDTV on the DTT platform with ITV, Channel 4 and Five in 2006 and has approval to launch on this platform in the future, and

(d) Television-over-the-Internet—the BBC’s iPlayer will provide a free ‘seven-day catch-up’ service.

89 With around 60 per cent of audience shares for television news in October 2006 (BBC1, BBC2 and BBC24). Source: New News, Future News, Ofcom, 4 July 2007 (Figure 3.2).
90 See paragraph 4.112.
4.41 The BBC’s television (and radio) channels are funded principally from the annual television licence fee which, for the year ended 31 March 2007, generated £3.2 billion. The BBC also has some commercial activities, with a combined income of around £976 million (including £810 million from BBC Worldwide, which provided a profit of £111 million).

- The commercial public service broadcasters

4.42 We give an overview of ITV in paragraphs 2.41 to 2.46. The other two commercial PSBs are Channel 4 and Five.

4.43 Originally established in 1982, Channel Four Television Corporation is a statutory organization created by an Act of Parliament. Its particular public remit is to offer distinctive programming the market might not otherwise provide. Channel 4 is a national channel, and is available FTA on analogue terrestrial as well as in digital format. It is funded primarily from television advertising revenues. Its total programming costs (including the purchase of ready-made content) are in excess of £500 million a year. Channel 4’s total group turnover for the year ended 31 December 2006 was £937 million.

4.44 Channel 4 operates three digital-only channels, Film4, E4 and More4, available on all the main digital platforms (FTA on DSat and DTT). Channel 4, like the BBC and ITV, also operates a television-over-the-Internet VoD service known as 4oD—the first terrestrial television company in the UK to allow programmes to be downloaded over the Internet. It has a 20 per cent stake in DTVSL. Channel 4 has a generally younger audience than ITV1 with a higher proportion of ABC1 viewers.

4.45 Five was set up in 1997 and is wholly owned by RTL Group (part of the German Bertelsmann group). Its main channel has slightly less than full national coverage, with its terrestrial analogue transmissions reaching about 82 per cent of UK homes. Five launched two digital-only channels, Five US and Five Life, in October 2006 which, together with Five, are available on all three of the main digital platforms.

4.46 Five is a general entertainment channel which obtains its income primarily from advertising. Its total programming spend (in 2005) was around £190 million, relying mainly on original commissions and acquired programming, and its revenue for the year ended 31 December 2006 was £318 million. Five has the smallest share of viewing of the commercial public service broadcasters, with a bias towards a younger, mid-market, male audience.

- The pay-TV retailers

4.47 The pay-TV retailers include BSkyB, Virgin Media and the newer entrants such as BT Vision, Tiscali and Top Up TV. Paragraphs 2.34 to 2.39 give a brief outline of BSkyB. In paragraphs 4.48 to 4.54 we set out the key details of the other pay-TV retailers.

4.48 Virgin Media was launched in February 2007. It was created by the merger in March 2006 of NTL and Telewest and the subsequent purchase of Virgin Mobile. For the
year ended 31 December 2006 it had total revenue of £3.6 billion.Virgin Media controls access to nearly all the UK's cable network, with coverage mainly limited to urban areas (available to 45 per cent of UK households at the end of 2006). It offers customers a number of television, broadband, fixed-line and mobile telephony services. NTL and Telewest were the first to begin rolling out VoD services in January 2005, available to all digital subscribers by the end of 2006. A dispute with BSkyB over wholesale terms of supply has meant that, since the end of February 2007, BSkyB’s basic channels (Sky One, Sky News, Sky Travel and Sky Sports News) have not been available from Virgin Media.

4.49 At the start of 1999, Virgin Media had penetration of 12.4 per cent of households. As at Q1 2007 it had grown to 13.4 per cent, with penetration of 26.7 per cent for households within cabled areas. Virgin Media has stated publicly that it is looking to expand the provision of its services outside its cable network by using local loop unbundling (LLU) technology.

4.50 Several companies are now using IPTV technology to deliver audiovisual services to end-users. These include Tiscali and BT Vision. Tiscali offers a range of packages of television channels from news and current affairs to documentaries and entertainment, as well as VoD. BSkyB retails some of its channels directly to Tiscali customers over the ‘Sky by Wire’ service.

4.51 To date, Tiscali’s IPTV services have been limited to parts of London and Stevenage, where it had around 60,000 customers (as at the end of March 2007). It has announced plans to expand its footprint to over 10 million homes by the end of 2007. In October 2006, it announced a target of reaching 1.3 million customers via LLU by the end of 2010, of which around 35 per cent would take IPTV. Tiscali also has around 1.5 million broadband customers, which will rise to 1.9 million following the acquisition of the broadband and voice division of Pipex.

4.52 BT Vision was launched in December 2006 as BT Telecommunications plc’s (BT’s) new digital television service available to BT broadband customers. It offers access to DTT channels through its set-top box, as well as a range of on-demand entertainment over IPTV. At the end of September 2007 it had more than 60,000 customers. It forecasts that subscriptions will reach [X] by the end of March 2008, rising to between [X] in the medium term. Customers have the choice of subscribing to a range of content packs or acquiring content on a pay-per-view basis.

4.53 Top Up TV provides pay-TV services over the DTT platform. In addition to the Freeview channels, it offers VoD content from about 25 basic tier channels at £9.99 per month. DTT customers can subscribe to Setanta Sports for £9.99 per month without the need to ‘buy-through’ any Top Up TV retail service. It currently has a relatively small number of subscribers ([X]) and is seeking to increase this to reach [X] within about [X]. Top Up TV’s current model is based on a ‘push VoD’ methodology, where content is downloaded to a PVR and stored for viewing at any time. Setanta Sports is available in traditional linear format.

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96 The unaudited pro-forma results show that for the full year ended 31 December 2006, the total merged business would have had revenue of £4.2 billion.
97 Ofcom, The Communications Market 2006, 10 August 2006, Figure 4.76, p247.
98 Many of these customers were acquired through the acquisition of Homechoice, which had been in operation since 2000.
99 Estimates of subscriber numbers from Figure 1 and Footnote 2 of Ofcom, ‘Digital Progress Report’, 20 June 2007.
103 UK Gold and UK Style are also currently distributed in this way.
In addition, there are a number of players who retail their own channels directly to consumers on the DSat platform, including, for example, Setanta, Zee TV, Sony and Playboy. Setanta supplies sports channels within the UK over DSat, cable, DTT and IPTV platforms. In some cases it retails its channels directly to the consumer. Its channels in the UK are led by three Setanta-branded channels: Setanta Sports One, Setanta Sports Two and Setanta Golf. Setanta said that as at the end of November 2006 they had more than 1 million premium subscribers in the UK and Ireland.

**Market shares**

There are many reasons why market shares may not give a clear indication of the relative strength or market power of competitors in the market. In a differentiated product market, market shares often do not provide a good guide to the strength of different competitors. Furthermore, competitors in this market adopt different business models, and market shares based on one revenue stream alone could provide a misleading indication. However, we find it useful to present several measures which together can provide a useful overview of the main competitors and give a broad indication of their relative strengths in the market.

We therefore sought to gain a view of market shares using shares of viewing and shares by distribution platform. We also set out details of the revenues of the main competitors to provide additional context.

Figure 2 shows viewing shares by platform. These are closely related to revenues from advertising for commercial channels.

**FIGURE 2**

**Audience shares by platform, 2006**

Source: Broadcasters’ Audience Research Board Ltd (BARB) data, CC analysis.

Notes:
1. BBC does not include UKTV channels, which are a joint venture between Virgin Media and BBC Worldwide, the commercial arm of the BBC. BSkyB does not include joint venture channels. Channel 4 includes S4C.
2. The ‘Other’ category includes over 150 reported channels. Within this group, the individual channels with the highest share in all homes are UKTV Gold and Living, with viewing shares of less than 1 per cent each; all other channels have viewing shares of less than 0.5 per cent. The channels owned by Virgin Media have a significant presence within this group, with a viewing share of just under 2 per cent in all homes, which rises to around 4 per cent in cable homes. UKTV channels (co-owned by Virgin Media and BBC Worldwide) have over 3 per cent share in all homes and over 5 per cent in cable and satellite homes.
3. Data is for 2006 and includes all individuals aged 4+.

4.58 These figures show that a relatively small number of broadcasters capture the majority of viewers. There is also significant variability in the importance of the various broadcasters on different platforms, with the old analogue channels winning significantly greater market share in analogue and DTT homes. Overall, however, this measure gives significantly more emphasis to the BBC and to ITV than to players who have a strong pay-TV retail presence, such as BSkyB. This follows from the fact that companies that adopt an FTA strategy with a focus on advertising actively seek to maximize their viewing shares as this in turn will lead to high revenue from advertising. In contrast, pay-TV retailers, such as BSkyB or Virgin Media, seek to maximize various revenue streams including that arising from subscription fees. This may lead them to pursue a strategy that is not aimed at maximizing viewers but nonetheless is profit-maximizing.

4.59 We therefore also considered turnover figures which give a rough indication of the size of a company and do not rely on the specific strategy adopted. We note, however, that it is very difficult to ensure that turnover figures by company compare like with like. For example, both BSkyB and Virgin Media revenue figures include other businesses such as broadband and telephony. According to published company figures, BSkyB is the largest company in terms of turnover. Its revenue was £4.6 billion for the year ended 30 June 2007. The BBC’s group income was £4.2 billion for the year ended 31 March 2007. ITV’s revenue, by comparison, was £2.2 billion for the year ended 31 December 2006. Virgin Media’s revenue was £3.6 billion for the year ended 30 June 2007.\textsuperscript{103} Channel 4 and Five’s revenues were £937 million and £318 million respectively for the year ended 31 December 2006.

4.60 Finally, Figure 3 presents recent figures on the shares of main television sets which are linked to different distribution platforms.

\textsuperscript{103}The unaudited pro-forma results (which show the operations of Virgin Media Holdings, the former Telewest and Virgin Mobile businesses as if the acquisitions had occurred as at the beginning of 2006) give a revenue figure of £4,162 million for the year ended 31 December 2006.
4.61 This data shows that DTT and satellite have broadly comparable platform shares. Both are significantly more important than analogue terrestrial (which is in any case being phased out) and cable (which has limited coverage).

4.62 It is not possible, in our view, to quote definitive market shares from these three very different measures. However, they illustrate that, regardless of the precise measure, both BSkyB and ITV are very significant competitors in the market. The BBC and Virgin Media are, in different ways, the other major competitors.

4.63 We note that the BBC, given its status (see paragraph 4.39), is not necessarily subject to the same incentives as commercial operators which focus on generating revenues and maximizing profits. This does not necessarily reduce its impact in the competitive landscape, but means that it will not necessarily respond to competitive conditions in the same way as others.

Levels of competition absent the acquisition

4.64 Paragraph 4.37 sets out our conclusion that BSkyB and ITV operate within a UK market for all-TV, which includes both pay-TV and FTA services. We recognize, however, that within this market there is significant product differentiation. We looked at the strength of the existing and future constraints on BSkyB in the market for all-TV, assessing the constraint from other pay-TV operators and from the FTA offer in the absence of the acquisition. Following our discussion of the constraint from the FTA offer in general, we discuss the role of each of the major FTA broadcasters within the overall constraint posed by the FTA offer.

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104Free-to-view satellite includes only those customers who only receive free-to-view satellite. IPTV falls in the category ADSL in this chart. Viewing of television-over-the-Internet is not covered. The television sets which receive analogue terrestrial will no longer be able to do so after analogue switch-off.
Pay-TV operators

4.65 Paragraphs 4.48 to 4.54 set out some details of the existing pay-TV operators and their offers. Virgin Media’s offer is the closest to that of BSkyB, both in terms of the range of channels and the type of content offered (including premium sport and movie channels). We note that since the end of February 2007, BSkyB’s basic channels have not been available on cable, and Virgin Media told us that BSkyB’s premium channels, whilst still available on subscription, were inferior in quality to the same channels over DSat, lacking, for example, interactive services, on-demand services or HD programming.

4.66 Virgin Media and BSkyB have recently been engaged in extensive advertising campaigns, comparing their services against one another. This followed BSkyB’s launch of its bundled offer, under the ‘See, Speak, Surf’ banner, which competes with Virgin Media’s ‘quadruple play’. This suggested to us that they actively target one another’s customers. BSkyB monitors market shares and switching destinations on a quarterly basis, as well as carrying out specific evaluation of competition from cable services. BSkyB told us that it was easy for customers to switch between cable and satellite platforms. BSkyB provides ready-made ‘cable switching packs’ on its website. Virgin Media offers standard cancellation letters to customers who wish to switch from BSkyB to Virgin Media. Further details of BSkyB’s analysis of the competition from cable services is set out in Appendix E.

4.67 As set out in paragraphs 4.48 to 4.54, there are an increasing number of alternative pay-TV offers in the market. In addition to Virgin Media, these include BT Vision and Tiscali, both of whom use IPTV technology to offer audiovisual services to consumers (see paragraphs 4.50 to 4.52). Orange is also in the process of rolling out an IPTV service. The LLU network is currently available to [x] per cent of the population and Orange plans to increase this to [x] per cent by 2010. Orange’s internal targets are to reach [x] customers by 2008 and [x] by 2010. There are also additional retailers such as Top Up TV (see paragraph 4.53).

4.68 These retailers currently offer some competitive constraint to the larger pay-TV retailers and this is likely to grow in the future. BSkyB said that IPTV was ‘developing pretty rapidly’. We note that BSkyB surveys its customers regularly to look at likely switchers and switching destinations within the next three months. [x]

4.69 We note that existing levels of subscribers to IPTV services are low and targets are relatively modest. Parties expressed a number of reservations about the growth potential of IPTV in particular. Virgin Media, for example, said that although it could not dismiss competitors such as BT Vision and Tiscali, they were hampered by the current state of technology. It said that it would be ‘a considerable amount of time’ before the technology allowed IPTV pay retailers to compete head to head with other players. ITV cited independent forecasts from ZenithOptimedia, which projected IPTV growth from 0.2 per cent penetration of all homes in 2006 to 1.6 per cent in 2012.

4.70 We also looked at reports by Datamonitor that considered the future of IPTV. One report explained that in other EU countries, IPTV developed sooner (particularly in France) and coverage is increasing. However, while Datamonitor predicted success for the VoD model put forward by BT Vision, it believed that for it to be successful it

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105[x]
107Datamonitor Media and Broadcasting Technology—The evolving broadcasting sector (Review Report).

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would have to compete strongly on price. In a second report, Datamonitor predicted that by 2010 just over 0.9 million households will have taken up IPTV.\footnote{Datamonitor, European and US digital TV, 2006–2012 (Review Report).}

4.71 We found that within pay-TV, services provided over cable and DSat platforms were close competitors. Although services provided over the IPTV platform offer a certain level of competitive constraint with an all-TV market, it is not clear to us that these players will be able to acquire significant market share within the foreseeable future. They are currently constrained in terms of the number of channels and the number of viewers who can be reached simultaneously compared, for example, to the DSat platform, and this was likely to take some time and substantial investments in technology to improve.

4.72 Retailers such as Top Up TV and Setanta also provided a degree of competitive constraint within the all-TV market. Top Up TV offers a narrower service than the one offered by BSkyB and Virgin Media. Setanta, on the other hand, operates primarily as a channel provider although it also retails some content from other providers. The competitive pressure Setanta can exert on BSkyB therefore arises from offering content that is similar to that offered by BSkyB. By reducing the degree of differentiation between BSkyB’s offer and those competing offers which include Setanta’s channels, this may limit BSkyB’s ability to charge higher subscription fees or to reduce the quality of its offer.

FTA broadcasters

4.73 In assessing the strength of the competitive constraint posed by the FTA offer on pay-TV, we looked at a range of evidence and submissions, including:

(a) internal BSkyB strategy presentations;

(b) BSkyB’s quarterly ‘Sky Tracker’ reports, which include regular analysis of its customers’ behaviour and preferences;

(c) specific analyses carried out by BSkyB including the effect of DTT availability on its own subscriptions;

(d) pricing and innovation in response to competition;

(e) BSkyB subscriber numbers and package prices; and

(f) third party evidence.

We set out our key findings in paragraphs 4.74 to 4.84; further details are set out in Appendix E.

4.74 Internal presentations provided to us by BSkyB assess the competitive challenge from FTA services and explain the ways in which it might be met. It notes that Freeview has benefited from terrestrial broadcasters increasing their programming spend and launching new channels (or moving existing channels from pay to FTA television).

4.75 Another presentation points out that a large majority (around per cent) of the top 150 programmes on multichannel television are on FTA channels in 2006. This presentation and \footnote{Footnote text.}.
4.76 The Sky Tracker reports contain an analysis of the destination of likely switchers from BSkyB (see Figure 1 in Appendix E). FTA services figure [X], with [X] and [X] per cent saying that they were most likely to switch to analogue terrestrial and DTT respectively. In the same document, BSkyB also presents actual switching data. This data shows that on cancelling their BSkyB subscriptions over [X] per cent of customers had moved, at least temporarily, to FTA services (including [X] per cent to Freesat from Sky).

4.77 In 2006/07, BSkyB carried out an econometric study to assess the specific effect of the availability of DTT on the demand for pay-TV services.

4.78 Both parties said that BSkyB had responded to competition through innovation and pricing. Examples included BSkyB’s announcement that it would drop its £10 per month charge for PVRs from July 2007, following the launch of ‘Freeview playback’ digital television recorders; the launch of the ‘Freesat from Sky’ service; and BSkyB’s new package structure introduced in September 2005 which placed a greater emphasis on marketing non-premium channels at lower rates.

4.79 We looked at subscriber numbers and package prices provided to us by BSkyB. Prior to September 2005, [X]. In September 2005 BSkyB changed its offer, introducing a range of basic packages based on genre themes at price points that were significantly lower than that of the Family Pack.

4.80 Although comparisons between the levels of subscription in the two models are difficult, due to changes in the content of the packages as well as the pricing, [X]. The details of BSkyB’s prices, which have been modified twice since September 2005, are set out in Tables 1 and 2 of Appendix E.

4.81 We also attempted to analyse trends in subscriber numbers over a longer time period, to see whether there were clear volume responses to changes in price (see Figure 2 in Appendix E). However, there are many factors that could play a role in influencing these trends, in particular changes in the content of packages, and we did not find it possible to draw a clear conclusion.

4.82 In March 2007 a strategic marketing consultancy, KAE, conducted research on behalf of BSkyB to look at the impact of changing BSkyB’s pricing structure.

4.83 Third party views on the closeness of competition between pay and FTA television varied (see paragraph 4.14). In general, there was agreement that, to the extent that the FTA offer represented a constraint for pay-TV, this constraint tended to operate on the basic offer. Virgin Media said that although it saw the FTA market as a separate market, customers who did not take a premium package would consider a ‘competitive set’ that included Freeview and pay platforms offering pay-TV services that customers could not obtain on a free platform.

4.84 In summary, we found that FTA services pose a constraint to BSkyB’s prices. BSkyB’s business model relies on the ability to persuade consumers to pay for the content available in its packages, rather than opting for freely-available services. Much of BSkyB’s internal research is also consistent with this view.
We looked at the importance of the individual broadcasters within the FTA offer. The BBC is central to the appeal of the FTA offer. As set out in Figure 2, the BBC channels account for between 40 and 50 per cent of viewing in terrestrial homes—a larger share of viewing than any other channel provider. Across all platforms, the BBC's viewing share is around 35 per cent. As set out in paragraph 4.40, it has a number of other interests which allow it to compete with ITV and BSkyB in the all-TV market, including the proposed launch of Freesat, and its role in Freeview. \[\text{[3]}\]

ITV is the second most viewed broadcaster on the DTT platform after the BBC. Although it was not a founding shareholder in DTVSL, it took a 20 per cent stake in October 2005 (as did Channel 4). ITV said that a strong FTA digital offering is of clear commercial benefit to it because its family of channels perform appreciably better in Freeview homes than in BSkyB homes. \[\text{[4]}\] Both parties have said that ITV is important to Freeview, both in terms of content and cross-promotional opportunities, and third parties agreed with this view. ITV also owns one and a half DTT multiplexes and is likely to play a key role in future developments including promoting the development of HD services on FTA platforms (both DTT and Freesat).

Channel 4 channels are also an important contributor to the FTA offer, with a viewing share of around 12 per cent (see Figure 2). \[\text{[5]}\] In the past two years it has chosen to take two of its digital channels FTA, which previously had been available only on a pay basis. \[\text{[6]}\] Five, whilst having a smaller viewing share, also contributes to the success of the FTA offer, both analogue and DTT.

We therefore found that the BBC and ITV are both key to the strength of the FTA offer, with Channel 4 and Five also making a significant contribution.

**Barriers to entry and expansion**

In order to assess barriers to entry, we considered views from parties and independent reports, as well as recent examples of entry. We looked first at barriers to entry and expansion to the production and supply of television channels, before addressing barriers to entry and expansion to the distribution and retail of audiovisual content for television.

BSkyB told us that there were no significant barriers to entry or expansion to the production and supply of television channels (as evidenced by the proliferation of channels in the UK). It noted that the key assets required in order to enter the market were: audiovisual programming, staff with industry knowledge, transmission and distribution facilities, and premises from which to operate.

ITV said that the barriers to entry for a small channel provider were low, noting that it was possible to launch a basic television channel for the UK on digital satellite or cable with less than £10 million a year in running costs. It noted, however, that the costs of expanding to other platforms were higher, citing the high costs of DTT capacity. \[\text{[7]}\] Distribution on DTT would depend on access to a channel slot on a commercial multiplex, and there appears to be little availability over the next few years (see paragraph 4.119).

\[\text{[3]}\]
\[\text{[4]}\]ITV1 secures a more than one-third of the share of commercial television audiences in Freeview homes but only around 20 per cent in BSkyB homes. Likewise, ITV's digital channels achieve a share of around 10 per cent in Freeview homes but only around 5 per cent in BSkyB homes.
\[\text{[5]}\]Channel 4 made E4 FTA in May 2005 and Film4 in July 2006.
\[\text{[6]}\]Full national reach through analogue terrestrial is impossible for a new entrant.
4.92 ITV also suggested that there were barriers to new entrants securing significant viewing shares. It said that ‘given the position of established incumbents with strong brands and high programming budgets, the required level of investment is likely to be high’. ITV said that the main FTA broadcasters had large programming budgets. These channels also spend significant sums on marketing (in 2006, for example, Channel 4 spent £45 million marketing its channels.\(^{117}\)) However, ITV noted that pay channels can be profitable with relatively small audiences.

4.93 This suggested to us that, whilst it might be relatively straightforward to set up a new television channel, acquiring or producing quality content that would be sufficiently attractive to capture a significant share of viewing would require high levels of investment. Hence, in our view, barriers to entry as a channel provider may be relatively low but barriers to expansion would be high.

4.94 In terms of the barriers to entry or expansion as a pay-TV retailer, BSkyB told us that a pay-TV retailer would need to secure content, subscriber management systems, and the ability to distribute content to end-users on a secure basis. The costs of these would vary according to a number of factors, including the type and range of content involved, whether the retailer intends to offer its own or third party channels/VoD services, and the delivery platform the retailer intends to use.

4.95 ITV told us that the barriers to entry for establishing new audiovisual distribution platforms in the UK were very high. It considered that the most significant costs were associated with infrastructure build-out and access to necessary capacity (in the case of DTT spectrum and LLU exchanges). Other costs were associated with accessing appealing content and channels to drive usage. ITV also considered that the position of incumbents, including economies of scale and scope, would put any new entrant at a disadvantage.

4.96 We note several cases of recent entry by pay-TV retailers. This includes players who use IPTV, DTT and a mixture of the two. Entry by IPTV retailers using LLU involves substantial investment.\(^{[\star]}\), and Orange told us that it had invested £[\star] million in an LLU network that would reach [\star] per cent of the UK population. In addition, Orange expected to invest a total of £[\star] in proprietary and third party systems for the provision of IPTV services by the end of [\star]. BT Vision told us that [\star]. The Datamonitor reports (see paragraph 4.70) suggest that there are significant barriers to expanding a retail offer using an IPTV platform. IPTV entrants are discussed further in paragraphs 4.67 to 4.69.

4.97 Top Up TV, which provides its pay-TV services over the DTT platform, told us that [\star] we note that the lack of available DTT capacity makes further entry on this platform seem unlikely.

4.98 In summary, our view is that there are relatively low barriers to entry for a television channel provider aiming to reach a small number of subscribers. However, it would be much more difficult for a new channel to acquire or develop quality content and reach large audiences by providing FTA services. We also found that there are significant costs to establishing new platforms on which to launch retail offers. New retailers who take advantage of existing platforms may face lower costs although, for most platforms, capacity is relatively scarce. Overall, we did not find that entry or expansion would be likely to constrain the parties and hence mitigate BSkyB’s incentive to influence ITV’s strategy.

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\(^{117}\)Channel 4 Annual Report 2006.
**Impact of the acquisition**

4.99 We start by assessing the impact of the acquisition on current competition. We then look at the impact on possible future competition.

**Current competition**

4.100 Paragraphs 3.66 and 3.67 set out our view that BSkyB has the ability materially to influence ITV’s policy. We found that ITV’s financial position is such that in order to raise substantial funding for a major strategic move, it would be likely to need equity funding (see paragraph 3.43).

4.101 We considered whether circumstances were likely to arise in the foreseeable future in which ITV would need to raise such funding. ITV's strategy update, published on 12 September 2007, focuses on a three- to five-year plan for content-led growth funded through gains in efficiency and the disposal of remaining non-core assets. [\textcircled{1}] Given the dynamic environment in which ITV operates, we found it likely that the board would need to make major investments over the next two to three years. A non-pre-emptive rights issue would be the only feasible or efficient funding mechanism for some investments. However, in order to pursue this route the board would have to be confident that it could secure a special resolution approving the waiver of pre-emption rights. BSkyB’s ability to block a special resolution would limit ITV’s ability to raise funds, ruling out some strategic options and affecting its ability to compete in the market for all-TV.

4.102 [\textcircled{1}] We considered BSkyB’s incentive to exercise material influence over ITV’s policy. Our assessment of competitive constraints absent the acquisition (see paragraphs 4.64 to 4.88) shows that, given the competitive constraint of the FTA offer on BSkyB’s services, and the importance of ITV within the FTA offer, BSkyB would have the incentive to influence ITV’s strategy in such a way as to minimize the constraint it offered to BSkyB. We therefore thought it likely that BSkyB would exercise its ability to influence ITV’s strategy so as substantially to lessen competition. In paragraphs 4.106 to 4.118 we set out a number of examples of the ways in which, in practice, this might occur.

4.103 In response to our provisional findings BSkyB said that, with respect to each of the examples given, we could not establish that an SLC was more likely than not to arise. We did not, however, consider it necessary to establish that any particular example was more likely than not to arise in order to form an expectation that BSkyB would be likely to exercise its ability to influence ITV’s strategy.

4.104 BSkyB also said that there had been several ITV strategic initiatives towards the end of 2007 for which no shareholder approval was required and in relation to which ITV had not sought to consult BSkyB. These included the PSB’s Memorandum of Understanding (MoU: see paragraph 4.112), the announcement by ITV, BBC and Channel 4 of their joint on-demand service, and ITV’s announcement of its acquisition of the television production company 12 Yard. However, we did not think that these were examples of strategic initiatives that we would expect to require shareholder approval.

4.105 We considered several examples of ways in which BSkyB might seek to exercise its influence over ITV’s strategy. First, it could seek to influence ITV’s strategy in relation to content production and commissioning. Ofcom research suggests that viewers regard content as the most important aspect of retail television services. Individual
consumers have specific content preferences, but with no significant differences in the nature of these preferences across platforms. We understand that both broadcasters and viewers regard content quality as a key differentiator. ITV’s strategy, which it announced to the market on 12 September 2007, outlined a content-led plan to restore growth to the business funded by enhanced efficiencies and disposals of non-core assets. [38].

4.107 ITV said that the present board and management were committed to a high level of investment in the schedule (around £1 billion a year). However, ITV said that its decision to invest heavily in content could be contested by its shareholders. In the past, in the context of falling advertising revenues, the argument had been put to its shareholders that the ITV1 budget should be reduced, in particular by relying on more acquired programming and less original content. BSkyB could credibly present a case against increased investment in programming, which might gain support from other shareholders. In general, given its interests as a competitor, and despite its interests as a shareholder, we believe that BSkyB would have the incentive to reduce ITV’s investment in content in order to reduce the competitive constraint of FTA on BSkyB. [39]

4.108 Further, ITV could seek to acquire additional rights to existing content in order to improve the quality of its offer. Certain rights, in particular the rights to major sports events, involve significant investments on the part of bidders. At the last auction of live Premier League football rights, for example, the highest winning bid for a single package was £[40] and only one of the six packages sold for [40]. We note that [40] If ITV sought to raise additional finance to support such an acquisition, either alone or as part of a joint bid, BSkyB would have an incentive to seek to disrupt this.

4.109 We received submissions, both before and after publication of our provisional findings, suggesting that BSkyB’s influence over ITV would extend beyond the ability to prevent ITV from raising the necessary funds to acquire such sports’ rights. In particular, some parties argued that third parties might be deterred from joint bidding with ITV because of a fear that sensitive information would be passed to BSkyB, or that BSkyB and ITV might bid together more frequently, preventing others from bidding jointly with ITV.

4.110 We thought that concerns about the passing of sensitive information to BSkyB would require BSkyB to have influence over the day-to-day operation of ITV. Given the level of BSkyB’s shareholding, we did not find this to be the case. We were not persuaded, more generally, that the acquisition significantly altered the ability or incentives of BSkyB and ITV to bid jointly with one another. On balance, while we believe that joint bidding between ITV and other firms may reduce as a result of the acquisition, we found that the main way in which BSkyB could affect ITV’s strategy was through BSkyB’s ability to prevent ITV from raising funds. Further details on sports rights are set out in Appendix F.

4.111 Second, BSkyB could seek to influence investment by ITV in HDTV or in other services requiring additional spectrum. ITV said that it had an increasing sense of the likely future importance of HD, reinforced by BSkyB’s proposed launch of pay-TV channels on DTT (Picnic). Third parties told us that many consumers who had

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118 This was set out in ITV’s strategy presentation of 12 September 2007.
119 [38]
120 [39]
purchased television sets equipped to provide an HD picture\textsuperscript{121} would expect HDTV to be available across different platforms, including the FTA offers.

4.112 As set out in paragraph 2.6, Ofcom has announced a market-led allocation of spectrum capacity release after analogue television signals are switched off. This could lead to a wide range of bidders looking to use the spectrum in a variety of different ways. Ofcom is also currently consulting more specifically on its proposals to upgrade the DTT platform over the next few years by introducing new technologies that will increase the capacity available and allow up to four HDTV channels on the DTT platform. It proposed that it would use a comparative selection process to allocate this capacity, limited to the PSBs. On 20 November 2007, the BBC, ITV, Channel 4 and Five signed a non-binding MoU that, if agreed, would allow them to deliver one HD channel each on Freeview by the projected completion of digital switchover in 2012.\textsuperscript{122}

4.113 ITV told us that, if this technical solution and the MoU progress as envisaged, it would have sufficient spectrum to launch a single HD channel. Nevertheless, this did not rule out the participation of [\textsuperscript{123}] broadcasters in any auction to allow them to broadcast more of their channels in HD format or to obtain spectrum for other purposes. ITV said that there was a [\textsuperscript{124}]. It may wish to be able to broadcast its other channels (particularly ITV2) in HD format. [\textsuperscript{125}]. We understood that the FTA broadcasters would need to invest significantly to obtain additional spectrum in any auction.

4.114 BSkyB said that ITV would have limited means of making a return on investments in HD. The investment costs would be substantial, relating in particular to the costs of acquiring additional spectrum. BSkyB said that although there would potentially be a limited, non-financial return in terms of elements such as brand reputation, offering an HD service would not enable ITV to earn more advertising revenue.\textsuperscript{123} BSkyB said that, given ITV’s inability to earn additional revenue from HD services, and the arrangements that were being put in place by Ofcom to enable ITV to launch a single HD channel it was, in its view, improbable that ITV would seek to raise additional capital to purchase DTT spectrum in an Ofcom auction. BSkyB told us that it would be irrational for ITV to bid a substantial amount for HD spectrum and that, as a shareholder, it would be extremely concerned if ITV intended to do so.

4.115 BSkyB also said that its DSat platform was well placed to offer HDTV services. It had sought to encourage investment in HD services by a range of FTA and pay-TV content providers in order to build demand for HDTV. For example, BSkyB said that [\textsuperscript{126}]. It therefore said that it would not be in its interest to discourage ITV in developing HDTV services.

4.116 We accept that BSkyB has an incentive to encourage the development of HDTV content, and would therefore be unlikely to discourage investment by ITV in HDTV content. However, there is a distinction between investment by ITV in HDTV content, and the availability of that content FTA. In our view, DSat’s advantages in transmitting HDTV are likely to increase as the availability of HDTV content increases, given DSat’s significant capacity advantages. Any increase in spectrum devoted to HDTV services on the DTT platform would be likely to reduce BSkyB’s competitive advantage over FTA services. We therefore thought that, although

\textsuperscript{121}ITV said that sales of HD-ready televisions already numbered more than 4 million.  
\textsuperscript{122}Ofcom notes that the PSBs’ proposal is based on using the capacity freed up by the Ofcom upgrade proposals and therefore assumes that Ofcom will not proceed with its comparative selection process.  
\textsuperscript{123}BSkyB said that, on 28 November 2007, ITV’s Executive Chairman told the House of Lords Select Committee on Communications that ‘‘if we were required to bid for HD spectrum we have no ability, unlike telephony operators and so on, to pass the costs of that on to the customers…and we cannot pass it on to the advertisers…’’
BSkyB would have the incentive to encourage the development of HDTV content, it would also have the incentive to seek to use its expertise and experience to influence ITV’s other shareholders in relation to any attempt by ITV to raise funds to participate in any auction for additional spectrum. In our view, Ofcom’s proposals to upgrade the DTT platform did not rule out ITV’s participation in any auction.\textsuperscript{124}

4.117 There are other areas which may not require significant investment but which BSkyB may, nevertheless, be in a position to influence through its 17.9 per cent shareholding in ITV. For example, BSkyB could attempt to influence the course of any future transactions involving ITV to weaken the constraint that FTA services would otherwise provide, for example by disrupting an acquisition of ITV that might otherwise strengthen ITV’s competitive position,\textsuperscript{125} or by attempting to encourage the acquisition of ITV by another buyer who might act in BSkyB’s interests, for example by \[\text{[\text{[\text{x}}\text{]}}\]. With regard to the first of these examples, \[\text{[[\text{x}]}\] certain acquisitions would create a stronger threat from ITV: \[\text{[[\text{x}]}\] . The second scenario would cause substantial disruption to ITV’s current business model, and would be likely to weaken its contribution to the appeal of FTA services. \[\text{[[\text{x}]}\] \textsuperscript{126}

4.118 Another example in which BSkyB might be able to leverage its direct influence to disrupt ITV’s strategy is in relation to Freesat. ITV is currently involved in the planned launch of the Freesat service with the BBC. Satellite is currently the only platform which allows HD broadcasting with national coverage. Since BSkyB is currently the most significant retailer able to offer HD channels, it would have an incentive to disrupt this development. However, it was not clear to us whether BSkyB would have the ability to disrupt ITV’s strategy in this area.

4.119 As the owner of SDN and co-owner of Digital 3 & 4 (both multiplex licence holders), ITV controls a significant portion of DTT capacity. Access to this platform is regulated, although some concern has been expressed to us as to whether current regulation sufficiently enables competition and non-discriminatory access to capacity. However, BSkyB would not have a direct influence over the allocation of this capacity, and there appears to be little spare capacity to be made available over the next few years.\textsuperscript{127}

4.120 We conclude that, as a result of the acquisition, there is likely to be a loss of rivalry between ITV and BSkyB in the all-TV market. This might arise in a number of ways, and several examples are set out in paragraphs 4.106 to 4.118. Given the importance of ITV for the FTA offer as a whole, we did not think that other FTA competitors would be able to improve their offers to compensate for such a loss of rivalry.

4.121 We therefore conclude that there is likely to be an SLC in the all-TV market. This may be expected to result in a reduction in the quality of the offer, a reduction in innovation, or an increase in the price of audiovisual services in the all-TV market, compared with the levels that there would otherwise have been absent the acquisition.

\textsuperscript{124} ITV’s strategy announcement on 12 September 2007 says that ITV intends to be ‘at the forefront of the HD revolution for our viewers and advertisers.’
\textsuperscript{125} We noted in paragraphs 3.56 and 3.57 that an agreed takeover might form part of ITV’s strategy. BSkyB could influence a resolution to approve a scheme of arrangement to acquire ITV.
\textsuperscript{126} We note that in its strategy announcement of 12 September 2007, ITV said that SDN was an attractive asset which continued to deliver fast-growing, high-margin revenues. However, it would regularly review the strategic benefits of holding this asset versus the value to ITV of selling it to invest elsewhere.
Future competition

4.122 We also considered the likelihood that ITV might provide pay-TV services in the foreseeable future in order to assess the possible impact of the acquisition on pay-TV services. Since pay-TV offers are, in general, a closer substitute to BSkyB than FTA offers, the acquisition would have an adverse impact if it reduced the likelihood of ITV providing pay-TV services. We looked at three possible scenarios:

(a) ITV could be acquired by a third party with a presence in pay-TV, thus strengthening that retailer’s pay-TV offer. For example, ITV might be acquired by Virgin Media. In this scenario ITV could be thought of as a vehicle for entry or expansion.

(b) ITV could expand its offer to include the wholesale provision of pay-TV channels. This strategy could be carried out alone or in conjunction with another party.

(c) ITV could enter as a pay-TV retailer. This could occur through the acquisition of a third party, [\textcircled{C}]. We examine each of these in turn.

- **ITV as a vehicle for entry or expansion by another pay-TV retailer**

4.123 We looked in particular at the evidence provided by Virgin Media about ITV as a vehicle for expansion in pay-TV. In its internal documents, Virgin Media presents its strategic vision of a merger with ITV, [\textcircled{C}].

4.124 [\textcircled{C}]

4.125 [\textcircled{C}]

4.126 [\textcircled{C}]

4.127 These documents suggest that Virgin Media seriously considered the implications of a merger with ITV and the synergies it would bring. It is possible that such a merger would have significantly increased competition for pay-TV services. However, whether such a scenario would have resulted in an increase in the overall competitive constraint on BSkyB would depend on the specific policies of the merged entity. For example, it is possible that by positioning some of ITV’s existing channels as subscription channels, the constraint from FTA would have been weakened.

- **ITV as a supplier of subscription channels**

4.128 ITV’s internal documents show that it has, in the past, considered a move into the provision of pay-TV channels. [\textcircled{C}]

4.129 [\textcircled{C}]

\[\text{References}\]

128 [\textcircled{C}]

129 [\textcircled{C}]

130 [\textcircled{C}]

131 [\textcircled{C}]

132 [\textcircled{C}]

133 [\textcircled{C}]

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4.131 ITV has, in the past, supplied digital channels through pay-TV retailers on a subscription basis. This does not necessarily represent an additional constraint to retailers such as BSkyB. However, in certain contexts ITV could begin to threaten BSkyB’s position.  

- *ITV as a pay-TV retailer*

4.135 We have seen evidence that ITV and third parties have considered ways in which ITV’s role in pay-TV could be increased. However, we have not seen any firm evidence that any of these is likely to occur in the foreseeable future. In addition, ITV has told us that while it continues to review its options in pay-TV, it is currently committed to the FTA model. This was supported by its strategy update on 12 September 2007 which emphasized its commitment to the FTA model and did not discuss any strategy for pay-TV. Based on the evidence that we have received, we did not expect ITV to develop a pay-TV offer, or strengthen a competitor’s existing offer. We therefore did not consider it necessary to look at the details of how BSkyB might prevent such developments as a result of the acquisition.

4.136 We conclude that there is unlikely to be an SLC arising from a loss of potential rivalry from a pay-TV offer developed or strengthened by ITV.

*Conclusions on competitive effects*

4.137 We conclude that there is likely to be an SLC arising from a loss of rivalry in the all-TV market between ITV and BSkyB.

*Advertising*

*Market definition*

4.138 ITV and BSkyB overlap in the supply of television advertising. ITV’s sales house sells advertising time on all of its own analogue and digital channels, and on behalf of SMG, Ulster and Channel. BSkyB’s sales house, Sky Media, sells advertising on its own channels, and on behalf of a number of joint-venture and independent channels.

4.139 We examined the market for television advertising in 2003 when we considered the merger between Carlton and Granada to form ITV. In that case we defined a market for television advertising in the UK. Both parties said that the effects of this acquisition could be assessed within the framework of a television advertising...
market, although both also said that competition from Internet advertising was growing strongly.

4.140 We considered whether it was still appropriate to define a market for television advertising in the UK. We noted that ITV was the largest supplier of television advertising and consistently delivered large audiences at peak times. We were told that Channel 4 could offer audiences of the same size, but on a much less regular basis. ITV said that it was possible to achieve the same level of coverage for a campaign without using ITV1. Third parties told us that expenditure with other sales houses was constrained by the possibility of switching to ITV. For example, the IPA told us that ITV would be one of the alternatives for customers who wished to switch expenditure away from Sky Media.

4.141 On the basis of this evidence, we formed the view that the market should be drawn at least as widely as television advertising.

4.142 We considered whether the market should be drawn more widely to encompass other forms of advertising. We were told that Internet advertising was the closest substitute to television advertising, but that it was generally used for different purposes. The IPA told us, for example, that while large FMCG companies advertised extensively on television, they had yet to do so on the Internet. The Internet was more often used for gaining product and pricing information and for making transactions and had not been used successfully to date to build a non-Internet brand in the same way as television.

4.143 ZenithOptimedia forecasts suggested that rapid growth in Internet advertising would be accompanied by a continued real decline in television advertising revenues up to 2010 (along with a decline in most other forms of advertising). ITV said that, in its view, customers were making substitution decisions between media at the margin, and competition from the Internet was now ‘a crucial constraint’ on television advertising. BSkyB also said that competition from Internet advertising was growing strongly. However, we saw no evidence to suggest that the Internet acts as a constraint on the pricing of television advertising currently, nor that it was likely to do so in the foreseeable future, and hence our view was that the market should not be extended beyond television advertising.

4.144 We also looked at the appropriate geographic market definition. The ITV and Sky Media sales houses operate in the UK. The process for selling television advertising in other countries differs and the majority of suppliers operate within the UK. We saw no evidence to suggest that the market is wider than the UK.

4.145 We conclude that the effects of the acquisition can be assessed within a UK market for television advertising.

Underlying factors affecting existing competition

4.146 In order to assess the effects of the acquisition, we looked at existing television advertising market shares and the process by which advertising is sold.

4.147 ITV is the largest supplier of television advertising, with between 42.5 and 47 per cent of the market. Sky Media is the third largest supplier, with a market share of [\(^{138}\)] per cent (including its wholly-owned channels, its joint-venture channels, and

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139 Fast-moving consumer goods.
140 Sky Media has a separate organization operating in Ireland.
The negotiation and sales process for television advertising is complex. The annual negotiation rounds between television sales houses and media buyers start in the autumn and are generally concluded by the end of the calendar year. Media buyers generally negotiate with the sales houses in order of priority, beginning with ITV. They often negotiate ‘umbrella’ deals covering various clients.

Deals often involve a media buyer committing a share of television advertising budget or, in some cases, a particular volume of expenditure. In exchange they are offered a relative price for advertising exposure. This price is often expressed as a discount on the ‘station average price’ (SAP). The SAP is an average price per impact across a channel or set of channels. There are different SAPs for different demographic groups. Some sales houses quote prices relative to the previous year, taking into account changes in the number of impacts and revenue.

The CRR was implemented at the end of 2003 to counteract any adverse effect on competition arising from the merger of Carlton and Granada. We were told that the CRR, while only applying to advertising on ITV1, had worked successfully to date. Third parties told us that ITV’s financial performance was now linked to its ability to deliver audiences, and ITV could no longer ‘more or less set its prices’. ITV said that given its continuing loss of market share, it would not be in a position to raise prices for television advertising above the competitive level even absent the CRR. We note that this will be assessed as part of the review of CRR announced by the OFT to start in January 2008 (see paragraph 2.17). Given the review process that will be undertaken in relation to CRR, we assumed for the purpose of assessing the impact of this acquisition that the CRR mechanism, or something similar to it, would remain in place for the foreseeable future.

Impact of the acquisition

Paragraphs 3.66 and 3.67 set out our conclusion that BSkyB has the ability materially to influence ITV’s policy as a result of its acquisition of a stake in ITV. We consider the specific concerns that have been raised by third parties in relation to BSkyB’s incentives to influence ITV in relation to the market for television advertising in the UK in paragraphs 4.152 to 4.159.

The main concern that was put to us was that the parties might coordinate to raise the price of television advertising. Such coordination could range from the exchange of specific information to a combination of the two sales houses.

Although we found that the acquisition would give BSkyB material influence over ITV, we do not expect the acquisition of a 17.9 per cent stake to lead to operational control or integration and we consider it unlikely that ITV and BSkyB would seek to combine their sales houses. It was not clear to us that the acquisition would materially alter the incentives of the parties to undertake such a move.

We looked at whether some form of coordination might take place between the two sales houses. The parties might, for example, seek to exchange information in order to improve their negotiating positions and increase prices. BSkyB’s prices for

For more details on the structure of the television advertising industry, see Appendix G.

More specifically they are offered a commitment to a particular pricing mechanic, and the final price is calculated ex-post.

One impact represents one viewer who sees a particular advertisement once.
advertising are, on average, lower than those of ITV1 in particular and hence it might be in a position to gain from an increase in price.

4.155 We believe that there would be a disincentive to ITV sharing information with BSkyB, since, given the operation of CRR, it would not stand to gain in terms of price increases over the majority of its advertising revenue (i.e. arising from the sale of advertising on ITV1). BSkyB also said that any explicit coordination between the two sales houses would, in any case, be subject to competition law. The parties also argued that the complexity of the sales process would make any form of tacit coordination difficult.144

4.156 We looked at whether the parties might coordinate to raise prices on other channels. There was no evidence to suggest that the parties would have market power in the sale of ITV’s other digital channels (including ITV2, ITV3 and ITV4) and the channels covered by Sky Media. As set out in paragraph 4.140, advertisers would be likely to switch away from BSkyB in response to an increase in price. This was also likely to be the case for ITV’s other channels (where, for example, only three individual broadcasts since January 2007 have achieved audiences of over 1 million viewers).

4.157 Given the evidence set out in paragraphs 4.153 to 4.156, we reached the view that it was unlikely that the parties would coordinate to raise the price of television advertising.

4.158 Third parties suggested various other ways in which the acquisition might have an adverse effect on the market for television advertising in the UK:

(a) ITV and BSkyB might partition audiences by scheduling programmes aimed at different demographics, allowing them to raise prices;

(b) ITV and BSkyB might bundle sales of channels, particularly if ITV transferred the sales of some of its channels to the Sky Media sales house; and/or

(c) ITV and BSkyB might lower their prices to engage in predatory pricing.

4.159 The partitioning of audiences as set out in (a) would require a high degree of cooperation at a detailed level which we did not consider was likely to arise as a result of the acquisition. With regard to the possible bundling of sales, ITV said that this would be against its commercial interests, since it would involve passing on detailed information about programming and scheduling. In addition, it was not clear to us that the incentives of the parties to undertake such a move have been changed as a result of the acquisition. The CRR was a barrier to predatory pricing, since it committed ITV to offering any terms offered in one year in future years as well, preventing it from recouping any losses. We therefore formed the view that the acquisition was unlikely to lead to any of the adverse effects set out in paragraph 4.158.

Conclusions on competitive effects

4.160 Although third parties have raised a number of concerns in this market, we do not believe that any of the mechanisms outlined could be expected to result in an SLC. The CRR currently prevents ITV from raising prices for sales of advertising on ITV1, and we saw no evidence to suggest that the parties would be able to raise prices for advertising on their other channels. We also found that the nature of the influence

144We note that one of the three conditions for coordination is that the market is sufficiently transparent for deviations from the prevailing behaviour to be clear.
obtained by BSkyB as a result of the acquisition would be unlikely to facilitate the
types of anti-competitive behaviour described by third parties.

4.161 We therefore conclude that the acquisition is unlikely to result in an SLC arising from
a loss of rivalry between ITV and BSkyB in the UK market for television advertising.

**National television news programme supply**

**Market definition**

4.162 The acquisition results in a direct overlap between BSkyB and ITV in the retail
 provision of national television news to viewers and in an indirect overlap, through
ITN, in the wholesale provision of news programming to other channels.\textsuperscript{145}

4.163 We looked at the retail provision of news to viewers. BSkyB and ITV both provide
news programming on some of their channels. BSkyB currently offers its 24-hour Sky
News channel to viewers on DSat, DTT and IPTV platforms.\textsuperscript{146} BSkyB also shows
the morning news programme *Sunrise* on Sky One. ITV has regular news bulletins
on ITV1 and has an obligation as a public service broadcaster to offer 'high-quality
news' and to provide news programming at peak times.\textsuperscript{147}

4.164 While viewers/subscribers value television news provision—and it forms part of the
brand or image of those channels that provide it—we were told that news program-
milling was not a decisive factor in driving the take-up of subscriptions. ITV further
noted that viewing of news programmes represented a small proportion of overall
television viewing for most viewers. We therefore formed the view that television
news was perceived by viewers to be part of the overall range of programmes for which viewers would be prepared
to pay a premium.

4.165 We also looked at the wholesale provision of national news. As well as providing
national news to BSkyB and ITV respectively, Sky News and ITN provide news
programming to other channels, including Channel 4 and Five. As set out in
Appendix B, ITV, Channel 4 and Five have obligations to provide some news
programming as part of their PSB licences. Some commercial radio stations also
take news content from Sky News and IRN (in which ITN owns a stake).

4.166 The PSB regulations would not allow ITV, Channel 4 or Five to substitute other forms
of content for the news service that they provide.\textsuperscript{148} We therefore formed the view
that there was a distinct economic market for the wholesale supply of news
programming to channels with public service obligations to provide news content.
BSkyB provides news only at the national level, and we therefore defined the
geographic market to be UK-wide.

4.167 We conclude that the effects of the acquisition can be assessed within a UK market
for the wholesale provision of television news. We did not identify a separate market
with respect to the retail provision of television news.

\textsuperscript{145} ITV also provides regional news but there is no overlap with BSkyB in this activity.
\textsuperscript{146} Although BSkyB proposes to remove Sky News from the Freeview package (see footnote 29).
\textsuperscript{147} Ofcom set out the terms of reference for its second review of Public Service Broadcasting on 11 September 2007. This
review includes, for example, a review of the PSB obligations in relation to the provision of news.
\textsuperscript{148} Self-supply may also be an option, though we note that Channel 4 would require Ofcom consent to supply its own news
programming.
Underlying factors affecting existing competition

4.168 In order to assess the effects of the acquisition, we looked at the main competitors in television news provision, their respective market shares, and some of the economic characteristics of television news provision.

Main television news providers

4.169 Table 1 summarizes key aspects of the providers of the most widely-watched television news programmes in the UK.

<table>
<thead>
<tr>
<th>Channel provider</th>
<th>News provider</th>
<th>Distribution platforms</th>
<th>Public service obligations?</th>
<th>Main source of funding for channel</th>
</tr>
</thead>
<tbody>
<tr>
<td>BBC</td>
<td>BBC</td>
<td>All platforms</td>
<td>Yes</td>
<td>Licence fee</td>
</tr>
<tr>
<td>ITV</td>
<td>ITN</td>
<td>All platforms</td>
<td>Yes</td>
<td>Advertising</td>
</tr>
<tr>
<td>Channel 4</td>
<td>ITN</td>
<td>All platforms</td>
<td>Yes</td>
<td>Advertising</td>
</tr>
<tr>
<td>Five</td>
<td>Sky News</td>
<td>All platforms</td>
<td>Yes</td>
<td>Advertising</td>
</tr>
<tr>
<td>Sky News</td>
<td>Sky News</td>
<td>DTT, DSat, IPTV</td>
<td>No</td>
<td>Advertising and other revenues</td>
</tr>
</tbody>
</table>

Source: CC.

4.170 In addition to the providers listed in Table 1, a number of other news services are available on digital platforms only (see Appendix H, Table 1). With the exception of S4C2, which provides Welsh news programming, each of these is provided on a purely commercial basis and tends to focus on news events in other countries or, in the case of Bloomberg, on business news.

4.171 We note that competition to supply news programming on a wholesale basis takes place relatively infrequently since long-term contracts are more appropriate to the economics of news provision (see paragraphs 4.173 to 4.177). For example, the contract to supply news to Channel 4 runs from the start of 2006 until the end of 2010; the contract to supply news to Five runs for five years from 2005 and the contract to supply news to ITV has recently been renewed until 2012.

Viewing shares

4.172 Figure 4 shows the shares of national television news viewing of the main channel providers (measured in terms of the total number of hours watched by all viewers). BBC channels account for over 60 per cent of all television news watched in the UK. ITV is the next most widely-viewed channel provider for news, with a viewing share of just over one-quarter. Channel 4, Five and Sky News each have viewing shares of less than 5 per cent. Other channel providers account for only a very small proportion of news viewing. In its advice to the Secretary of State, Ofcom estimated that the combined audience share of the national television news viewing of the other channel providers was no more than 2.5 per cent.
FIGURE 4

National television news consumption by channel provider, 2006

<table>
<thead>
<tr>
<th>Channel provider</th>
<th>Audience share (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>BBC</td>
<td>60</td>
</tr>
<tr>
<td>ITV</td>
<td>20</td>
</tr>
<tr>
<td>Channel 4</td>
<td>10</td>
</tr>
<tr>
<td>Five</td>
<td>5</td>
</tr>
<tr>
<td>BSkyB</td>
<td>5</td>
</tr>
</tbody>
</table>

Note: Estimates relate to viewing shares on main channels only and are based on BARB/TNS Infosys analysis of 2006 viewing data for all individuals generated on Network Plus.

Economic characteristics of television news provision

4.173 We looked at the particular economic characteristics of television news, including the levels and nature of newsgathering costs and levels of profitability.

4.174 A newsgathering organization incurs high costs because of the need to maintain a network of correspondents, able to report on the day’s stories, wherever these may be. Given the fixed nature of some of the costs of newsgathering (and to a lesser extent programme production), suppliers benefit by spreading these fixed costs over a number of television outlets or across different media. Ofcom reported, for example, that ITV estimated the value of shared costs between it and Channel 4 to be worth at least £5 million a year to each company.\(^{149}\) We were also told that newsgathering costs were falling, as the costs of transmitting stories from reporters to the studio reduced and user-generated content increased.

4.175 Several news providers told us that providing original news content was not a profitable activity for channel providers.\(^{150}\) Ofcom found that, based only on an analysis of direct revenue and costs, news provision on ITV and (to a lesser extent) Channel 4 was not a profitable activity.

4.176 However, assessing the profitability of news on a stand-alone basis is not necessarily meaningful. There may, for example, be less tangible benefits to image and brand of providing a high-quality news service, and additional consequences of being a PSB

\(^{149}\) Source: New news: Future news, paragraph 3.33. This figure has not been endorsed by Channel 4.
\(^{150}\) [\(\_\_\_\)]
as well as opportunity costs associated with the provision of peak-time news. Further
details are set out in Appendix H.

4.177 Where channels can draw on newsgathering activities that would already be taking
place, the business case for providing a UK news channel may be more
straightforward. The incremental cost of providing news programmes to the UK
market will be relatively low, and channels may be able to cover it from the
advertising or subscription revenue that they obtain.

Existing levels of competition and impact of the acquisition

4.178 We next look at the existing levels of competition and the impact of the acquisition.
We focus on competition in the wholesale supply of news programming.

4.179 Appendix H sets out the details of the existing levels of competition between ITN and
Sky News to supply news programming to each of ITV, Channel 4 and Five. Sky
News won the Five news contract against ITN in 2004 and unsuccessfully took part
in a consortium to win the ITV news contract in 2001. In both of these cases, Sky
News (either individually or as part of a consortium) was the only significant
competitor to ITN. Channel 4 noted that having alternative news supply options,
including Sky News, placed it in a stronger negotiating position with ITN when it
renewed its contract.

4.180 We asked ITV, Channel 4 and Five which other providers of news they considered
could bid for their news contracts in the future (see Appendix H). ITV and Five
considered that there were other companies which could credibly bid to supply their
news programming in the future. In addition to Sky News, ITV identified a number of
news providers with established UK capabilities currently focused on international
news or print/online journalism (such as Reuters, CNN and the Press Association).
Five noted that entry barriers to news provision were falling and considered that, by
the time its contract was next renewed, it may be possible for a ‘resourceful
independent production company’ to provide news programming to a sufficiently high
standard, in addition to the established news providers.

4.181 Channel 4, on the other hand, said that it considered that only the BBC, Sky News
and ITN currently possessed the infrastructure, personnel and know-how to produce
a television news service of sufficient quality to meet its requirements. The BBC told
us that it was ‘very unlikely’ that it would supply news content to commercial
broadcasters or commercial news providers.

4.182 At present, competition between ITN and Sky News gives significant leverage to
each of the three channel providers that use their services. We note that each of the
main customers of Sky News and ITN has now selected a news provider until at least
2010. Nevertheless, we looked at the possible impact of the acquisition on the
selection of news provider.

4.183 We formed the view that ITV was likely to retain significant leverage over its news
providers, as it has the financial capability to, in effect, sponsor a new entrant. Five
considered that it would have a range of potential suppliers to choose from, when it
next awarded its news contract. Channel 4 was the most concerned, in part because
of its high-quality specification for its news services.

4.184 We considered three potential mechanisms through which competition could be
reduced between Sky News and ITN.
• **Unilateral reduction in competition by Sky News to ITN**

4.185 In principle, the ownership link between BSkyB and ITV might lead Sky News to compete less aggressively with ITN to preserve the value of BSkyB’s indirect investment in ITN. However, we thought this unlikely. BSkyB owns 100 per cent of Sky News—and therefore, although restricted to a 20 per cent stake in any consortium bidding for the ITV contract, would benefit from all gains arising from winning a new contract from ITN—whereas it would incur only a small proportion of any losses incurred by ITN from losing the same contract.\(^{151}\)

• **Weakening ITN as a competitor to Sky News**

4.186 A second broad area of concern is that BSkyB might be able to influence ITV to weaken ITN and hence reduce the competition it offers Sky News. This might arise, for example, through BSkyB influencing ITV away from ITN as its news provider when ITN’s contract with ITV next comes up for renewal in 2012;\(^{152}\) BSkyB influencing ITV to under-invest in ITN, thereby weakening ITN’s ability to compete with BSkyB for future contracts; and/or BSkyB otherwise influencing ITV to weaken ITN, for example by restricting ITN’s rights to the content generated under the ITV contract.

4.187 We note that BSkyB has an incentive for Sky News to win business from ITN, both before and after its acquisition of a 17.9 per cent in ITV. We have seen no evidence that BSkyB sought to exert influence over ITV when ITV extended its contract with ITN in April 2007, although we note that this decision was taken at a time when the acquisition was subject to competition scrutiny.

4.188 In addition, ITV has the clear ability to take steps that could harm ITN as a competitor to BSkyB, both in its capacity as the largest shareholder in ITN and particularly as ITN’s largest customer. Given the high fixed costs of newsgathering and the economies of scope in producing programmes for different clients (see paragraph 4.174), losing the ITV contract, which accounts for a significant proportion of ITN’s turnover,\(^{153}\) could weaken ITN’s ability to bid for other contracts (eg Channel 4 and Five).

4.189 We therefore looked at whether BSkyB has the ability to influence ITV to take steps that would harm ITN as a competitor to Sky News. We set out in paragraph 3.33 our view that BSkyB’s material influence over ITV is likely to relate to matters of strategic importance. This suggests to us that BSkyB is unlikely to have material influence over ITV’s decisions in relation to wholesale news provision.

4.190 In addition, we note that no major wholesale contract will come up for renewal before 2010\(^ {154}\)—and that the ITV contract has been agreed until 2012. This constrains the ability of BSkyB to harm ITN through any material influence it may have over ITV. As a 40 per cent shareholder in ITN, ITV might also be expected to have a strong interest in ITN’s continuing success. As a customer of ITN, ITV also has a financial

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\(^{151}\) BSkyB’s financial stake in ITN might be calculated by multiplying the shareholding of BSkyB in ITV (17.9 per cent) by ITV’s percentage shareholding in ITN (40 per cent).

\(^{152}\) For example, ITN said that it was ‘concerned that in the future BSkyB could influence how the ITV news contract is awarded’.

\(^{153}\) We note that other smaller contracts, not covered by PSB obligations, may come up before 2010. On 13 September 2007, for example, ITN was appointed producer of Setanta Sports News.
interest in ITN winning or retaining other business, if it can benefit from any resulting cost savings. 155, 156

4.191 We conclude that BSkyB has an incentive to seek to encourage ITV to favour Sky News over ITN and that ITV has commercial influence over ITN. However, we do not consider that the acquisition would enable BSkyB materially to influence ITV to take any such steps in the foreseeable future, given, in particular, the size of BSkyB’s stake, the non-strategic nature of wholesale news provision and the fact that no relevant contracts will come up for renewal before 2010.

- Increased likelihood of coordination

4.192 Third parties have also raised the possibility that the acquisition could increase the likelihood of coordination between ITN and Sky News. This might arise through a significant sharing of resources—short of a full acquisition—between ITN and Sky News, reducing the ability of customers to operate a fully competitive tender between ITN and Sky News, or by increasing the likelihood of coordinated bidding between ITN and Sky News.

4.193 Explicit coordination between Sky News and ITN would be subject to scrutiny under Article 81. Our guidelines set out three conditions for assessing tacit coordination, which would not be subject to Article 81:

(a) there must be sufficient transparency in the market to achieve a coordinated outcome;

(b) firms must have clear incentives to coordinate; and

(c) other competitive constraints must be weak. 157

4.194 Prior to the acquisition, the second of these conditions, in particular, does not appear to have been met. The incentives to compete for individual contracts (eg Channel 4) between ITN and Sky News were high. Contracts only came up occasionally; there was a long period in which no retaliation could occur and ITN and Sky News could both benefit from economies of scope with their existing news provision activities by winning contracts. Absent the acquisition, there may have been some incentives for pooling newsgathering resources between Sky News and ITN to reduce overall costs, though this has not happened to any significant extent.

4.195 We considered whether the acquisition was likely to affect any of the above factors:

(a) We do not consider that the acquisition significantly affects the level of transparency between Sky News and ITN. Neither ITV nor ITN will acquire any more information about Sky News as a result of the acquisition. Given the non-strategic nature to ITV of its wholesale news contract and its stake in ITN, it does

155 ITV said that ‘given the high fixed costs involved in news provision … there are clear cost advantages to ITN in seeking to service multiple news contracts across a range of broadcasters and other clients. Such cost advantages may feed through to improved terms for ITN’s existing customers; ITV has therefore encouraged ITN to compete for contracts with Channel 4, Five and others’. 156 We note that, even in the absence of the acquisition, ITV’s interests will not always be aligned with those of ITN, or that ITV will always support ITN over other providers of news programming. A significant proportion of the market value of ITN to its shareholders resides in its contract with ITV. As a customer of ITN, ITV has an incentive to obtain news services from ITN at the lowest possible price and to that end ITV held a competitive tender for its news service in 2001, which enabled it to reduce the cost of the contract. For a discussion of the relationship between ITV and ITN, by a former head of ITN, see ‘And Finally? Not Quite Yet’, Stewart Purvis, British Journalism Review, 6 2004; vol 15: pp15–20.

157 See Merger guidelines, CC2, paragraphs 3.37 to 3.39.
not appear likely that BSkyB will acquire access to additional information about ITN.

(b) The shareholding means that the interests of Sky News and ITN’s owners are slightly more closely aligned than before. However, as noted earlier, BSkyB still has a strong incentive to favour Sky News over ITN, whereas the other shareholders in ITV and in ITN will have different incentives from BSkyB.

(c) The acquisition appears unlikely to weaken other competitive constraints.

Conclusions on competitive effects

4.196 We conclude that the acquisition is unlikely to result in an SLC arising from a loss of rivalry in the wholesale provision of national television news.

Conclusions on the SLC test

4.197 We therefore conclude that BSkyB’s acquisition of a 17.9 per cent stake in ITV is likely to result in an SLC arising from a loss of rivalry between ITV and BSkyB in the all-TV market.

4.198 We conclude that the acquisition is unlikely to result in an SLC arising from:

(a) a loss of potential rivalry from a pay-TV offer developed or strengthened by ITV;

(b) a loss of rivalry in the UK market for television advertising; and/or

(c) a loss of rivalry in the UK market for wholesale provision of national television news.

5. Plurality

5.1 This section of our report sets out our assessment of the issues raised by the admissible public interest consideration, namely the need, in relation to every different audience in the UK or in a particular area or locality of the UK, for there to be a sufficient plurality of persons with control of the media enterprises serving that audience. Under section 47(2)(b) of the Act, we are required to consider, taking account of this public interest consideration, whether the merger operates or may be expected to operate against the public interest. 158

5.2 We start by considering the legal and regulatory framework relevant to the analysis of the effect of the acquisition on plurality and by defining some key terms. We then look at the effects of the acquisition in relation to two audiences: national television news and cross-media news.

158 An ‘admissible public interest consideration’, according to section 47(11) of the Act, means any public interest consideration specified in the Secretary of State’s reference. The DTI’s guidance on media mergers (DTI Guidance) further specifies that the only public interest considerations that the Secretary of State may take into account are those set out in section 58(2C) of the Act.
Framework for plurality assessment

5.3 The media public interest consideration specified by the Secretary of State in the intervention notice dated 26 February 2007 and incorporated in our terms of reference is set out in section 58(2C)(a) of the Act (see paragraph 5.1).

5.4 This is the first inquiry to be referred to us by the Secretary of State under the public interest regime in the Act and therefore the first to consider the public interest consideration specified in section 58(2C)(a) of the Act. In paragraphs 5.5 to 5.35 we discuss a number of relevant key terms and concepts and set out the framework that governs our assessment.

Plurality, sufficiency and media enterprises

5.5 We considered carefully how we should approach the public interest consideration specified by the Secretary of State. We received detailed submissions from a number of parties both before and after publication of our provisional findings. Our analysis takes account of the views that we received.159

5.6 We listened carefully to the views expressed on media plurality by the sectoral regulator, Ofcom. Ofcom’s views on the acquisition were set out in Ofcom’s report to the Secretary of State of 27 April 2007 under section 44A of the Act. We also held two hearings with Ofcom prior to publication of our provisional findings to gain a better understanding of its views. A summary of key points from these hearings is on our website.

5.7 Section 58A of the Act provides for construction of the media public interest considerations specified in section 58(2C). There is no statutory definition of plurality in section 58A or elsewhere in the Act. We took the concept of plurality of persons with control of media enterprises to refer both to the range of and the number of persons with control of media enterprises.

5.8 We also considered the underlying reasons why the plurality of persons with control of media enterprises is the subject of a public interest consideration in section 58 of the Act. In doing so, we took into account evidence relating to the importance of plurality in the media and how it might best be safeguarded.

5.9 We recognized the link between media plurality and the democratic process. This is consistent with the views of Parliament when introducing the plurality provisions as part of the Act. For example, Lord McIntosh of Haringey (Parliamentary Under-Secretary, DCMS) stated that ‘media plurality is important for a healthy and informed democratic society. The underlying principle is that it would be dangerous for any person to control too much of the media because of his or her ability to influence opinions and set the political agenda’.160 Similarly, Lord Puttnam said, in moving the

159 We took into account the dictionary definition of plurality; other legal provisions which refer to plurality; and the existing literature on media plurality. We also considered the following sources of evidence among others: oral evidence and submissions from the main providers of national television news; written evidence from other media groups; contributions from academic and other experts, both at a roundtable hearing and in written submissions; existing academic research (eg Tony Prosser Public Service Broadcasting: A Special Case, Chapter 9 of The Limits of Competition Law: markets and public services, Michele Polo Regulation for pluralism in media markets, Chapter 5 in Paul Seabright and Jürgen von Hagen (eds): The Economic Regulation of Broadcasting Markets: Evolving Technology and Challenges for Policy; Parliamentary debate about plurality as well as the findings of other bodies who have looked at plurality (including Ofcom, the European Commission and the Power Inquiry and the oral evidence given to the ongoing inquiry by the House of Lords Select Committee on Communications inquiry into Media Ownership and the News).

160 Hansard HL Debate, 2 July 2003, c 912–913, quoted in Ofcom, Report for the Secretary of State pursuant to Section 44A of the Enterprise Act 2002 of British Sky Broadcasting Group plc’s acquisition of 17.9% shareholding in ITV plc, 27 April 2007, paragraph 1.7.
amendment which later became section 58, ‘in Committee, in another place, Dr Howells summed it up quite neatly: “our key aim is to ensure that there is a range of competing voices available to citizens so that they are free to form their own opinions.”’

5.10 We concluded that a plurality of control within the media is a matter of public interest because it may affect the range of information and views provided to different audiences. In our provisional findings, we defined plurality in these terms. In response to comments on our provisional findings, we thought it important to draw a distinction between the plurality of persons with control of media enterprises and the implications of that plurality for the range of information and views made available to audiences.

5.11 In considering the range of information and views that might be expressed by media enterprises, we also thought that it was appropriate to distinguish between the range of information and views that are provided across separate independent media groups (‘external plurality’) and the range that are provided within individual media groups (‘internal plurality’).

5.12 We note that the regulation of media enterprises in relation to plurality and impartiality are distinct (see paragraphs 2.12 and 2.13). Impartiality relates to the fair and balanced treatment of differing viewpoints in relation to particular news stories. However, it does not address the relative prominence given to each story. In our view, it is a matter of public interest that decisions about the relative importance of different news stories should be made by a range of independent people and reflect diverse perspectives.

5.13 We note that there is also no statutory guidance as to what constitutes a ‘sufficient plurality of persons’. We examined the explanatory notes to section 375 of CA 2003, and the DTI guidance. We also had in mind Parliament’s intentions behind the plurality provisions (see paragraph 5.9).

5.14 BSkyB argued that the legal threshold for an adverse public interest finding is high and will only be exceeded if the merger gives rise to ‘unacceptable levels of … dominance’ and/or a ‘significant reduction in plurality’. BSkyB drew attention to paragraph 8.8 of the DTI Guidance which states that the Secretary of State will only consider intervening ‘in exceptional circumstances’ where there continue to be media ownership rules (like the ‘20/20’ rule in this case) or where there have been no such rules and the merger ‘may give rise to serious public interest concerns’.

5.15 Whilst recognizing that it would not be sufficient for plurality purposes to rely on a single provider (for example, the BBC), we do not consider it necessary to take a view on precisely how many owners would constitute a ‘sufficient’ level of plurality of persons. Rather, we have looked qualitatively at sufficiency. We have considered sufficiency by reference to the current levels of plurality, having regard to any change

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161 Hansard HL Debate, 5 June 2003, c 1432. Similarly, in opening the debate on the Communications Bill in the House of Lords, Baroness Blackstone explained that one of the main purposes of the legislation was to ‘ensure the existence of a range of media voices, safeguarding the vibrancy of democratic debate’ (Hansard HL Debate, 20 November 2002, c 381).

162 Section 375 of CA 2003 introduced the provisions in section 58 of the Act. The Explanatory Notes state that subsection 58(2C)(a) ‘is concerned primarily with ensuring that ownership of media enterprises is not overly concentrated in the hands of a limited number of persons’.

163 Enterprise Act 2002: Public Interest Intervention in Media Mergers—Guidance on the operation of the public interest merger provisions relating to newspaper and other media mergers, May 2004 (DTI Guidance). The DTI Guidance states in paragraph 7.7 that ‘This broadcasting and cross-media public interest consideration, therefore, is intended to prevent unacceptable levels of media and cross-media dominance and ensure a minimum level of plurality. The DTI Guidance adds further that ‘The Secretary of State will assess whether there is likely to be a significant reduction in plurality in relation to any relevant audience as a result of the merger’.
in plurality that arises as a result of the acquisition. Moreover, in considering the sufficiency of persons with control of media enterprises, we have regard to the implications of the level of control exercised for the range of information and views available. We considered this in relation to both internal and external plurality.

5.16 We also considered the implications of sub-sections 58A(4) and (5) of the Act which provides as follows:

- **Section 58A(4):** ‘Wherever in a merger situation two or more media enterprises serving the same audience cease to be distinct, the number of such enterprises serving that audience shall be assumed to be more immediately before they cease to be distinct than it is afterwards.’

- **Section 58A(5):** ‘… Where two or more media enterprises—

  (a) would fall to be treated as under common ownership or control for the purposes of section 26, or

  (b) are otherwise in the same ownership or under the same control,

  they shall be treated (subject to subsection (4)) as all under the control of only one person.’

5.17 Our conclusion is that the presumption in section 58A(4) is intended to serve primarily as an anti-avoidance provision to ensure appropriate scrutiny of all mergers, ‘including those involving an increase in the levels of control of such media enterprises … even though the number of enterprises may in fact be unchanged.’

We note that the DTI Guidance (at paragraph 7.13) also expresses the view that ‘this means that the Secretary of State can assess whether, as a result of the merger, there will be a sufficient plurality of persons with control of enterprises serving the relevant audience even though the number of enterprises serving that audience may be unchanged’.

5.18 Ofcom, in its advice to the Secretary of State and third parties, including Virgin Media, argued that the effect of section 58A(4) is to create a statutory presumption that there has been a reduction in the number of media enterprises serving an audience and, hence, a reduction in plurality. For example, in response to our provisional findings, Virgin Media said that under section 58A(4), ‘there is deemed to be a greater degree of plurality prior to the creation of the merger situation than after it’.

5.19 In considering these arguments, we thought it significant that the public interest consideration specified in section 58(2C)(a) is plurality of *persons with control* of media enterprises, not plurality in the *number* of media enterprises. Section 58A(4), which is concerned with the *number* of media enterprises, cannot be said expressly to deem that there has been a reduction in plurality of *persons with control*. This suggested to us that the section is not intended to deem a reduction in plurality where section 58(2C)(a) has been specified.

5.20 We were satisfied that section 58A(4) does not deem a reduction in plurality in place of our substantive assessment of the impact of the acquisition. We noted references

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164Explanatory Notes to section 375(2) of CA 2003.
in the debates before Parliament to the need to examine media mergers in an ‘analytical, fact-based way’ and the need for an ‘evidence-based approach’.  

5.21 Moreover, although section 58A(4) may be interpreted as deeming a reduction in the number of media enterprises serving a relevant audience, such a reduction would not necessarily cause a reduction in the range of information and views available to that audience. We therefore thought that the outcome of our assessment of plurality would not depend on which interpretation of section 58A(4) we adopted.

5.22 We also considered the interpretation of section 58A(5). One interpretation put to us was that this section requires that once a media enterprise falls to be treated as under the control of another for the purposes of section 26 of the Act, it must also be treated as under the same ownership as that other person. Under this interpretation, we would need to assume that any degree of control amounted to full control—that is to say a full merger—in undertaking our plurality assessment. Virgin Media argued that section 58A(5) reflects the ‘fragile nature of plurality’, which ‘embodies the principle of an independent view devoid of the possibility of common influence to a common denominator’.

5.23 BSkyB submitted that the CC should not follow this approach but instead consider the actual effects of the level of influence acquired and not proceed on the basis of any legal fiction as respects the nature of control. BSkyB said that this interpretation of the statute was confirmed by the fact that BSkyB is expressly prohibited by law from acquiring full control of ITV as a result of the ‘20/20’ rule. In addition, BSkyB referred to the 20/20 rule as one of several regulatory provisions which, taken together, ensure sufficient plurality.

5.24 In our provisional findings, we thought that the better interpretation of section 58A(5) is that it is applicable not to the merging media enterprises but to other media enterprises serving that audience. We noted that paragraph 7.14 of the DTI’s guidance states:

Where a number of media enterprises would fall to be treated as under common ownership or common control for the purposes of section 26 of the Act, they are treated as being controlled by one person for the purpose of determining whether there is sufficient plurality of control of media enterprises... Apart from the merging media enterprises, when looking across the spectrum to assess who has control of the remaining media enterprises, it is important to be able to look not just at the owners of those entities, but the controllers of those entities to get an accurate picture in relation to plurality in order to carry out the assessment relating to sufficiency of plurality (emphasis added).

5.25 In response to our provisional findings, Virgin Media argued that this interpretation does not pay regard to the literal language of section 58A(5). However, in our view, the word ‘would’ in section 58A(5)(a) means that section 58A(5)(a) cannot easily be applied to two media enterprises which have in fact been treated as under common ownership or control for the purposes of section 26, as in the present case.  

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165Lord Puttnam, Hansard HL Debate, 5 June 2003, c 1432.
166We also noted that section 58A(5)(b) does not appear to apply to the merging parties, as it contemplates a finding of ‘common ownership or control’ on a basis other than those specified in section 26. Paragraph 807 of the Explanatory Notes to the CA 2003 notes that section 58A(5)(b) ‘is intended to cover any situation where the other media players have never been “brought” under common ownership or control at any point’ (italics added). This may suggest that section 58A(5) is, as a whole, concerned with parties other than the merging parties.
5.26 Nevertheless, we recognized that there is an argument that section 58A(5) requires us to treat the merging parties as under the control of only one person. We therefore considered the implications of this alternative interpretation of section 58A(5), under which BSkyB and ITV are deemed following the merger to be under the control of a single person. On this interpretation of sub-section (5) it remains for the CC to assess whether, following the merger, there is sufficient plurality of persons with control of media enterprises serving relevant audiences. In our view, that will depend in part on the extent and nature of any control exercised by BSkyB over ITV, and on the implications of that control for the range of information and views made available to relevant audiences. Even if section 58A(5) requires ITV to be treated as under the control of only one person, we could see nothing in section 58A(5) to suggest that the degree of control exercised by that person should be treated as equivalent to full control or ownership if that is not in fact the case. That is particularly so since section 26 of the Act covers a range of different degrees of control. We therefore conclude that the nature of the assessment we should carry out for the purposes of section 58(2C)(a) does not depend substantially on our interpretation of section 58A(5).

5.27 We also considered the definition of media enterprises. ‘Media enterprises’ are defined under section 58(A)(2) of the Act as enterprises whose business consists in or involves broadcasting. This clearly encompasses the businesses of both the parties. News content providers such as ITN may not in themselves be media enterprises. However, we consider that the parties’ respective news content providers are also relevant to an assessment of plurality, in that ITV serves a television audience for news through ITN and BSkyB serves a television audience for news through its in-house news service, Sky News. We note also that the definition of ‘media enterprise’ under section 58A(2) of the Act includes newspaper enterprises where at least one of the merging parties is involved in broadcasting.

5.28 In its main submission, ITV also queried whether the production of television news ‘should be a central factor in any assessment of plurality’ given that the relevant merger situation relates to ITV rather than ITN. Given ITV’s shareholding in and relationship with ITN, as well as the fact that ITV serves a television audience for news through ITN and BSkyB serves a television audience for news through its in-house news service, Sky News, we believe that it is appropriate to consider ITN in our assessment of the impact of the acquisition on plurality.

5.29 BSkyB argued that ‘it is not appropriate for the Commission to consider News International’s newspaper publishing interests as a relevant consideration’ for the purposes of this analysis on the grounds that neither News Corporation nor any of its subsidiaries has the ability to influence BSkyB’s or ITV’s news content. Moreover, it said that any interpretation which assumed that News International would be able to influence the news content of a company in which BSkyB had a stake of less than 20 per cent would undermine the validity of a regulatory regime approved by Parliament which was specifically designed to deal with the present situation (the 20/20 rule).

167We noted that BSkyB is the single largest shareholder in ITV by a significant margin, and the only shareholder in ITV likely to be treated as having control of the company for the purposes of the Act. To that extent, it does not appear that the ‘deeming’ effect of section 58A(5), as interpreted in this paragraph, is substantially different from the position in fact.

168 See also paragraph 805 of the Explanatory Notes to the CA 2003, which states that section 58A(5) ‘ensures that the authorities can look at the substance of who controls media enterprises when carrying out a plurality assessment’ and paragraph 7.6 of the DTI Guidance which says that ‘it will be necessary to analyse and consider all the relevant circumstances on a case-by-case basis’.

169 Section 44(9) of the Act explains that ‘broadcasting’ consists of services which Ofcom licences under Part 1 or 3 of the Broadcasting Act 1990 or Part 1 or 2 of the Broadcasting Act 1996.
However, our view is that sections 58 and 58A of the Act explicitly provide for such cross-media considerations in the context of the public interest test and that we can and should undertake a cross-media analysis in this case. Whilst the ‘20/20’ media ownership rule was envisaged to be ‘a sufficient check on the power of newspaper proprietors for the public interest to be satisfied’,\(^\text{170}\) the relevant public interest consideration was not disapplied from situations in which the 20/20 rule is applicable. The DTI Guidance expressly notes (at paragraph 8.8) that intervention may be considered necessary in exceptional circumstances even where there are media ownership rules in place as well. Moreover, the fact that the public interest provisions introduced in the CA 2003 sit alongside revised and updated media ownership rules suggests that Parliament intended the public interest test to supplement the regulatory framework provisions.\(^\text{171}\)

**Relevant audiences**

We then looked at the interpretation of ‘relevant audience’. Under section 58A(7) of the Act we have considerable discretion in the definition of an ‘audience’.\(^\text{172}\) We therefore considered how to define the relevant audiences.

The parties overlap in a broad range of content, but news and current affairs are the genres most closely connected with the formation of public opinion about issues of national significance through the communication of a range of information and views. National news is an important genre of programming for both ITV and BSkyB.\(^\text{173}\) Considering all content genres, including current affairs, documentaries and satire, viewers rank news first in terms of ‘societal importance’,\(^\text{174}\) with a majority of the public saying that news helps them feel part of the democratic process.\(^\text{175}\) We also believe that news provision is a reasonable indicator of, and better defined than, a wider range of other content relevant to the formation of public opinion about issues of national significance. We therefore focused on national news and refer to the range of information and views communicated to audiences through the news as the ‘plurality of news’.\(^\text{176}\)

BSkyB said that the relevant audience for television news needs to be considered on a platform-by-platform basis. We do not consider that the Act limits us to analysing television news in this way.

We looked at both national television news and cross-media news (obtained via television, radio, newspapers, magazines and the Internet) and the diversity of audiences for each. We also looked at the diversity of behaviour within audiences—for example, variation in terms of location and socio-economic group. While the parties do not overlap in the provision of regional news, we considered whether the

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\(^\text{170}\)Dr Howells, Minister for Tourism, Film and Broadcasting, House of Commons, 30 January 2003, quoted in Sky Initial Submission at note 127, p58.

\(^\text{171}\)As Baroness Buscombe put it in agreeing with Lord Puttnam’s public interest test proposals: ‘one needs an extra provision to preserve media plurality in some way’—Hansard HL Debate, 5 June 2003, c 1439.

\(^\text{172}\)See also section 58A(6) of the Act and paragraph 7.12 of the DTI Guidance.

\(^\text{173}\)Local and regional news, although an important component of ITV’s programming, is not provided by BSkyB. ITV also provides current affairs programming and has a public service quota for this genre, and Sky News provides some current affairs programming.

\(^\text{174}\)Ofcom, *Annexes to New News, Future News*, 26 June 2007, Figure 2.14, p42.

\(^\text{175}\)Ofcom, *Annexes to New News, Future News*, 26 June 2007, Figure A1.29 (p47) & Figure A1.31 (p49).

\(^\text{176}\)We use the term ‘news’ to mean the provision of information on current national and international events and ideas (and local and regional events and ideas of national interest and/or importance), including material dealing with public policy and political or economic controversy.
acquisition was likely to have a differential effect on news audiences in the regions or
nations of the UK, including Scotland, Wales and Northern Ireland.\textsuperscript{177}

5.35 BSkyB has argued that ‘it is not appropriate for the Commission to consider News
International’s newspaper publishing interests as a relevant consideration’ for the
purposes of this analysis. However, as noted in paragraph 5.27, the definition of a
media enterprise includes references to newspaper enterprises and the Act explicitly
provide for such cross-media considerations in the context of the public interest test.
We note that under section 58A(8) audience can also mean readership. We conclude
that we can and should undertake a cross-media analysis in this case.\textsuperscript{178}

\textit{Regulatory provisions}

5.36 Regulatory change of ownership provisions relevant to the assessment of plurality of
news are set out in paragraph 2.12. Relevant regulatory provisions which serve to
maintain a degree of internal plurality include:

\begin{enumerate}
\item \textit{(a)} ITV licence obligations under section 279(1)(b) CA 2003 which require, inter alia,
ITV to provide news and current affairs programmes that are of ‘high quality’ and
deal with both national and international matters;
\item \textit{(b)} Ofcom’s Broadcasting Code: content rules (which apply both to ITV and BSkyB)
that are designed, inter alia, to ensure due impartiality, due accuracy and
fairness; and
\item \textit{(c)} PSB requirements under section 265 CA 2003, which provide a public service
remit for every Channel 3 licensee for the ‘provision of a range of high quality and
diverse programming’. These requirements help to fulfil an important internal
plurality objective by providing a range of content to cater to different audience
groups. In conjunction with ownership restrictions, they also play a role in
generating external plurality.
\end{enumerate}

5.37 These regulatory obligations are then cascaded into contracts. For example, the ITV/
ITN contract (currently in ‘Heads of Agreement’ form) commits ITN to ‘supply high
quality national and international news to the regional Channel 3 licence holders in
compliance with their legal and regulatory obligations’.\textsuperscript{179}

5.38 BSkyB said that, in its view, the existing regulatory framework ensured sufficient
plurality. Section 2 and Appendix B set out the overall regulatory framework.
However, we believe that there is a difference between the Broadcasting Code which
is designed to ensure impartiality in terms of news presentation and the statutory
need for there to be a sufficient plurality of persons with control of media enterprises.
We found that the regulatory framework, while relevant to the plurality of news and,
hence, the statutory public interest assessment, does not on its own ensure a
sufficiency of plurality of news.

\textsuperscript{177}We note that the Channel 3 licences for Scotland, Northern Ireland and the Channel Islands are independently owned, with
ITV having a 16.9 per cent shareholding in SMG plc, the holder of the two Channel 3 licences in Scotland.
\textsuperscript{178}BSkyB submitted that the DTI Guidance appears to suggest that section 58A(2) applies only to circumstances where a
relevant merger situation involves both broadcast media enterprise and a newspaper enterprise. BSkyB submitted that this is
not the case here because the merger referred was the ceasing to be distinct of BSkyB and ITV. However, we did not think that
section 58A(2) is limited in the way suggested.
\textsuperscript{179}ITV main submission on the public interest test, paragraph 5.7.
Existing levels of plurality of news

5.39 We looked at:

(a) the existing levels of plurality for national television and cross-media news audiences absent the acquisition, including the number of independent providers, shares of supply and plurality of output (indicators of plurality of news);

(b) the contribution of BSkyB, ITV and related companies to existing levels of plurality of news, leaving aside any influence that BSkyB might exert over ITV; and

(c) the degree of internal plurality, in particular the degree of editorial independence enjoyed by outlets under common ownership.

Plurality of news

5.40 An Ofcom survey indicates that television is the main platform used for news for around two-thirds of adults (see Figure 1, Appendix I), although individuals use an average of 3.8 news platforms.\(^{180}\) Television is also the most trusted platform for news, with around three times as many adults considering its output impartial as compared to newspapers, magazines and the Internet (see Figure 2, Appendix I). This may, in part, reflect the impartiality regulations that govern television news provision (see paragraph 2.13).

5.41 We note that individuals may also interact socially with people who access a different range of news sources to them.\(^{181}\) Some sources of news can have a strong influence on the overall news agenda and thus public opinion, despite much smaller audience shares than some television news bulletins.

5.42 We looked at how news provided through media other than television and newspapers was likely to influence the plurality of news. Since 2003, the number of outlets providing news content (eg over the Internet) has grown rapidly. Our preliminary view, however, is that the development of alternative media is unlikely to reduce the significance of traditional media in terms of plurality for the foreseeable future.

5.43 The expansion of Internet sources of news has significantly affected the provision of news content in recent years. These include dedicated news websites owned by traditional media outlets and news content suppliers, news ‘aggregators’, blogs, and ‘feeds’ of pre-requested types of news story.\(^{182}\) Figure 1 in Appendix I shows a three-fold increase in the number of people who consider the Internet to be their main source of news between 2002 and 2006 (increasing from 2 to 6 per cent). Figure 4 in Appendix I shows that around one-fifth of the population visits news sites on the Internet, compared with over 60 per cent who actively watch television news.

5.44 However, despite the rapid growth in this source of news, the public still makes more use of the ‘pre-selected’ news agenda provided by traditional media sources (see

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\(^{181}\) Ofcom, Report to the Secretary of State, 27 April 2007, paragraph 3.15. Because of this social interaction, and the ability for viewers to switch between television platforms, we do not propose to look specifically at television news audiences by separate distribution platform (eg analogue terrestrial, cable, DSat, DTT).

\(^{182}\) News aggregators, such as Google News, do not have their own newsgathering operation but instead provide links to news content from other sources (such as news agencies like Reuters). Blogs are websites consisting of regular postings by an author and often comment and reaction by readers. ‘Feeds’ include RSS and regular emails (perhaps picked up by mobile phone).
Figures 1 and 2 in Appendix I). We consider that for the time being and for the foreseeable future, online sources of news are more likely to complement than to replace television and other traditional news platforms.\textsuperscript{183} We also note that online news is still largely provided by existing media players. Of the top ten news websites measured by time spent by a visitor, seven are connected with established media outlets such as the BBC (see Figure 3 in Appendix I).\textsuperscript{184}

5.45 We noted the following indicators of the existing plurality of news:

(a) While television news programming is available on a range of channels, the five main channel providers (BBC, ITV, BSkyB, Channel 4 and Five) account for at least 97.5 per cent of total television news viewing. The BBC is by some margin the most widely viewed channel provider for news, followed by ITV.

(b) Television news programme supply is more concentrated still. There are three main providers of news programming, BBC, ITN and Sky News, providing news programming to all of the five main channel providers.

(c) Looking across media, television is most likely to be regarded by people as their main source of news, with newspapers and radio considered to be the next most important sources. While the Internet is growing rapidly, people still largely rely on traditional sources of news and traditional news providers.

(d) Content analysis of television news reveals less diversity than a simple tally of news providers might suggest. Recent research by Ofcom into the actual diversity of news content available to the public (on BBC1, ITV, Channel 4 and Five) found that key stories tended to be treated with a similar degree of prominence by all channels.\textsuperscript{185} Moreover, news stories often shared a limited range of ultimate sources (such as other broadcasters, newspapers or news agencies): ‘news outlets of all kinds often tell the same stories, from the same perspective, using much the same material’.\textsuperscript{186}

\textit{Contribution of BSkyB and ITV to existing plurality of news}

5.46 We looked at the contribution of BSkyB, ITV and related companies to the existing plurality of news.

5.47 ITV is the second most watched channel operator in terms of news after the BBC. BSkyB is one of the five main channel providers for television news. Between them, ITV and BSkyB account for around 30 per cent of television news viewing (see Figure 4).

5.48 Looking at cross-media audiences, BSkyB’s largest shareholder and ultimate parent company, News Corporation (with a 39.1 per cent stake), owns News International, which is the largest provider of national newspapers in the UK (its newspapers The Times, The Sunday Times, News of the World and The Sun have a combined

\begin{flushleft}
\textsuperscript{183}According to Ofcom research, ‘active news consumers in particular are employing more and more internet resources to find out about things that interest them, although they tend to use them in addition to traditional sources of news—especially television—rather than instead of them’. Ofcom, \textit{New News, Future News}, 26 June 2007, paragraph 1.36.

\textsuperscript{184}Six of the top ten news websites are connected with established media outlets when measured by unique visitors to a website, rather than average time spent.

\textsuperscript{185}Ofcom, \textit{Annexes to New News, Future News} 26 June 2007, Annex 3 ‘Content Analysis’.

\end{flushleft}
35.9 per cent national share of circulation). BSkyB and ITV (indirectly via ITN’s stake in IRN) also have interests in the supply of news content to radio news providers.\footnote{Moreover, Ofcom recently awarded ten digital radio licences to 4 Digital Group, led by Channel 4 and including BSkyB.}

5.49 We noted that some specific groups are more likely than others to take their news content from ITV, BSkyB and News International newspapers. For example, the C2DE socio-economic group,\footnote{C2DEs make up about half of the total population.} compared with the UK population as a whole, consumes more of the national news provided by ITV and by News International. ITV has 29.9 per cent of the C2DE audience, compared with 25.8 per cent of all individuals,\footnote{Ofcom Report to the Secretary of State, 27 April 2007, paragraph 4.14.} and News International newspapers have a readership share of 43.6 per cent for the C2DE socio-economic group, compared with 36.2 per cent for all adults.\footnote{Ofcom Report to the Secretary of State, 27 April 2007, paragraph 4.18.}

5.50 We investigated the extent of such differences further using data from TGI and Touchpoints. The results of this analysis are set out in Appendix I. Our view is that, whilst viewing shares and readership vary somewhat by socio-economic group, there are no fundamental differences in the significance of ITV, BSkyB and News International to particular sections of the UK population. Nor did we find any fundamental differences in the significance of ITV, BSkyB and News International between nations within the UK.

5.51 We also investigated whether there were particular individuals within the UK population, who currently took news from ITV and BSkyB and/or News International, but from no other source. We found that no more than 1 per cent of the population, and quite possibly less than this, fell into this category (see paragraph 21, Appendix I).

5.52 In summary, we note that ITV is a significant channel provider for television news and that BSkyB, whilst smaller, is still significant. ITV is the most widely-viewed alternative to the BBC, with BSkyB one of three smaller players in news provision (together with Channel 4 and Five). The parties’ links to related companies—in particular, ITV’s links to ITN and BSkyB’s links to News International and News Corporation—further increase the significance of their contribution to the plurality of news.

Internal plurality of news

5.53 We looked at the nature and extent to which media owners are able to influence news content which affects the degree of internal plurality within the media outlets that they own. Paragraphs 5.54 to 5.57 discuss television news; paragraphs 5.58 to 5.60 discuss newspapers.

5.54 In television news, existing regulatory mechanisms—including quality controls (eg in the Broadcasting Code), requirements for impartiality and quotas for television news and current affairs programming—reduce the scope for influence over editorial decisions by owners of television channels which broadcast news.\footnote{For example, the Broadcasting Code stipulates that ‘alternative viewpoints must be adequately represented’.} These may not, however, necessarily prevent owners of television channels from influencing the news agenda by setting the overall strategy for news, the prominence of particular stories or types of news stories within that agenda or through the choice of editorial staff.
5.55 Each of the three channel operators which contract out news programming (ITV, Channel 4 and Five) described a broadly similar relationship between the channel operator and the programme provider. In particular:

(a) The contract between the news provider and the channel owners sets out a detailed specification of the news service to be provided and the commercial terms of provision. This provides a legal framework within which the channel owner and news provider operate.

(b) The channel operator is responsible for 'strategic' editorial decisions including the 'look and feel' of its news programming, tone and high-level story prioritization (e.g. the balance between national and international news). This strategic direction helps differentiate news programming and is generally considered important to the brand image of the channel. A specific individual within the channel operator (e.g. Commissioning Editor or Network Director of News) will be charged with monitoring news provision on the channel and setting this strategic direction.\(^{192}\)

(c) Within the strategic framework provided by the channel operator, the news provider (e.g. ITN, Sky News) is responsible for day-to-day editorial control, such as selecting the stories to be presented on a given bulletin and the way in which they are to be presented.

(d) The channel operator remains ultimately accountable (including to the regulator) for the news that is presented on its channels. The presentation of individual news stories may on some occasions be discussed between the programme provider and the channel operator either before or after transmission.\(^{193}\)

We note that the oral evidence given to the House of Lords Select Committee on Communications inquiry into Media Ownership and the News is consistent with this description.

5.56 The board of the channel provider would only be involved in decisions relating to particularly controversial stories. We were told that it was rarer still for individual shareholders of the channel provider to be involved in relation to the content of news provided over that channel. ITV told us that it was not aware of any occasion on which its shareholders had sought to influence the content of its news programming and that it was not conceivable that a shareholder could successfully influence it as to the content of its news programming.

5.57 BSkyB and the BBC, which both provide news in-house, emphasized the role of their editorial staff in determining the day-to-day content of their programming. BSkyB told us that all editorial decisions regarding the content of BSkyB’s various news services were taken by the Sky News editorial staff. BSkyB board’s role was to consider the competitive strategy and funding of BSkyB’s news content at a high level; it had no role in the day-to-day editorial control of Sky News content on television or online. We received no evidence from third parties to suggest that senior executives at BSkyB or its parent companies exerted influence on the Sky News agenda. Similarly, the BBC told us that the main judgements about news programming were made by the programme and output editors, under the oversight of senior managers within the BBC’s news hierarchy.

\(^{192}\) The channel operator may also be able to exert some influence over the appointment and dismissal of key personnel in the news provider.\(^{195}\)

\(^{193}\) For example, ITN and ITV operate a Pre-Broadcast Protocol, whereby ITN consults ITV (normally the Network Director of News) on controversial matters and stories.
5.58 There are fewer regulatory restrictions on newspapers than on television news and, in particular, newspapers are able and expected to take an explicit editorial position in relation to topical issues. All respondents to our questionnaires told us that day-to-day editorial decisions for newspapers and allied websites were made by editors and journalists, and not by board directors or shareholders. However, boards usually play some role in the appointment of editors, and may also determine the overall political stance in line with the target audience for a particular newspaper title.

5.59 Third parties have identified examples of alleged influence by News Corporation on the editorial decisions of its newspapers. This was raised, for example, in the House of Lords debate on the Communications Bill in 2003. For instance, Lord McIntosh of Haringey said: ‘the noble Lord [Lord Harris, of High Cross] might also like to circle the world and find out why 274 out of 275 editors of Newscorp newspapers came to exactly the same conclusion as their proprietor on the war in Iraq.’ However, other examples were provided of News International newspapers taking different views on major issues (such as in relation to support for particular political parties during the last general election).

5.60 News International said that:

- editors do not take instructions from management or board members or shareholders on editorial matters; their remit is to produce a newspaper which reflects the views and opinions of its readers, to increase the sales of the newspaper, to confirm or challenge accepted wisdoms through columnists and writers and generally to provide as much news, information and entertainment as is possible within agreed budgets.

News International also told us that Mr Rupert Murdoch and the News International Executive Chairman had regular discussions with the Editor of The Sun on a range of editorial matters, from page design to editorial policy, whereas, in relation to The Times and The Sunday Times, the position on news coverage, editorial stance and appointment of editors is governed by the terms of the DTI consent of 27 January 1981 relating to the transfer of these titles to their current ownership.\(^{194}\) We concluded that there was a considerably greater degree of involvement by Mr Rupert Murdoch in relation to The Sun than some other News International newspapers, such as The Times (see Appendix I for submissions from main media groups on editorial influence). It remains to be seen whether this level of involvement continues with the changes in responsibilities announced on 7 December 2007 (see paragraph 2.39).

**Impact of the acquisition on plurality of news**

5.61 Paragraph 5.15 sets out our view that we should undertake a qualitative assessment of the impact of the acquisition on the sufficiency of the plurality of persons with control of media enterprises, taking into account the nature and extent of any control acquired by BSkyB over ITV and the implications of the acquisition for the range of information and views made available to audiences for news.

5.62 We looked at the impact of the acquisition on the control of media enterprises serving audiences for news. The acquisition creates a link of control between BSkyB and

\(^{194}\) These arrangements provided for the creation of ‘independent national directors’ (INDs) in the holding company of Times Newspapers Holdings Limited. The articles of association of that holding company include provisions aimed at maintaining the editorial independence of the titles, such as the requirement that the majority of the INDs must consent to the appointment or dismissal of the editor of either newspaper title. In addition, the INDs are the final arbiter in any dispute between an editor and the directors of Times Newspapers Limited.
ITV, and hence between Sky News and ITN (see Section 4). Sky News and ITN are two of the three significant providers of television news programming, together with the BBC. ITN provides news programming to both ITV and Channel 4 and Sky News provides news programming to both BSkyB and Five. Sky News and ITN therefore provide news programming to four of the five channel providers with significant audience shares for television news. The largest shareholder in BSkyB is News International, the ultimate parent company of which is News Corporation. Looking at cross-media audiences, the acquisition also creates a link of control between the second largest channel provider of television news (ITV) and the largest provider of newspapers (News International), again through News Corporation.

5.63 Nevertheless, we noted that the acquisition does not bring ITV and BSkyB under common ownership. Rather, the degree of control which BSkyB exercises over ITV is limited to an ability materially to influence matters of policy. That ability may be treated under the Act as control for the purposes of establishing jurisdiction, but it does not equate in practice to full control or ownership.

5.64 We considered the impact of the acquisition on the plurality of news. We looked at two ways in which influence might be exerted by BSkyB or its parent companies (including News Corporation) over ITV or ITN as a result of the acquisition so as adversely to affect the plurality of news:

(a) Direct editorial influence over ITV news programming could lead to the loss of ITV as an independent provider of national news.

(b) Commercial influence over ITV could have an impact on ITV news programming. This could also be extended to the news provision by ITN of other channels, notably Channel 4.

For the purposes of our analysis, we assumed that News Corporation had material influence over BSkyB.

Editorial influence

5.65 Paragraph 5.55 sets out the influence that ITV has over the strategic direction of its news provision. Third parties said that editorial influence might be exerted through a number of mechanisms—formal or informal. In particular, if staff were simply aware of the views of major shareholders, they might tailor the news appropriately, whether or not they are specifically asked to do so. We received evidence from third parties, including Ofcom, to suggest that such mechanisms could be important in determining the content of television news coverage.\(^\text{195}\)

5.66 We sought evidence of editorial influence that had been exerted in the past. Third parties gave us evidence in particular of Mr Rupert Murdoch’s influence in recent years in the Labour Government and his editorial influence over News Corporation’s newspapers. They also referred, for example, to Harold Evans’ autobiography *Good Times, Bad Times*, Andrew Neil’s memoir *Full Disclosure* and Alistair Campbell’s recently published diaries.\(^\text{196}\) We did not receive evidence of any direct editorial

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\(^\text{195}\)Summary of hearings with Ofcom, paragraphs 20 to 22. In particular, Ofcom said that there was no clearly defined path leading from a significant shareholding in a broadcaster to the content of that broadcaster’s news. But there was a process of influence which could operate through informal communications, corporate and social events and even chance encounters. Those in principle subject to influence included editors and journalists with professional careers which could be expected to span different broadcasting organizations. A person seeking to exert influence could readily exploit informal communications by expressing a strong point of view which could affect decisions.

influence that had been exerted over television news in the UK. We also noted the debate in the USA, relating to the acquisition by News Corporation of the *Wall Street Journal* and the arrangements made to safeguard editorial independence following that acquisition.\(^{197}\)

5.67 We note that both BSkyB and ITV have said that the editorial content of ITV news would be unlikely to be a matter of strategic importance. We received no evidence to suggest that it features as a key policy objective for either company. We note, for example, that ITV’s strategy update on 12 September 2007 made no mention of particular strategic objectives for news (with the exception of statements about a reduction in regional news). Our view that BSkyB’s influence over ITV is likely to relate to matters of strategic importance suggests that BSkyB is unlikely to have the ability to exert material influence over ITV in relation to the editorial content of news.

5.68 In addition, the evidence that we received suggested to us that there was a strong commitment to editorial independence across television news broadcasting which would lead to editors resisting any direct board intervention or intervention from shareholders to set the news agenda. Both ITV and ITN demonstrated a strong commitment to editorial independence. ITV said that ‘it is not conceivable that a shareholder in ITV could successfully influence the editorial decisions of its news programming’. ITN had in the past broadcast news stories that were unfavourable either to the channel on which the news was provided (eg in relation to phone-in quizzes on Channel 4) or to other commercial interests (eg advertisers). We saw no reason why this should not continue.

5.69 We note that there are a number of internal and regulatory constraints in the production of television news which are likely to limit any possible single minority shareholder influence on editorial decisions. In particular:

(a) The final decisions on matters of editorial judgement relating to the coverage of particular stories on ITV news are made by the programme editors at ITN and not by executives at ITV.

(b) ITV is subject to regulation by Ofcom in relation to the impartiality of its news programming (see paragraph 2.13).\(^{198}\)

(c) The reputational risk to ITV and ITN of compromising this impartiality in response to a shareholder’s request would be very substantial.\(^{199}\)

5.70 Given the evidence set out in paragraphs 5.66 to 5.69, we conclude that there is insufficient evidence to suggest that the acquisition of a stake of this nature would give BSkyB or its parent companies the ability or incentive to exert editorial influence over ITV’s news output.

\(^{197}\)See, for example, Steve Stecklow, Aaron O Patrick, Martin Peers and Andrew Higgins, ‘Calling the Shots—In Murdoch’s Career, A Hand on the News,’ *Wall Street Journal*, 5 June 2007.

\(^{198}\)Mr Grade said ‘I would imagine that if a controlling shareholder of ITV tried to influence the news agenda, get stories pulled or stories inserted into news that were favourable to their commercial interests for example, I think ITN would certainly protest publicly and loudly, and might well protest to Ofcom’.

\(^{199}\)Mr Grade said ‘I also think … that Parliament sets a great deal of store by the impartial provision of news alternative to the BBC that ITN provides to the mass audience, to the same audience as the BBC. I think Parliament would be in uproar if there were any attempt to subvert the editorial independence of ITN’.
5.71 We think it likely that ITV is able to exert commercial influence over ITN: both as a shareholder with a 40 per cent stake in ITN, and as ITN’s biggest customer. ITV may also have the ability to influence ITN in relation to its news coverage through other mechanisms, such as employment decisions (eg appointment of editors or senior journalists), or through strategic decisions (eg sourcing of news content). ITV’s main commercial influence over ITN is in its choice of ITN as its provider of national news. We note that ITV and ITN have agreed that ITN should provide ITV with news programming until 2012.

5.72 ITV’s commercial influence over ITN could, in principle, extend beyond ITV’s news output. In particular, if ITN were unable to function as an effective independent supplier of news content in competition with Sky News (for example, if it were to lose the ITV contract), this could reduce the ability of other channels, such as Channel 4, to provide an independent news voice.200

5.73 However, while we thought it likely that BSkyB would have an incentive to favour Sky News over ITN, it is not clear to us that the acquisition would significantly alter BSkyB’s ability to influence ITV to do so. ITV has pointed out that:

Out of a total investment in programming nearing £1 billion, it invests around £[X] in ITN network news. Even with respect to periodic decisions to renew ITN’s contract, ITV would not expect to consult with shareholders (and did not do so with respect to the recent contract negotiations). … Nor would a decision with respect to news programming be subject to shareholder approval or, indeed, the subject of a special resolution (see paragraph 5.67).

5.74 We therefore conclude that the acquisition of a 17.9 per cent stake in ITV does not give BSkyB the ability to exert significant commercial influence over ITV’s news output or more widely over ITN.

Conclusions on plurality

5.75 Given the extent of the influence conferred on BSkyB by its acquisition of a 17.9 per cent shareholding in ITV, we conclude that the regulatory mechanisms, combined with a strong culture of editorial independence within television news production, are likely to be effective in preventing any prejudice to the independence of ITV news. We do not therefore expect BSkyB’s ability materially to influence ITV to have an adverse effect on the plurality of news relative to the position absent the acquisition. We therefore concluded that the acquisition would not materially affect the sufficiency of plurality of persons with control of media enterprises servicing audiences for news.

5.76 We conclude that the acquisition may therefore not be expected to operate against the public interest, having regard only to the specified public interest consideration.

5.77 We arrived at these conclusions based on the evidence available and taking into account the circumstances of this case. We note that each case must be decided on its own facts, and we may in other cases, where there are, for example, different degrees of control, arrive at a different conclusion in relation to the impact of any acquisition on plurality.

200 Channel 4, under section 295(1) of CA 2003, is not permitted to produce its own programmes in-house.
Conclusions on public interest

5.78 Under section 47 of the Act, we are required to consider whether the merger may be expected to result in an SLC and, taking account only of any SLC and the media public interest consideration specified by the Secretary of State, to consider whether the acquisition operates, or may be expected to operate, against the public interest.

5.79 We conclude that BSkyB’s acquisition of a 17.9 per cent stake in ITV may not be expected to operate against the public interest having regard to the media public interest consideration. However, we also conclude that it may be expected to result in an SLC based on our assessment of the competitive effects of the acquisition. In these circumstances, we conclude that, overall, the acquisition may be expected to operate against the public interest.

6. Remedies

6.1 This section of our report discusses possible remedies to the SLC and the consequent adverse effect on the public interest.

6.2 Under section 47(7) of the Act, having decided that the relevant merger situation may be expected to operate against the public interest, we must decide:

(a) whether action should be taken by the Secretary of State under section 55 of the Act for the purpose of remedying, mitigating or preventing any of the effects adverse to the public interest which have resulted from, or may be expected to result from the creation of the relevant merger situation;

(b) whether the CC should recommend the taking of action by others; and

(c) in either case, if action should be taken, what action should be taken and what is to be remedied, mitigated or prevented.

6.3 The Secretary of State might decide to make no finding in connection with the reference. In that case, section 56(6) provides that we should proceed as though the reference had been made under section 22 of the Act. Accordingly, section 47(8) of the Act provides that, if we have decided on a reference under section 45(2) that there is or will be a substantial lessening of competition within any market or markets in the UK for goods and services, we should also decide separately the following questions:

(a) whether action should be taken by the CC under section 41 for the purpose of remedying, mitigating or preventing the SLC concerned or any adverse effect which has resulted from, or may be expected to result from it;

(b) whether the CC should recommend the taking of action by others; and

(c) in either case, if action should be taken, what action should be taken and what is to be remedied, mitigated or prevented.

6.4 Where we have found that a merger may be expected to operate against the public interest on the basis of an SLC, and for the purposes of answering the separate questions under section 47(8) of the Act, we will approach the remedies phase of a
reference under section 45 as we would a reference under sections 22 or 33 of the Act. Accordingly, we are guided by the considerations set out in our guidance.\textsuperscript{201}

6.5 In assessing possible remedies, we first considered the effectiveness of different options in dealing with the SLC and the consequent adverse effects on the public interest. The Act requires us ‘in particular to have regard to the need to achieve as comprehensive a solution as is reasonable and practicable to the substantial lessening of competition and any adverse effects resulting from it’.\textsuperscript{202} Our guidance notes that one-off remedies that change the structure of the market (structural remedies) are likely to be preferable to remedies that impinge upon the behaviour or conduct of firms (behavioural remedies) as they address the effect of the merger directly and will require comparatively little, if any, monitoring or enforcement of compliance.\textsuperscript{203}

6.6 Having identified the effective remedy options (or packages of options), we considered the question of proportionality. When choosing between two equally effective remedies, we must choose the least cost, least intrusive remedy.\textsuperscript{204} However, our guidance states that ‘since the cost of divestment was, in essence, avoidable, the Commission will not, in the absence of exceptional circumstances, accept that the cost of divestment should be considered in the setting of remedies’.\textsuperscript{205}

6.7 In choosing between or designing effective remedies, we will also take account of any Relevant Customer Benefits (see paragraph 6.72).

\textit{The remedy options}

6.8 In the Notice we invited views on three remedy options:

(a) divestiture of the whole of BSkyB’s shareholding in ITV;

(b) divestiture of such part of BSkyB’s shareholding in ITV that it would cease to have material influence over ITV;\textsuperscript{206} and

(c) behavioural remedies to accompany partial divestiture remedies.

6.9 In the Notice we did not propose behavioural remedies alone for discussion as none appeared to be appropriate and effective in addressing the SLC and the consequent adverse effects on the public interest that we had provisionally found. However, we said that we were willing to consider any practical alternative remedies to divestiture that parties considered would remedy the SLC identified and/or the adverse effects. In response to our remedies working paper, BSkyB proposed two further possible remedies:

(a) placing the entirety of BSkyB’s voting rights in ITV in a voting trust; and

\textsuperscript{201}CC2 and CC 8.
\textsuperscript{202}Section 47(9) of the Act; see also CC2 paragraphs 4.4 and 5.8.
\textsuperscript{203}CC2 paragraph 4.15.
\textsuperscript{204}CC2 paragraph 4.9.
\textsuperscript{205}CC2 paragraph 4.10.
\textsuperscript{206}The ultimate purpose of this option (partial divestiture) is to remedy, mitigate or prevent any adverse effect on the public interest and/or the SLC, and not simply to address the material influence we have identified. Having said this, it may be that the SLC can be remedied by removing the possibility of material influence, and this is reflected in paragraph 4.24 of our Guidance CC2. We note, however, that paragraph 4.24 of CC2 relates to an anticipated merger in which the potential acquirer has already acquired a shareholding in the target company. This is a different situation from that being considered here.
6.10 We also invited views on other measures that might be needed to ensure that either a full or partial divestiture of BSkyB’s shareholding in ITV would be effective and that no new competition concerns would arise.

**Effectiveness of remedy options**

6.11 This section of the report discusses the effectiveness of each remedy option in addressing the SLC and the consequent adverse effects on the public interest.

**Full divestiture**

6.12 The full divestiture of BSkyB’s 17.9 per cent shareholding in ITV would remove all possible sources of BSkyB’s influence over ITV, including both its voting rights and its economic interest in ITV. Our guidance states that our starting point will be to choose remedial action that will restore the competition that has been, or is expected to be, lessened as a result of the merger situation.207

6.13 BSkyB said that this remedy would undoubtedly be effective, as it would represent a complete unwinding of BSkyB’s acquisition of the shares in the market. However, it said that it would be disproportionate because lesser remedies would be effective in remedying the SLC identified (see paragraph 6.68).

6.14 ITV told us that full divestiture was the only effective and comprehensive remedy to the SLC identified. Unlike BSkyB, ITV said that our finding of material influence was broadly based on the absolute and relative size of BSkyB’s shareholding; the consequent, likely ability of BSkyB to block special resolutions; and the industry knowledge and standing of BSkyB and its ability to exercise authoritative opposition to the strategy of the ITV board. The magnitude of BSkyB’s shareholding gave it both an important ‘lead role’ among shareholders and credibility among those shareholders. It argued further that BSkyB’s acknowledged industry knowledge and standing gave it a unique degree of influence over other shareholders.

6.15 Virgin Media said that, in addition to the ability to block a special resolution, there was a range of alternative ways in which BSkyB may be expected to influence the strategic commercial behaviour of ITV. In response to our provisional findings, it told us that we had understated the degree to which BSkyB could use its importance and stature as an industry player, together with its position as the largest shareholder, to influence the overall strategy and commercial direction of ITV. It gave examples of activist minority shareholders having had a material impact on the strategy and direction of major companies.208 It argued that full divestiture was the simplest and most clear cut remedy to address the identified SLC and said that this was the only remedy that would restore the competitive status quo ante.

6.16 The OFT told us that, as a general principle, full divestment and the restoration of the status quo ante should be the default position for determining a remedy in completed shareholding acquisitions that created an SLC, since this offered certainty in terms of the effectiveness of a remedy and was in line with international best practice. As a

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207CC2 paragraph 4.23.
208Virgin Media submitted academic research which indicated that active investors, such as Hermes, could have a significant impact on the strategy of companies, with relatively small stakes of less than 10 per cent (Returns to Shareholder Activism, Becht, Franks, Mayer and Rossi, ECGI working paper 138/2006). We noted this research, though we also noted that the position of an active financial investor was somewhat different from an investor, such as BSkyB, who was also a competitor.
result, the starting point for thinking about remedies in this case should be full divestment.

6.17 Other third parties (for example, Channel 4) recommended remedies which fell short of full divestiture. The BBC told us that any of the proposed divestment remedies would address the SLC.

6.18 We found that the full divestiture of BSkyB’s shareholding in ITV would be effective in remedying the SLC and the consequent adverse effects on the public interest as it would restore the situation prior to the acquisition.

Partial divestiture

6.19 We next considered whether partial divestiture of BSkyB’s shareholding in ITV would be effective in addressing the SLC and the consequent adverse effects on the public interest.

6.20 BSkyB said that our reasoning suggested that a relatively small reduction in its shareholding in ITV would enable the ITV directors to be confident that BSkyB could not block a special resolution on a matter of ITV’s competitive strategy. It said that such a reduction could be achieved through ceding voting rights to a voting trust and initially proposed that 3 per cent of its shareholding in ITV should be made subject to such a trust. This would reduce its voting control on the matters to which the trust applied (which might be some or all issues) from 17.9 per cent of ITV’s shares to 14.9 per cent. It subsequently proposed that it could place the entirety of its voting rights into the trust arrangement or, alternatively, undertake not to exercise the entirety of its voting rights. This is discussed further in paragraphs 6.39 to 6.57.

6.21 ITV considered that, although full divestiture was the only effective and comprehensive remedy to the SLC, a divestiture by BSkyB to 4.9 per cent of its shareholding would reduce its concerns. In response to our remedies working paper, it said that a continued shareholding of 7.5 per cent would leave BSkyB as ITV’s second largest shareholder with an economic interest in ITV worth approximately £400 million. This economic interest, together with BSkyB’s likely ability to block a squeeze-out, its influence derived from its industry knowledge and standing, and its ability to act as a disruptive shareholder, would mean that BSkyB, with a shareholding of 7.5 per cent, would retain a significant level of influence over ITV’s strategy.

6.22 Virgin Media said that even at a shareholding of just below 10 per cent there would remain a material risk that BSkyB would continue to be able to exert unwarranted influence over the strategic decisions of ITV. Channel 4 told us that BSkyB should be required to divest a sufficient proportion of its stake in ITV to ensure that it is not able to influence ITV’s strategy through its shareholding. It noted that, prior to the acquisition, Fidelity was ITV’s largest shareholder with a shareholding of 11 per cent. It said that a divestiture by BSkyB down to this level may address the SLC.

6.23 While the OFT’s preferred remedy was complete divestment (see paragraph 6.16), it acknowledged that, in principle, partial divestment might still be acceptable, but that we would need to be confident that it offered an effective remedy. Recognizing that there could be practical difficulties in implementing and monitoring a shareholding

209 See paragraph 3.15.
threshold of zero,\textsuperscript{210} the OFT proposed that we should consider a remedy that would allow BSkyB a ‘de minimis’ shareholding and suggested that a figure of no more than 3 per cent might be acceptable. Such a shareholding would make it unlikely that BSkyB would be the largest shareholder; there would be no company law rights attached to the shareholding; it would be below the threshold for shareholding notifiable under the Stock Exchange Rules; and would be consistent with previous practice.\textsuperscript{211} BSkyB told us that OFT’s reasons for a ‘de minimis’ shareholding were, in its view, unsatisfactory.

6.24 In considering the extent of partial divestiture of shares (if any) that would be effective in remedying the SLC and the consequent adverse effects on the public interest, we considered the level of shareholding at which there would no longer be a realistic prospect that BSkyB could exert material influence and at which the ITV Board could not realistically expect BSkyB to be able to do so. In doing so, we took into account the different elements of material influence that we had identified—both the level of shareholding at which BSkyB alone would be able to block a special resolution and BSkyB’s ability to persuade other shareholders to vote against a special resolution as a result of the size of its shareholding combined with its industry knowledge and standing (see paragraphs 3.39 to 3.67).

6.25 We looked at historical data associated with the five general meetings since the creation of ITV to inform our view of voting turnout and the levels of votes against (see paragraph 3.45). Although historical data provides some guidance in relation to these factors, there is also a degree of uncertainty associated with both. Therefore, assessing the effective level of partial divestiture is not solely a matter of calculation or quantitative analysis, but involves an element of judgement. To inform this judgement, we looked at various different scenarios of the size of BSkyB’s shareholding, the voting turnout and the proportion of ITV’s other shareholders who would vote against (see Annex 4 to Appendix D).

6.26 As set out in paragraph 3.52, we did not form an expectation that the trends noted in the Lintstock Reports (in terms of increasing turnouts and higher turnouts for contentious issues) would give rise to a significant change in voting patterns at ITV compared to the recent past. In considering voting turnout, however, we took into account the prospect that a number of shareholders would abstain from voting on any specific resolution, so that the ‘effective turnout’ on specific resolutions could be less than the proportion of shareholders represented at any given meeting. Overall, turnout has been between 63 and 72 per cent in the previous five general meetings, with between 0 and 7 per cent of votes withheld.

6.27 Drawing on analysis in the fourth Lintstock Report, BSkyB said that we should not be using effective turnout to calculate the potential weight of its stake because the choice to withhold votes by shareholders was a deliberate expression of the shareholders’ dissatisfaction with ITV management. Votes withheld might therefore translate into votes for or against a given resolution.

6.28 Although we recognized that, in some cases, votes may be withheld deliberately to demonstrate dissatisfaction, we did not think it possible to identify such votes with any degree of certainty in practice, other than in exceptional circumstances. In addition, we believed that using effective turnout represents a suitably cautious approach to assessing the effective level of BSkyB’s influence on specific resolutions.

\textsuperscript{210}The OFT said, for example, that pension funds associated with the acquirer may hold shares in the target company as part of a normal investment portfolio and that monitoring compliance in these situations could become difficult and costly.

\textsuperscript{211}The OFT gave the example of the 3 per cent maximum shareholding thresholds set in the undertakings given by Walmart (Asda), Sainsbury’s and Tesco in the Safeway case (see http://www.oft.gov.uk/shared_oft/mergers/undertakings/tesco.pdf). BSkyB said that the OFT’s reference to consistency with previous practice was misguided.
approach to the assessment of voting turnout in the remedies context, given the need for us to be confident about the effectiveness of our remedy. We therefore conclude that it is appropriate to consider effective turnout.

6.29 Having regard to historical voting patterns and likely future voting levels, we thought that the lowest realistic level of effective turnout would be 60 per cent (see Appendix D).\footnote{Based on analysis in the Lintstock Reports and set out in Appendix D, we note that the lowest turnout and the highest proportion of shares withheld were at the same AGM in 2004, the most distant general meeting and the first following the creation of ITV. The minimum effective turnout at that meeting was 56 per cent. However, we noted that this related to an exceptional set of circumstances (surrounding the re-election of those directors who backed a compensation payment for the ex-Chairman of Carlton, Michael Green). We did not think it appropriate that this should drive our conclusions about a realistic level of effective turnout. On all other resolutions that we considered, the effective turnout was over 60 per cent and, in most cases, votes withheld were less than 1 per cent.}

6.30 We also considered the proportion of shareholders who had voted against resolutions proposed by the ITV Board at the previous five general meetings. We found that up to 6 per cent of shareholders had voted against the ITV Board on certain resolutions.

6.31 BSkyB said that we should not make any allowance for the possibility that other shareholders might also vote against the ITV Board, saying that it would be inappropriate to attribute that vote to BSkyB given that BSkyB and the shareholder(s) are not acting in concert. BSkyB also suggested that a higher proportion of investors were willing to vote against resolutions relating to governance than those relating to strategy and day-to-day management. It said that there were no instances in the previous five general meetings of more than 3 per cent of the shareholder base voting against a resolution concerning strategy or day-to-day management.

6.32 We took the view that, in practice, we were seeking to ensure that BSkyB would not be in a position to block a special resolution, either by exercising its own voting rights—with or without a certain percentage of the votes being exercised independently in the same way—or by using its industry expertise and status, combined with its shareholding, to influence other shareholders to vote with BSkyB. We therefore thought it important that we should make a conservative assumption as to the number of shareholders who might be expected to vote against ITV.

6.33 We noted that an assessment of the highest percentage of shareholders that might realistically vote alongside BSkyB against a particular special resolution is, necessarily, a matter of judgement. BSkyB told us that there had not been any examples of contentious strategic resolutions passed at the last five general meetings comparable to the examples that we outlined in paragraphs 4.106 to 4.118. Nevertheless, based on previous experience of the levels of shareholders voting against specific resolutions, and recognizing BSkyB’s ability to influence other shareholders, we thought that the highest realistic percentage of votes against a special resolution (other than those of BSkyB) would be 7.5 per cent.

6.34 We noted that, assuming the lowest realistic effective turnout of 60 per cent and the highest realistic level of votes against at 7.5 per cent, BSkyB would only be able to block a special resolution if it were to retain a shareholding of 7.5 per cent or more (see Appendix D for further details). Given that we regarded these assumptions as at the outer realistic limits, we were satisfied that BSkyB would not be able to block a special resolution, and that the ITV board would not realistically expect it to do so, if BSkyB held a shareholding in ITV of below 7.5 per cent.\footnote{Historically, the lowest effective turnout at ITV general meetings was 56 per cent (at the 2004 AGM) and the lowest number of votes cast against a resolution, as a percentage of total shares, was 6 per cent (at the 2006). Whilst we have already considered that situation, we did not think it appropriate that this should drive our conclusions about a realistic level of effective turnout. On all other resolutions that we considered, the effective turnout was over 60 per cent and, in most cases, votes withheld were less than 1 per cent.} This is not to say that ITV
could never lose a vote on a special resolution which BSkyB chose to vote against, but rather that reducing BSkyB’s shareholding to below 7.5 per cent means that there would be no realistic prospect that BSkyB would be able to exercise material influence over ITV’s strategy.

6.35 It was put to us that BSkyB’s shareholding should be reduced to below the level at which it could effectively block a ‘squeeze out’ in the event of a contested takeover. A ‘squeeze out’ can only be effected once 90 per cent of shareholders have accepted an offer. In any listed company, a proportion of votes (for example, those of the deceased) will be unavailable to a bidder, so in practice a ‘squeeze out’ may be prevented by a shareholder with less than a 10 per cent stake.214

6.36 However, as set out in paragraph 3.56, we did not consider that BSkyB’s ability to block a contested or ‘hostile’ takeover of ITV would give it the ability to affect ITV’s strategy. By definition, such an event would not be part of ITV’s management’s strategy, but rather part of the acquirer’s strategy. In the event of an agreed takeover, the transaction could instead be structured as a scheme of arrangement, in which case a shareholder would need a larger share of votes cast—25 per cent—to block the transaction. Accordingly, we do not place weight on the argument regarding the squeeze out in itself, although we note that a shareholder with a stake large enough to block a squeeze out could enjoy additional credibility with other shareholders.

6.37 It has also been put to us that, even with a very small shareholding, BSkyB would be able to act as a disruptive shareholder by virtue of its industry expertise. However, in our view the combination of expertise and a significant shareholding is important. We do not regard BSkyB’s status and expertise as sufficient in themselves to enable BSkyB to influence ITV’s strategy, and do not therefore believe that any level of partial divestment would be ineffective. Nevertheless, BSkyB’s ability to influence other shareholders is a factor we have taken into account in making cautious assumptions as to what level of shareholding BSkyB would have to divest in order for a partial divestiture remedy to be effective (see paragraph 6.32).

6.38 We therefore conclude that a divestment of shares to below 7.5 per cent would be effective in remedying the SLC and the consequent adverse effects on the public interest. We recognize that this assessment is not solely a matter of calculation or quantitative analysis, but is in part a matter of judgement. However, based on the analysis that we conducted, we were confident that, below this level, there would be no realistic prospect that BSkyB would be able to exercise material influence in the ways that we have identified. ITV would therefore be able to design and implement its strategy unfettered by a competitor.

A voting trust

6.39 BSkyB proposed an alternative mechanism to a full or partial divestiture of its shares in ITV—namely a voting trust. It initially proposed that 3 per cent of its voting rights regarding certain special resolutions relating to a waiver of pre-emption rights would be ceded to an independent trust. BSkyB would retain the economic rights relating to those shares. It subsequently proposed that the trust should vote a portion of BSkyB’s ITV shareholding on all resolutions put to shareholders and finally proposed

questioned the validity of taking 56 per cent effective turnout into account, we note that if both of these events were to recur, then a shareholding of 8 per cent would give an effective voting weight of 25 per cent.

ITV told us that a very small proportion (around 0.025 per cent) of its shareholders are entirely un-contactable. However, in the event of a squeeze out ITV believes that around 5 per cent may in practice fail to respond to an offer, although it impossible to calculate this figure precisely. ITV undertook an analysis of public company takeovers over the last two years which indicated that the number of shareholders that fail to respond may be as high as 7 per cent.
that the trust might cover the entirety of BSkyB’s voting rights. We noted that this last proposal was broadly consistent with a proposal by one third party [3].

6.40 We considered the effectiveness of a voting trust mechanism as a potential remedy. We noted BSkyB’s evidence that voting trusts have been used to address potential shareholder conflicts of interests or to meet regulatory concerns. However, with regard to UK merger control, a trust has been used by the CC only as a transitional measure (for example as part of a divestiture remedy) or as one part of a remedy package. In contrast, we noted that the arrangement proposed by BSkyB is fundamental to its proposal and would have to remain for as long as BSkyB retained a significant shareholding in ITV. We are unaware of any circumstances in which a voting trust has been used as a permanent and complete solution to an adverse finding on a merger inquiry.

6.41 We therefore regarded BSkyB’s proposal as a novel one and considered from first principles whether the transfer of some or all of BSkyB’s voting rights to an independent trust could be an effective means of remedying the SLC and the consequent adverse effects on the public interest.

6.42 We recognized that, in principle, such an arrangement could limit BSkyB’s voting power, thereby reducing its ability to influence ITV’s strategy. We considered whether (a) monitoring and enforcement risks and (b) the retention of BSkyB’s economic interest in its shareholding might reduce its effectiveness as a remedy compared with a straightforward full or partial divestiture of shares.

6.43 BSkyB said that the voting trust arrangement required a minimal amount of monitoring. In order to ensure compliance with any arrangement, BSkyB also said that it could incorporate a ‘whistle-blowing’ clause in the event that BSkyB approached the trustee in relation to the exercise of its vote.

6.44 We thought that the voting trust should be subject to appropriate monitoring arrangements. The impartiality of the trustee would need to be verified initially and monitored subsequently. Further, the performance of the voting agreement by the trustee should be monitored for as long as the shares were subject to the trust. We did not accept BSkyB’s argument that it would be sufficient simply to entrust the implementation of the remedy to a third party with little or no monitoring.

6.45 We note that the draft agreement provided to us by BSkyB proposed that the trust would work by vesting in the trustee complete discretion as to how to vote the shares. In reality it would be impossible to determine whether the trust had in fact exercised its voting rights independently. In addition, if any compliance questions were to be raised in relation to the trustee’s voting behaviour, this could only take place ‘after the event’, and the monitoring process could not correct or remedy a breach of the undertakings. The effectiveness of the remedy would therefore depend completely on the voting trustee properly fulfilling its role.

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215 An example in which a voting trust was included as a minor part of a remedy package (though not used in practice) was in **DBAG/LSE**.

216 Any concerns that we had had about the scope of the voting rights ceded to the trust were overcome through BSkyB’s proposal to cede all its voting rights.

217 Our Guidance CC2 states in paragraph 4.15 that in considering the effectiveness of a remedy, the ease of monitoring is a relevant consideration, and that one-off remedies that change the structure of the market (so called structural remedies) are likely to be preferable to remedies that impinge upon the behaviour of firms (so called behavioural remedies) as they address the effect of the merger directly and will require comparatively little, if any, monitoring or enforcement of compliance.

218 BSkyB said that its proposal was closer to a structural than a behavioural remedy, being a one-off remedy which would change the structure of the market. It regarded the voting trust as a means of securing a structural remedy, namely the divestment of voting rights.
6.46 We are not calling into question the impartiality or professionalism of BSkyB’s proposed trustee. However, we see risks in a long-term remedy which places complete reliance on a third party in this way, and have significant concerns that it would not be appropriate to adopt a remedy which would be completely or substantially incapable of the necessary effective monitoring.

6.47 We considered whether the trustee could be instructed to vote in a certain way to make it easier to monitor compliance. The trustee might, for example, be instructed to vote in proportion to all votes cast, in line with the Board or to abstain from voting altogether. We thought, however, that there were potential distortions associated with each of these solutions:

(a) it would not be appropriate to stipulate that the trust should always vote with the Board, since this would distort the votes cast and guarantee the ITV Board a block vote;

(b) it seemed to us, in principle, fairer that it should vote in proportion to all votes cast. However, although the trustee would still cast its votes, the votes could never determine the outcome since the proportion of the votes for and against would remain the same. This would distort the outcome of the vote. In addition, this would be difficult to achieve in practice, since it would involve the trustee only voting once all other votes had been cast; and

(c) finally, if the trust abstained from voting this would distort the voting weight of all other shareholders (see paragraph 6.55).

It was therefore not clear to us that there was a simple method of pre-determining the way in which the trust should exercise its vote which would not distort the votes cast.

6.48 Other monitoring and enforcement issues arise because the remedy would depend on a contract between BSkyB and a third party. The content of that contract would have to be subject to the undertakings—for example, any changes to the contract would have to be monitored. There would also be risks associated with the collapse of the contract—for example, if there were a dispute between BSkyB and the trustee about its performance or remuneration, if the trustee ceased to do business, or if it wished to terminate the arrangement.

6.49 Secondly, we note that a partial divestiture would result in BSkyB relinquishing both its economic interest in, and its voting control over, the shares divested. The voting trust mechanism proposed by BSkyB, on the other hand, whilst taking some or all of ITV shares out of BSkyB’s voting control, would leave the economic interest of the whole of its 17.9 per cent stake in ITV with BSkyB.

6.50 BSkyB would therefore remain much the largest owner of shares in ITV. Even if BSkyB did not retain any voting rights, other shareholders could still attach additional weight to BSkyB’s views on ITV’s strategy, as a result of its substantial economic interest in ITV. Further, as set out in paragraph 4.117, by retaining its economic rights relating to a 17.9 per cent shareholding, BSkyB could have the opportunity to influence the course of any future transactions involving ITV, since it would, for example, still be able to choose whether to sell its shares to a third party.

219BSkyB subsequently proposed that it might undertake not to exercise the entirety of its voting rights (see paragraphs 6.54 to 6.57), which would be equivalent to the trust abstaining from voting altogether.

220We noted also that, under a voting trust arrangement, BSkyB would retain control over the shares that it owned and would be able to block a squeeze out (see paragraphs 6.35 and 6.36). As discussed in paragraph 6.36, we do not place great weight on BSkyB’s ability to block a squeeze out, in itself, although we consider that a shareholder with a stake large enough to block a squeeze out could also enjoy additional credibility with other shareholders.
6.51 ITV told us that BSkyB’s proposals (see paragraph 6.9) also raised a number of practical issues which would need to be resolved if they were to be pursued including, for example, how its proposals would work in the context of any future pre-emptive rights issue, a scheme of arrangement or a takeover situation.

6.52 In summary, we have significant concerns regarding the likely effectiveness of the voting trust mechanism as put forward by BSkyB, when compared with a divestiture remedy. In particular, we are not satisfied that effective mechanisms could be put in place to provide the necessary oversight and enforcement of the remedy. We recognized the additional concerns put forward by ITV in paragraph 6.51, but did not find it necessary to pursue these further since we had concluded in any case that the remedy proposal was unlikely to be effective.

6.53 We therefore conclude that BSkyB’s proposal to cede all its voting rights to a voting trust would not address effectively the SLC and the consequent adverse effects on the public interest.

Undertaking not to vote shares

6.54 BSkyB also proposed to undertake not to exercise the entirety of its voting rights (see paragraph 6.20). We recognize that it would not be necessary to construct a voting trust for this arrangement to take place—BSkyB could simply give a behavioural undertaking not to vote.

6.55 Any such arrangement would be inherently distorting, giving greater weight to the votes of the remaining shareholders (see paragraph 6.47). In effect, turnout would be 17.9 per cent lower than if the stake were held by an active shareholder. This seemed to us to be a significant distortion to the operation of ITV’s corporate governance were this remedy to be adopted.

6.56 BSkyB said that this proposal provided a clean-cut structural solution. However, as with the voting trust proposal, we were concerned that this proposal would create the need for ongoing monitoring and enforcement, in contrast to full or partial divestiture. The OFT would have to monitor compliance with the undertakings for as long as BSkyB retained its stake in ITV and would also have to enforce any conditions that might relate to the subsequent sale of the retained stake (for example, not to dispose of the shares to an associated person, see paragraph 6.64). The need for ongoing monitoring and enforcement would create additional risks for ITV. Moreover, as set out in paragraph 6.50, BSkyB could also have the opportunity to influence the course of any future transactions involving ITV as a result of retaining its economic interest and hence remaining much the largest owner of shares in ITV.

6.57 We therefore conclude that BSkyB’s proposal not to exercise the entirety of its voting rights would not address effectively the SLC and the consequent adverse effects on the public interest that we have identified.

Other behavioural remedies

6.58 We also invited views as to whether to supplement a partial divestiture remedy with behavioural remedies. In our assessment of material influence, we did not assume that BSkyB would achieve Board representation. However, we note that if BSkyB did in fact obtain Board representation, this might give rise to concerns regarding

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221 For example, with a 60 per cent turnout, a shareholder with a 5 per cent stake in ITV would have an effective voting weight of 12 per cent if BSkyB did not vote, compared to an effective voting weight of 8 per cent if BSkyB voted.
BSkyB’s influence over ITV. The interim undertakings that BSkyB will not seek or accept Board representation will lapse on final determination. For the avoidance of doubt, we therefore consider it appropriate that, in addition to a partial divestiture remedy, BSkyB should give undertakings that it will neither seek nor accept Board representation. Such undertakings would be clear, visible and easily enforceable.²²²

6.59 Other behavioural undertakings would also be needed to support the divestment. In particular, BSkyB should be prohibited from reacquiring shares in ITV.²²³

Implementation

6.60 We considered whether any risks may arise relating to the timing or the manner of disposal of some or all of BSkyB’s shareholding in the event of a divestiture remedy.

6.61 We acknowledge that the sale of BSkyB’s shareholding could disrupt ITV’s share price, at least temporarily, and that such disruption might be avoided if the sale were conducted over a period of time. Our guidance states that the divestiture period will normally be six months at a maximum although in practice shorter periods have sometimes been specified.²²⁴

6.62 BSkyB told us that, if it were to be required to divest its entire stake, an appropriate period within which to effect the divestment would be around 17 to 20 months. Such a period would minimize the creation of a stock overhang and would allow a reasonable time for BSkyB [istentense] to explore divestment [istentense] in a manner that would minimize disruption to ITV’s share price. ITV, by contrast, said that it wanted a ‘normal’ market in its shares to return as soon as possible, and said that three months would be adequate to find a buyer or buyers for the relevant shares while limiting any further damage to ITV’s share price.

6.63 We [istentense] consider that a period of [istentense] from agreement of the undertakings would be adequate for the orderly and non-disruptive disposal of the requisite portion of BSkyB’s stake in ITV.

6.64 We believe that certain safeguards should accompany a full or partial divestiture to avoid purchaser risk—in particular the risk that BSkyB might sell its stake to an associated person—and the risk of BSkyB influencing ITV’s strategy during the divestiture period.

6.65 With a divestiture period of no more than [istentense], we believe that it would be appropriate to seek short-term behavioural undertakings from BSkyB, which would preclude it from voting the shares that it was required to divest and from selling the shares to an associated person. If, for any reason, the divestiture period was longer than this, a divestiture trustee could be mandated to sell the requisite portion of shares and hold the voting rights associated with these shares until divestiture. The terms of the trustee’s mandate would be agreed with the Secretary of State, and would incorporate a restriction on selling the shares to a person associated with BSkyB.

²²²BSkyB told us that it would be willing to give such undertakings.
²²³Paragraph 3.2 of CC8 says ‘In general, the merging parties will be restricted from subsequently purchasing assets or shareholdings sold as part of a divestiture package or acquiring material influence over them’.
²²⁴Paragraph 5.5, CC8.
Conclusions on remedies effectiveness

6.66 We conclude that two remedy options would be effective in addressing the SLC and consequent adverse effects on the public interest expected following the acquisition by BSkyB of a 17.9 per cent shareholding in ITV:

(a) divestiture of the whole of BSkyB’s shareholding in ITV; and

(b) divestiture by BSkyB of such part of its shareholding in ITV that it would hold less than 7.5 per cent of ITV’s issued ordinary shares, combined with an undertaking not to seek or accept ITV Board representation.

Proportionality

6.67 Having identified the two remedy options that would be effective in addressing the SLC and the consequent adverse effects on the public interest, we now consider the proportionality of each. As set out in our guidance, when choosing between two equally effective remedies, we must choose the least costly, least intrusive remedy. As noted in paragraph 6.6, our guidance states that ‘the Commission will not normally consider the costs of divestment to the parties in the case of a divestiture remedy’.

6.68 BSkyB said that full divestiture could be costly, not only in terms of the potential financial loss to BSkyB, but also for ITV shareholders since ITV’s market price would be depressed as a result of BSkyB being a forced seller of its entire stake. In its response to our Notice, BSkyB said that our SLC finding was ‘based solely upon certain specific potential effects which the CC considers that Sky’s present shareholding could have on certain hypothetical competitive strategies of ITV…which might require ITV’s board to seek shareholder approval by means of a specific special resolution’. A divestiture remedy—whether full or partial—would remove BSkyB’s voting rights on all resolutions in those shares which it was required to divest. BSkyB said that it would be disproportionate to require the divestment of the economic rights of the shares. This would, in its view, go far beyond what was necessary to remedy the SLC and adverse effects that had been identified.

6.69 BSkyB said that, in its view, the basis upon which we were finding jurisdiction in the present case was ‘unprecedented’. Nevertheless, we were satisfied that we should not consider the costs of divestment as part of our assessment of proportionality.

6.70 In our view, of the two effective remedies that we have identified, partial divestment is the least intrusive, as it requires BSkyB to divest a smaller proportion of its shareholding in ITV. We therefore thought it the more proportionate.

6.71 We are not required to consider the proportionality of either the voting trust or the option not to exercise the entirety of BSkyB’s voting rights, because neither remedy was considered to be effective. Nevertheless, we note that both could be considered to be more costly mechanisms than either of the divestiture options. However the voting trust was organized, it would require long-term monitoring and enforcement which would be costly to operate. The same consideration would apply to an undertaking from BSkyB not to vote its shares in ITV. We also thought it likely that, if BSkyB were to undertake not to exercise its voting rights, there would be additional administrative costs to ITV, and wider capital market inefficiencies, associated with having a large non-voting shareholder.

225CC2 paragraph 4.10.
Relevant customer benefits

6.72 Finally, we are required to have regard to any relevant customer benefits and any effects that our remedies may have on them. We have received no evidence concerning relevant customer benefits arising from the acquisition. We therefore see no reason to modify our remedy in the light of any relevant customer benefits.

Conclusions on remedies

6.73 We conclude that there are two effective remedies to the SLC and consequent adverse effects on the public interest that we have identified—full divestiture and partial divestiture.

6.74 We are satisfied that partial divestiture to a level below 7.5 per cent is in practical terms likely to be as effective a remedy as full divestiture, because it removes any realistic prospect that BSkyB would be able materially to influence ITV’s strategy. It is more proportionate than full divestiture because it is less intrusive. We are therefore satisfied that partial divestiture by BSkyB of its shareholding in ITV down to a level below 7.5 per cent is as comprehensive a solution as is reasonable and practicable to the SLC and any adverse effects resulting from it. We recommend that the Secretary of State should take action to implement this remedy. We also recommend that the Secretary of State seeks undertakings from BSkyB that it will not seek or accept representation on ITV’s Board.

6.75 We recommend that the divestiture should take place within [X] of undertakings being agreed, accompanied by undertakings from BSkyB to the Secretary of State that it will not vote the part of its stake in ITV to be divested during the divestiture period. If a longer period were allowed, we would recommend that a divestiture trustee be put in place and that the Secretary of State approves the trustee and its mandate. In either event, undertakings should be sought from BSkyB not to sell the shares to an associated person.

6.76 As set out in paragraph 1.4, in case the Secretary of State makes no finding at all, we must answer the questions set out in paragraph 6.3. Our recommendations set out in paragraphs 6.73 to 6.75 are also our answers to these questions.