



BT's response to BEREC's draft report on the impact of premium content on ECS markets and the effect of devices on the open use of the Internet

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Introduction and purpose of the report

1. BT welcomes the opportunity to comment on BEREC's draft report.
2. The BEREC report discusses two distinct topics: the impact of premium content on Electronic communication services (ECS) (chapter 2) and the impact of devices on the open use of the internet (chapter 3). The purpose of the report is to develop an understanding of the influence of other sectors, namely content and devices, on the electronic communications sector across Europe. The main sources of evidence for this report were the responses of BEREC members to a specifically designed questionnaire.
3. In this response BT focuses on BEREC's discussion of premium content and its impact on ECS markets. BT agrees with BEREC's observation that the bundling of premium content with ECS is an increasing phenomenon: for example in the UK the share of households who have a triple play bundle (including fixed voice, broadband and pay TV) rose from 16% in 2010 to 28% in 2016.¹ This increasing share across the total consumer base suggests that in recent years triple play services have represented an even more significant share of all services sold. It is therefore important that NRAs understand the implications such bundling has on the competitive dynamics and consumer outcomes in ECS markets.
4. Given the high level nature of the draft report, BT's comments are also high level at this stage. Should BEREC develop this work further, BT expects to contribute in more detail in further rounds of stakeholder consultations.
5. The response sets out below general observations regarding the content and purpose of BEREC's report before setting out a number of comments on BEREC's analysis.
6. It would be helpful if BEREC clarified the status of this work, its purpose, whether it intends to develop it further, and how stakeholders can get involved in that process. This will allow industry stakeholders to engage fully in this important workstream.

Further work is required to provide a complete and balanced view of the impact of content on ECS

7. The draft report is a useful first step that touches on many of the relevant issues related to assessing the impact of bundling on ECS markets. However, further work is required in order to develop a more complete and balanced view of how content markets influence ECS markets, and how this impacts the assessment of ECS markets in the context of ex ante regulation. This is particularly important should BEREC plan to use this draft report as the basis for recommendations or guidance to NRAs on the assessment of bundled markets. BT provides below a number of specific comments that a further iteration of the report might usefully consider.

¹ Ofcom, Communications Market Report 2017, Figure 1.5. The share of households taking a triple play bundle increases to 32% in 2016 and 33% in 2017 after Ofcom changed the way in which it asked consumers about their take-up of bundled services.

8. Any report considering the impact of content on ECS markets needs to start from an acknowledgement of the following three facts that the draft report does not explore and that BT would expect BEREC to consider in more detail as part of any further iteration of the report:
- a. **First, content is significantly more locally diverse and varied than ECS**, not only by virtue of differences in how they are regulated in different countries that may have led to very different content market structures, but due to natural language and cultural boundaries between countries and regions. It is therefore difficult to envisage universal solutions applicable across situations in all countries. By way of example, in the UK around one half of households hold a pay-TV subscription giving access to premium content and technical services.² The popularity and take-up of pay-TV, cable TV, free-to-air and other forms of TV subscription models is differs significantly across the EU.
 - b. **Second, content is a much more emotive product for consumers than ECS** and likely to influence purchasing decisions of service bundles more strongly than the voice and broadband elements of these bundles. Consumer research evidence from the UK suggests that for many customers, Pay TV is the most important part of their bundle³ Where ECS incumbents do not hold market power in content markets (which is the case in many EU member states, including the UK), their ability to leverage any market power in the ECS elements of bundles may be constrained. Furthermore, where ECS regulation captures content bundled by an ECS incumbent with voice and broadband services (e.g. through margin squeeze tests) it may restrict the regulated ECS incumbent's flexibility to use its content, even where new entry in content markets may be highly desirable.
 - c. **Third, digital markets, including content markets, change and innovate at pace.** The business models of content providers have been changing significantly, as has the way in which customers consume content. This includes the increasing bundling with ECS as well as the emergence of new over-the-top platform providers of premium on-demand content (particularly drama and movies). Regulators need to be mindful both of the potential of disruptive technology and market entry changing competitive dynamics, affecting their forward looking market assessments, and the potential for regulation to undermine innovation and evolution in digital market.
9. In addition BT has the following comments on specific aspects of BEREC's draft report, which further analysis of this topic should examine in more detail.

Further comments on specific aspects of BEREC's report

10. The report correctly identifies many of the key issues that are relevant when considering the implications of content bundling with ECS. The table on page 13 gives a useful summary of the potential benefits and drawbacks that can arise from bundling. It does not, however, go

² Ofcom, Review of the Pay TV wholesale must-offer obligation, 19 December 2014, paragraph 3.3.

³ Ofcom, Strategic Review of Digital Communications, 16 July 2015, paragraphs 1.61. and 8.35; and Ofcom Pay TV Omnibus Study 2013, table 23, available at https://www.ofcom.org.uk/_data/assets/pdf_file/0030/79914/pay-tv-omnibus-2013-data-tables.pdf.

beyond conceptual statements. Further, the report provides no evidence as to the balance between the benefits and drawbacks in practice. In light of the diverse landscape of content markets, a general cross-EU statement may be difficult, but BEREC could usefully explore in more detail how the benefits and drawbacks could in practice be identified and measured.

11. BEREC's approach appears to be focusing on sources of concern, rather than assessing the level of consumer benefits. The following quote appears representative of BEREC's mindset: *"If the ability to provide premium content turns out to be a major factor of choice between ECS providers from the consumer standpoint, more than the quality of the ECS provided, theoretically there may be a potential incentive for ECS providers to prioritise investment in premium content. Given the cost of premium content rights, this could have a non-negligible negative impact on the investment of ECS providers in their infrastructure."*

If BEREC's draft report were intended to provide guidance to NRAs for the assessment of bundled markets it needs to provide an objective view of both benefits and drawbacks for consumers.

12. In any event the facts do not support BEREC's concerns about ECS incumbents acquiring significant shares of exclusive premium content: across Europe, broadcasting rights to the national premier football leagues tend to be the most valuable content. BT understands that in only a few countries these are held by the ECS incumbent, which includes countries in which, as in the UK, the ECS incumbent holds only minority shares of the rights. This suggests that BEREC's primary concerns are of little relevance to market realities. The report should instead focus on ensuring that any regulation in ECS markets does not undermine ECS providers' ability to enter and compete in content markets on the merits.
13. BEREC's specific concern about content investment crowding out infrastructure investment is, in the case of the UK, entirely misplaced. Since BT entered the market for premium sports content in 2013 with the launch of its BT Sport channels, its investments in network infrastructure and service quality have remained high and unaffected by its investments in premium sport content.
 - a. In October 2015 BT reported that it had invested around £14bn in tangible assets over the previous seven years, a multiple of its competitors' combined capital expenditure over the same period. Openreach's capital expenditure alone had averaged over £1bn per annum.⁴
 - b. Openreach plans further network investments capable of delivering speeds above 100mbps in the near term, by deploying FTTP networks to up to 2m premises and G.fast to 10m premises.⁵
 - c. Openreach has also been investing in and improving its service quality: in 2016/17 it doubled its annual Fault Volume Reduction investment from the preceding year and exceeded all 160 Minimum Service Levels set by the regulator, and strengthened its service commitments to customers for the financial year 2017/18.⁶

⁴ BT's response to Ofcom's discussion document "Strategic Review of Digital Communications", 8 October 2015, paragraph 57, available at https://www.ofcom.org.uk/data/assets/pdf_file/0029/37937/bt.pdf.

⁵ BT's response to Ofcom's consultation document "Wholesale Local Access Market Review", 19 June 2017, paragraph 2.13, available at https://www.ofcom.org.uk/data/assets/pdf_file/0008/105011/BT.pdf.

⁶ Openreach, Quality of Service for WLR, MPF and GEA – Response to Ofcom's consultation on proposed quality of service remedies, 19 June 2017, paragraphs 3-5, available at https://www.ofcom.org.uk/data/assets/pdf_file/0013/105115/Openreach.pdf.

There can be no suggestion that the levels of BT's investments in the two distinct areas of content and network infrastructure had any impact on each other.

14. BT has in the past highlighted the asymmetry between ECS providers and content providers, given that access to ECS networks is highly regulated whereas owners of exclusive premium content can enjoy strong and persistent market positions typically without any wholesale regulation. As a consequence ECS providers face high entry barriers to premium content markets, whereas content providers can enter ECS markets with greater ease on the basis of regulated access products.
15. BEREC quotes a limited number of regulatory cases in which content played a role. It includes the imposition of the VULA margin squeeze test by Ofcom in the UK in 2015⁷, in which BT's costs for BT Sport, which is sold in bundles with broadband services as well as on a standalone basis, need to be recovered by margins on superfast broadband bundles. BEREC appears to use this case as evidence that it is justified, or even necessary, to include content cost recovery in margin squeeze tests on broadband services.
16. This however ignores the EC's comments made on Ofcom's proposed test which highlights clear concerns with the proposed way in which Ofcom required the recovery of content costs:⁸

"In the view of the Commission, Ofcom's proposed approach lacks the necessary flexibility in particular with regards to the treatment of costs for BT Sports. The Commission considers that the proposed static approach unduly limits BT's commercial activity with regards to a market in which it does not have SMP.

Indeed, Ofcom's purpose in designing the test is to address a competitive concern in relation to pricing of a regulated product, i.e. VULA, for which it does not propose a charge control. However, the design of the test proposed by Ofcom may result in BT choosing to address a failed test by changing its behaviour on a market other than the regulated market, for example by increasing retail prices or reducing costs for BT Sports. Given the magnitude of the costs involved, and the uncertainty of future costs and revenues of BT Sports as new rights auctions approach, there is a risk that Ofcom's regulatory intervention would have a significant impact on non-regulated markets, without necessarily affecting the price of the VULA input. Ofcom will therefore have to remain vigilant that the application of the test does not have unintended consequences in markets where the application of ex post competition law would be sufficient, or where BT's SMP in the WLA market does not necessarily play a role."

17. This case illustrates the risk that ECS regulation can inadvertently distort competition in content markets. BEREC should, in any further report, carefully examine this risk and provide guidance to NRAs how to avoid it.

⁷ In its recent consultation on its Wholesale Local Access Market Review Ofcom proposed the removal of the current VULA margin squeeze test from April 2018, particularly in light of the proposed VULA charge control. Ofcom is expected to publish its decision on this market review in early 2018.

⁸ European Commission, Commission Decision concerning Case UK/2015/1692: Wholesale local access at a fixed location in the United Kingdom, Comments pursuant to Article 7(3) of Directive 2002/21/EC, 13 February 2015, pages 5-7.

Conclusion

18. In conclusion, BT welcomes BEREC's interest in this important subject. In light of the growing importance of bundled services, a study of the implications for regulation of ECS is important and well timed. Any such study must recognise that the issues are likely to differ significantly in different member states.
19. It is notable, however, that the current draft report focuses on the task of identifying risks in scenarios in which ECS incumbents acquired exclusive premium content rights and the ability to exploit strong positions in content markets. This ignores the more prevalent scenario, in which ECS incumbents are smaller entrants in content markets. Where regulation of ECS incumbents captures also their content services, it can have detrimental effects on ECS incumbents' incentives and ability to compete freely and effectively in content markets, even where more competition in content markets were desirable. If the draft report is to develop further into a guidance document to NRAs it needs to address such risks in much further detail.