Submission to the Independent Communications Authority of South Africa ("ICASA")

DISCUSSION DOCUMENT ON THE INQUIRY INTO SUBSCRIPTION TELEVISION BROADCASTING SERVICES - Published in Government Gazette No. 41070 of 25 August 2017

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Introduction

1 Telkom SA Ltd welcomes the opportunity provided by the Independent Communications Authority of South Africa ("ICASA" or "the Authority") to provide written comments on its views on ICASA's '*Discussion Document: Inquiry Into Subscription Television Broadcasting Services',* published on 25 August 2017 in Government Gazette Notice 642 of 2017 ('the Discussion Document'). We look forward to engaging further with the Authority on the issues raised in any subsequent processes.

2 Telkom's submission is based on consideration of the particular characteristics of the South African market and international best practice. It is structured into two sections:

- Overall comments and questions on the Discussion Document; and
- Response to questions posed by the Authority.

Overall comments

3 This inquiry into competition issues in the subscription broadcasting market is critical and long overdue. The dominance of one player in the market over an extended period has inevitably affected not only the pay television sector in South Africa, but also the ongoing viability of free-to-air services and ultimately diversity of content and services available to South African audiences. Telkom thus believes that the issue should ideally be dealt with holistically so as to ensure that ICASA's mandate to ensure diversity in the South African broadcasting sector is met. In light of this, Telkom raises the following:

Integrity of the process

4 It is crucial that ICASA continues to ensure the integrity of the process to be followed in finalising this long overdue inquiry and that the process be thorough yet concluded timeously. The lack of competition in the pay-TV and its effects on other content related sectors has negatively affected ICASA's capacity to ensure that all

South Africans have access to a diverse range of content and the concerns become more entrenched over time.

Cooperation and collaboration with Competition Commission

5 We welcome suggestions by the Authority that it will work closely with the competition authorities where necessary. As noted in response to some of the questions, international best practice indicates that a collaborative approach between sector specific regulators and competition authorities has had the most impact on fair competition in the sector by addressing these.

6 This is further in line with the objectives and spirit of the Memorandum of Agreement Entered Into between the Competition Commission of South Africa and the Independent Communications Authority of South Africa ("the Memorandum or MOA")[1] which became effective in September 2002. In line with this Memorandum, Telkom notes that, while it does not explicitly deal with inquiries such as this, it does make provision for the establishment of Joint Working Committee (section 40 between the two regulators which it seems would be the ideal forum for such discussion. It further refers to the sharing of resources (paragraph 5) and information (paragraph 6).

Holistic approach

7 It seems from the Discussion Document that the Independent Communications Authority of South Africa ("ICASA or the Authority") will not be looking in this process fully at a number of related issues, including:

- The impact of dominance in the pay-TV market on access to advertising by free to air ("FTA") services (a crucial factor affecting ICASA's ability to fulfil its mandate). This issue has been raised by both SABC and e.tv as a critical competition issue over several years. Given that ICASA is currently considering licensing more FTA broadcasters, it would appear to be crucial to address this issue urgently.

[1] Competition Commission, Government Gazette, 20 September 2002, Notice 1747 of 2002

- Similarly, the impact of this on growth in other sectors (such as over-the-top - OTT - and video-on-demand – VOD - services). Should be considered and it is proposed regularly reviewed.
- Reviewing existing regulations/policies that may pose barriers to entry. Several submissions raise regulatory barriers to entry and suggest that these be identified through this Inquiry process. Issues that have been raised in submissions include the need to address potential barriers to entry inherent in DTT related rules and regulations, areas which are as yet unregulated (e.g. Internet Protocol Television), the failure by the regulator to address competition related issues expeditiously – despite commencing with several such processes, the length of time the regulator takes between issuing an invitation to apply for a licence and awarding these.
- What are called 'technical issues' in the Discussion Paper – i.e. interoperability of set top boxes, access to conditional access and subscriber management software/services and to electronic programming guides. While these are mentioned in the Paper, it is suggested that there might need to be a separate process to address this.
- The impact that agreements such as that between MultiChoice and the SABC on the news channel and Encore might have on other subscription operators.
- A full exploration of the ownership of subscription players and how, if at all, this impacts on the market. It is noted here that Naspers the ultimate owner of both DSTV and M-Net is the largest media company in South Africa and is active in a range of online and other sectors (apart from media). Due to the history of grandfathering of licences, among other things, it is also the only print media company allowed cross media control in the broadcasting sector. The impact of this on competition and diversity should be considered. Naspers is also active in a range of other online sectors.

Response to questions posed by the Authority

8 In this section, we present our answers to the questions posed by ICASA throughout the Discussion Document. These questions and answers are grouped according to the themes set out in the Discussion Document, namely (i) market

definition; (ii) consideration on the effectiveness of competition in the market; (iii) consideration of licensees with Significant Market Power (SMP); and (iv) possible pro-competitive licence conditions. Where relevant, we group together linking questions to present a comprehensive response.

Market Definition

Q1: Do you agree with the theoretical approach to defining relevant markets and market segments?
Q2: Are there aspects of this market definition theoretical framework that would not apply to subscription television broadcasting services?

9 As stated in para 5.2.2 of the Discussion Document, "market definition is a means to an end, the end being the identification of impediments to competition." As such, it is crucial to follow a clear theoretical framework for defining relevant product and geographic markets. Failure to do so may result in misguided (or insufficient) regulation being implemented.

10 In defining relevant markets, as required by section 67 of the ECA, it is customary to use the small but significant non-transitory increase in price (SSNIP) test. This is also standard best practice internationally.[2] However, as stated in the *Organisation for Economic Co-operation and Development (OECD) Policy Roundtable on Competition Issues in Television and Broadcasting* (2013), variables specific to audio-visual products need to be taken into account in a market analysis, namely "high fixed costs, low marginal costs, bundling, non-price competition, two-sided or multi-sided nature of markets, vertical integration or rapid technological development."[3]

11 There are two main issues that we would like to point out in terms of the application of the SSNIP test in the digital broadcasting market. The SSNIP test should start with the narrowest possible market and then consider potential substitutes. In the current case, the relevant question is whether subscription television broadcasting services form a separate market, whether there are separate sub-markets or

[2] OECD. 2012. Policy Roundtable: Market Definition.
[3] OECD. 2013. Policy Roundtable: Competition issues in Television and Broadcasting.

whether similar services (e.g. video on demand) form part of the relevant market. The first point that should be emphasised is that when prices are already at a monopoly level, it might seem that certain products are substitutes, while they in fact would not be considered substitutes at competitive price levels. This is an important issue for ICASA to bear in mind in the current inquiry. This has also been taken into consideration by the British regulator (Ofcom) in their study of market definition in pay TV services in 2007, where they identified the possibility that current prices may be above competitive prices as a difficulty in defining relevant markets.[4]

12 The problem is known in the literature as the cellophane fallacy, referring to a well-known case in the USA where the market was incorrectly defined as flexible wrapping materials, as the incumbent had already increased the price to the monopoly level. The application to the subscription television broadcasting market is as follows: since Multichoice is the main player currently, it might seem that services such as Netflix (or other services on OTT platforms), compete with Multichoice. However, this might simply be an indication that the prices have already been increased to a level where alternative services become substitutes. ICASA should bear this in mind when defining the relevant markets. I.e. one should be careful of defining overly broad markets based on notional substitutes at monopoly price levels.

13 The second issue that should be pointed out is that these types of markets are characterised by rapid technological developments.

14 This is especially pertinent in broadcasting and requires that the dynamic nature of this market be appropriately accounted for. As stated in the *OECD Policy Roundtable on Market Definition* (2012): "*Some industries such as the media industry, telecommunications, biotech or medical technology are characterised by rapid technological progress. New products are developed, formerly separate functionalities are integrated into one product and process innovations lead to the entry of firms from other industries thereby increasing the competitive pressure on incumbent firms. These developments are often unpredictable, leading to the*

[4] Ofcom (2007) "Market definition and market power in pay TV". Annex 13 to pay TV market investigation consultation".

creation of new markets or the convergence of formerly separate markets. As a result, ***market boundaries may shift rapidly*** [emphasis added]*."*[5] As such, the rapid (and often unforeseeable) changes in technology can create uncertainty in market definition and can lead to inconsistencies within competition litigation. It also brings about problems w.r.t. the drive towards technology-neutral legislation as noted in the Electronic Communications Act (ECA).

15 Although ICASA acknowledges future developments such as the impact of OTT services and the digital migration in sections 4.9 and 4.10 of the Discussion Document, these points are not explicitly incorporated in the discussion of the theoretical market definition framework in section 5.

16 Given the potential impact of technological change, it is also important to periodically review the market definition. ICASA could essentially classify the defined markets as either competitive, uncompetitive or prospectively competitive. The latter classification would reflect those markets which are not currently competitive, but where ICASA sees the development of competition and creating the requirement for a regular review of the extent of competition. This classification is consistent with the principles reflected in the EU Electronic Communications Framework[6] and is enshrined in the approaches adopted by National Regulatory Authorities (NRAs) in the European Union (EU) and in the many other countries who follow the broad principles of this framework.[7]

17 This approach would be beneficial for South Africa. The eventual goal of ICASA should be to develop competition in markets rather than rely upon regulatory intervention. In between these regular reviews, it should still be open to any interested party to provide qualitative evidence of changes that may affect the market definitions currently in place for regulatory purposes. This could include

[5] OECD. 2012. Policy Roundtable: Market Definition.

[6] Commission guidelines on market analysis and the assessment of significant market power under the Community regulatory framework for electronic communications networks and services (2002/C 165/03). Paragraph 20 states that in carrying out the market analysis NRAs should conduct a forward looking, structural evaluation of the relevant market, and determine whether the market is prospectively competitive.

[7] See Oftel's Notices of determinations to remove the determinations that Vodafone and BT Cellnet have Market Influence under Condition 56 of their respective licences. Oftel concluded that the mobile sector was "prospectively competitive".

evidence of demand or supply side substitution that would support the adoption of a narrower - or wider - market definition.

18 Furthermore, although ICASA does mention the two-sidedness of the market in para 5.3.3, not enough detail is provided to set out how this will be incorporated into the market definition. Importantly, in two-sided markets, where prices set on one side of the market influence demand on the other side, the knock-on effects of a price increase on one side of the market onto the other side should be considered in understanding whether the price increase would be profitable. In the television broadcasting sector, the two sides of the market are the subscribers and advertisers.

19 In summary, we agree with ICASA's use of the SSNIP test, but recommend that it takes full account of the nature of the broadcasting sector in developing the theoretical market definition framework.

Q3: Do you agree with the approach of using the value chain to identify functional markets?
Q4: If not, how would you go about defining the relevant market/s in subscription broadcasting?

20 We agree with ICASA's use of the value chain in identifying functional markets. As stated in *ICASA's Guideline for Conducting Market Reviews*: "the motive behind enhancing competition is to stimulate both allocative and dynamic efficiency up and down as well as across value chains in the supply of goods and services to the South African consumer."[8] The value chain is therefore the appropriate reference point from which to evaluate effective competition. However, the value chain and the various levels do not by definition constitute separate relevant markets. While ICASA lists several features of the market to distinguish Free to Air (FTA) and subscription TV, the same is not explicitly done for other potential substitutes (i.e. OTT and VOD). While we agree that FTA and other potential substitutes do not currently form part of the relevant market, we would recommend that more formal tests are applied to establish this. Questionnaires are notoriously

[8] ICASA's Guideline for Conducting Market Reviews (2010)

difficult to interpret correctly for market definition purposes and solely relying on such data will create problems for ICASA going forward.

21 The value chain also provides a clear delineation between the different stages of production, which can provide insight into the nature of vertical integration. For example, examining the value chain shows that MultiChoice is the only party that is active at every level and is therefore fully vertically integrated, an issue which is discussed in more detail in Q19 and Q23.

22 We do, however, recommend that the value chain should include what ICASA has referred to in its paper as technical services – i.e. those services which are crucial for managing subscriptions and the relationships with subscribers. These include distribution to all subscribers, subscriber management systems, conditional access systems and electronic program guides (EPGs). These services are distinct to subscription content services (unlike FTA) to ensure only subscribers can receive programming and that they received the bouquet or programmes they have selected. ICASA has it is noted explicitly defined such services as a wholesale market for technical services in section 5.10 of the Discussion Document and Telkom proposes that they be included in the value chain.

23 In terms of content, we note that ICASA has already defined subscription television as a separate market from audio-visual content and proceeded to define sub-markets within this market. It also excludes FTA services. Yet it is noted that in terms of advertising all these sectors compete. This may potentially limit the inquiry as ICASA is only looking narrowly at the impact of the dominance of DStv in the pay-tv market on other pay-tv providers and not at the broader South African broadcasting sector – or at the impact on the objectives of the broadcasting policies more broadly.

Q5: Do you agree with the Authority's definition of what constitutes premium content?
Q6: What other content would you classify as premium in the South African context and why?

24 ICASA proposes defining premium content as "*valuable content that is acquired on an exclusive basis and made available on high end premium bouquets*". This covers blockbuster movies, live sports, international and local series. We broadly agree with ICASA's definition of premium content. However, more clarity is needed on what constitutes "valuable" content.

25 It is important to note that there is no exact definition for premium content, as made clear by the various definitions provided in the responses to ICASA's questionnaire by the SABC, NAB, MultiChoice, Siyaya, SACF, e.tv and Telkom. We note that from Telkom's previous response to ICASA's questionnaire it defined premium content as the following: "*Sport and premium international channels like HBO Premium content is content which has high audience ratings in both its primary market as well as international market. It is also new programming from major distributors (Disney, NBC Universal, Warner Bros, Sony, Fox) which is anticipated to have high audience appeal. Premium content is also the ability to obtain first broadcast/VOD window for content.*"[9]

26 From Telkom's perspective therefore, emphasis is placed on high audience ratings, high audience appeal and implies that there is also a time-sensitive component. As such, it implies that premium content is linked to consumer demand for content and can be described as content which viewers find desirable and are willing to pay a subscription fee for. However, it should be noted that in the South African context, premium does not necessarily imply that it is content that is available on the highest available subscription package/bouquet. It may also refer to content which will draw the most viewers.

27 In order to unpack the consumer trends in more detail, we recommend that ICASA undertake a survey similar to the one in the Ofcom market investigation[10], or that it uses available data and reports to inform its definition of premium content. This will provide useful insights into what South African viewers regard as premium content.

[9] Telkom response to subscription TV questionnaire, response to 3.8 under "D-OTT, STREAMING & VOD PLAYERS".
[10] See Annexure 14 to pay TV market investigation consultation: Summary of quantitative consumer research.

28 In summary, we find that there is no exact agreed-upon definition of premium content. However, we have no contention with ICASA's proposed definition of premium content, namely blockbuster (first-window) movies, live sport, international and local series. Nonetheless, a more detailed analysis of consumer trends will provide ICASA with a better understanding of premium content within the South African context.

Q8: Do you agree with the Authority's characterisation of the retail market and the market definition as outlined above? If not, how would you define the relevant market/s in this regard?

29 The Authority's characterisation of the retail market and market definition firstly evaluates whether subscription TV and FTA TV should be defined as separate markets. We agree that that subscription broadcasting cannot be substituted with FTA, since subscription TV offers premium content as well as a more comprehensive bouquet of channels. However, this might vary with the introduction of FTA multi-channel DTT in particular in relation to cheaper bouquets (that exclude premium content). The Authority does not appear to have considered whether its view applies to all bouquets and will continue to do so in the near future. For example, the Discussion Document does not look at all at the issue of churn in the lower bouquets (or evaluate the extent of this). In particular, the regulator should consider the impact this might have on services that, unlike MultiChoice, are not present on both the satellite and DTT platforms.

30 ICASA also considers whether OTT and subscription TV are within the same market. However, little attention is paid to arguments made in some submissions that pay operators compete and with new OTT services. From our answer to Q1, we note that the market definition should take into account potential future developments in the market such as new technologies and platforms such as OTT. In para 5.7.6, ICASA states that from MultiChoice's submission, it perceives its competitors to be international OTT and video-on-demand service provides. However, the Discussion Document does not sufficiently unpack this statement or evaluate the potential for competition between subscription TV and OTT. We recommend this be evaluated in more detail and more formally, since designing

appropriate regulation needs to be sufficiently forward-looking w.r.t. potential changes in technology, specifically in telecommunications markets (as discussed in our answer to Q1/Q2).

31 For the purposes of the current market definition exercise, we agree with ICASA that broadband penetration in South Africa is insufficient into all areas and markets to provide a clear substitute for subscription TV across the country and to all audiences. However, it should be borne in mind that the consumers who subscribe to premium television content are likely to also have access to sufficient broadband speeds required to utilise OTT services. However, premium subscription TV typically offers first-window movie and series content, whereas OTT players do not. As such, we note that OTT does not currently offer enough of a constraint to subscription TV for it to be included in the same market definition. However, this may change in the foreseeable future and should be regularly evaluated by ICASA.

32 Finally, Telkom notes that within the defined subscription TV market, ICASA defines further sub-markets, namely for the supply of premium and non-premium content. Telkom is happy with this.

33 In summary, although we recommend that ICASA conduct a more thorough analysis of the substitutability between OTT and subscription TV, we agree that there is currently a separate market for subscription TV which can be further sub-divided into a market for premium and basic subscription TV.

Q9: Do you agree with the Authority's characterisation of the wholesale market and the market definition as outlined above? If not, how would you define the relevant market/s in this regard?

34 We broadly agree with the definition of the wholesale market for channel provision. Although we note that there are not only two tiers. We suggest having a market for premium channels and one for all other channels.

Q10: What is the nature of the bargaining power between independent wholesale channel suppliers and broadcasters? How has the nature of this power changed over time?

35 Telkom does not have any comments regarding the nature of bargaining power between independent wholesale channel suppliers and broadcasters.

Q11: Do you agree with the Authority's characterisation of the market and the market definition as outlined above [referring to the content market]? If not, how would you define the relevant market/s in this regard?

36 We broadly agree with ICASA's market definition. However, the concept is in many ways fluid – and channels sometimes themselves successfully make a sporting event premium which was not previously. As such, the definitions should not be set in stone by the Authority, but be adaptable and flexible to address a fluid market.

Q12: Do you agree with the Authority's characterisation of the market and the market definition as outlined above [referring to the market for technical services]? If not, how would you define the relevant market/s in this regard?
Q13: Is it necessary to define a market for technical services? What are the competition challenges in this market?

37 We agree that a market for technical services should be defined, including middle-ware and end-ware (i.e. subscriber management services (SMS), Conditional Access System (CAS) and set-top box (STB) interoperability). This is a key issue that affects ease of switch-over by customers StarSat may be increasingly reluctant to do so) as the boxes are not interoperable or made available to other providers. We note that the information and research provided by the Authority into these issues is limited. Regulators around the world have tried to deal with this issue and ICASA can learn how best to ensure ease of switching by consumers through reviewing, for example, Ofcom's interactions with BskyB over a protracted period in relation to such issues.

Consideration on the Effectiveness of Competition in the Market

Q14: Do you agree with the Authority's proposal to use the above factors in determining the effectiveness of competition? Please substantiate your answers.

38 We agree that the four factors listed by ICASA should form part of the determination of the effectiveness of competition (Discussion Document para. 6.2.1). However, we note that the list of factors to be considered is less exhaustive than the list provided in ICASA's Guideline for Conducting Market Reviews, which includes the following[11]:

- Assessment of relative market shares
- Actual and potential existence of competitors
- The level, trends in concentration and history of collusion in the market
- The overall size of each of the market participants
- Control of essential facilities
- Technological advantages or superiority
- The degree of countervailing bargaining power
- Easy or privileged access to capital markets and financial resources
- Dynamic characteristics of the market
- Economies of scale and scope
- The nature and extent of vertical integration
- Ease of entry into the market

39 In addition to evaluating the more complete list provided above, it is recommended that ICASA follow the method set out by the EU Commission w.r.t. electronic communications.[12] This entails a two-phased approach. The first phase entails conducting a three-criteria test to determine if a specific market should be regulated, where the following steps are evaluated cumulatively: (i) if there exist high and non-transitory barriers to entry of a structural, legal or regulatory nature; (ii) if the market structure does not tend towards effective competition in a relevant time horizon; and (iii) if the application of competition law alone would not adequately address the market failure(s) concerned. If a market passes the first phase (the three-criteria test), it needs to be assessed to determine whether any firm has SMP.

[11] Each factor is discussed in more detail in ICASA's *Guideline for Conducting Market Reviews*.
[12] European Commission Recommendation L 344/65 of 17 December 2007.

40 Importantly, with the assessment of market shares and dominance, it is important to be cognisant of the fact that high market shares do not necessarily equate to SMP, which we discuss in more detail in our response to Q23.

Q15: In your view, are there any competition concerns and is there a need for regulatory intervention in the market for the acquisition of non-premium content?

41 We note that no definition of non-premium content is explicitly provided, besides that it encapsulates all content that is <u>not</u> premium content. As such, we are of the view that it is all content besides sports, first-window movies, original content, international and local series.

42 It is noted that various submissions have been made to both ICASA and Government to the effect that DSTV has entered into exclusive agreements with community TV channels. This warrants an investigation into the type of exclusive agreements that are in place in relation to premium and non-premium content.

43 Benchmarking against international markets could assist further – for example, assessing what international channels are generally available to a range of different broadcasters (shoulder channels) versus only on an exclusive basis and assessing the situation here. An Audit of all exclusive contracts though could be illuminating.

Q16: Kindly comment on the nature of barriers to entry in the upstream market

44 Telkom agrees with the three barriers to entry discussed in the Discussion Document, namely the scarcity and cost of premium content, long-term exclusive contracts, and incumbency of special relationships. These barriers to entry in acquiring premium content play an important role in the viability of a broadcast network. As stated in South Africa's submission to the OECD roundtable discussion on television broadcasting: "The attractiveness of any particular

television broadcaster to potential viewers depends heavily on its ability to acquire content, particularly premium content.”[13]

45 It is noted that these barriers to entry are also present in the upstream market for non-premium content, but that it poses less of an impediment to success for broadcasters than is does in the case of premium content.

Q17: What in your opinion are the premium rights in the South African television sector? Who currently owns them?

46 Telkom agree with table provided on page 73 of the Discussion Document as a basis for this, but would also include:

1. TV series from the major Hollywood production houses – owned MultiChoice, or MultiChoice affiliated channels
2. Special Events i.e. FIFA World CUP, Olympics – Pay-TV rights owned by MultiChoice, noting further that with some of them they have gatekeeper rights

Q18: Kindly comment on the Authority’s proposal to use the number of rights as a unit of measure for market share calculation purposes. What other factors should be analysed to determine the dynamic character and functioning of the market?

47 We disagree with ICASA’s calculation of market shares as provided in Table 1 of the Discussion Document. Most importantly, ICASA provides no motivation for assigning the same weight to each right. Aspects that must also be considered include the length of time each of the rights is in place, the amount of content (whether in terms of minutes or number of events/movies) each right encompasses, and the popularity of the content, since more popular content will be more valuable in terms of attracting subscribers. These aspects will be more accurately captured by the value of the rights, as indicated by the amount that broadcasters are willing to pay to acquire it.

[13] OECD. 2013. Policy Roundtable: Competition issues in Television and Broadcasting. (p. 278)

48 Additionally, since ICASA defined separate markets for different types of content, it is unclear why it calculates market shares for combined content. We recommend that market shares be calculated for each of the identified markets in para 5.9.18 (a) to (f) in the Discussion Document.

Q19: Do you consider the nature and extent of vertical integration in subscription television likely to harm competition? Kindly elaborate on your answer.

49 Since Q24 relates to the nature of licensees’ vertical integration in the market and subsequent competition concerns, we do not discuss vertical integration w.r.t. any specific licensees in this answer. Rather, we limit our answer to the theory of vertical integration in the subscription television market and whether it is likely to harm competition.

50 According to Ofcom in its consultation document, “*Vertical integration can be beneficial, in that it can enable firms to exploit synergies between different layers of the value chain and therefore deliver efficiency improvements. However, vertically integrated firms are also likely to have an incentive to favour other parts of their business at different levels of the value chain; this could be detrimental to competition. Market power can enhance the ability of firms to act on these incentives.”*[14] More specifically, concerns that may arise from vertical integration include refusals to supply essential inputs to rival downstream firms, margin squeezes, raising rivals’ costs, exclusivity deals or monopsony in content acquisition.[15]

51 Since vertical integration can have pro- or anti-competitive effects, we agree that this should be an area of focus for ICASA in its investigation, specifically given MultiChoice’s prominent position in the market and its fully vertically integrated structure. Similarly, according to the OECD, “growing trends towards vertical integration in the broadcasting industry have raised concerns among both regulatory as well as competition authorities, some of which decided to launch

[14] Ofcom. 2007. Pay TV market investigation consultation document.
[15] OECD. 2013. Policy Roundtable: Competition issues in Television and Broadcasting.

public consultation to examine those concerns."[16] As such, we agree that there is a likelihood that vertical integration in the subscription TV market may harm competition. However, we note that ICASA's Discussion Document provides a very limited discussion regarding the nature and extent of vertical integration in the subscription TV industry. A more detailed analysis of the pro- and anti-competitive effects of vertical integration in the subscription TV market needs to be undertaken by ICASA before concluding that vertical integration is *likely* to harm competition. Of particular interest would be the effect of MultiChoice's position in the market.

Q20: Do you agree with the Authority's preliminary view that competition law alone is not sufficient to deal with possible market failures in the market for the acquisition of premium content?

52 Although ICASA does not provide much information on this point, it does state that "It is doubtful that competition law on its own can produce the desired market outcomes, hence the necessity of this inquiry to determine what the challenges are and what the possible remedies could be in an instance where it is found that competition is ineffective." We agree with ICASA in this regard.

53 More specifically, a market failure is not necessarily the result of anti-competitive behaviour. As such, competition law, which is backward-looking, cannot sufficiently address market failures on its own. Regulatory action is required to address structural problems in the market on an ex ante basis, especially given the rapidly changing landscape of the television broadcasting industry.

54 Importantly, sector specific regulation is likely also insufficient to address market failure. As such, the Memorandum of Agreement (MoA) between the Competition Commission and ICASA has the goal of fostering cooperation in this regard. We therefore agree with ICASA that competition law alone is not sufficient to deal with possible market failures in the market for the acquisition of premium content and that ex ante regulation as well as cooperation between the Competition Commission and ICASA are needed.

[16] *Ibid.*

Q21: Kindly comment on the above analysis of possible barriers to entry at retail level of the market. What other barriers to entry are prevalent in the market?

55 We generally agree with the barriers to entry at the retail market detailed in the Discussion Document. For smaller broadcasters and new entrants, the substantial capital required to acquire premium content might be prohibitive, with MultiChoice having exclusive rights to much of the available premium content and the capital to outbid the smaller broadcasters and new entrants, leaving the latter unable to induce consumers to switch. As such, smaller broadcasters and new entrants have to find other ways of convincing consumers to incur the switching costs. Strategies may include low subscription fees (especially just after entering), free or discounted set-top boxes (an important aspect of the switching costs due to the current lack of interoperability), and more. This places an additional burden on the smaller broadcasters and new entrants, originally stemming from the barriers to entry in the upstream market and feeding through to the downstream market.

56 What the Authority fails to mention is the potential hesitancy of consumers to incur the switching costs after seeing the new entrants Astrasat fail in 1998 after less than two years of operations,[17] and TopTV (now StarSat) going into business rescue in 2012 after launching only in 2010.[18] Consumers may deem it more prudent to stay with their current broadcaster instead of investing in new set-top boxes and satellites (if necessary) only to have the new entrant fail, making their investment worthless.

57 We note that while the Authority mentions the bundling of premium and non-premium content – which we agree may pose a barrier to entry – it does not consider the bundling of different platforms of accessing content. For example, certain DStv subscribers can access content on satellite television as well as online and on mobile devices via their streaming services (e.g. DStv Now[19]) Additionally,

[17] Fourie, P.J. ed., 2001. Media Studies: Institutions, theories, and issues (Vol. 1). Juta and Company Ltd. (p. 20).
[18] https://www.businesslive.co.za/bd/companies/telecoms-and-technology/2012-11-01-toptv-opts-for-business-rescue/
[19] https://www.dstv.com/topic/about-dstv-now-20160909

free access to Showmax[20] (subscription video on demand) is bundled with the DStv Premium package, access to BoxOffice is bundled with certain packages as well as the catch-up service (VOD). DStv also offers BoxOffice (transactional video on demand – TVOD) to anyone in South Africa, although DStv Premium, Extra or Compact subscribers pay a reduced fee to rent a New Release move online. In addition, only these subscribers have access to BoxOffice on a personal video recorder (PVR) device.[21] All of these bundled products make a DStv subscription more attractive than subscriptions from broadcasters that do not offer it. For small broadcasters and new entrants, the need to offer all of these services in order to be able to successfully compete increases the capital requirement substantially.

58 While the Discussion Document provides a short description of some regulatory barriers, it does not refer to the digital migration and the regulatory barriers that come along with it, for example, regarding set-top boxes.

59 Finally, we point out that long-term agreements between broadcasters and *subscribers* are not mentioned by the Authority. For example, DStv (the incumbent) offers "Price Lock" for Premium subscribers. This includes a DStv Explora 2 (with DStv Wifi Connector), DStv Premium subscription and fixed access fee for 24 months, as well as installation with DStv Smart low noise block (LNB).[22] Consumers may be hesitant to switch when they are still in the 24 month period and would need to pay a price that has increased with inflation, etc. to a different broadcaster. In this situation incumbency provides a distinct advantage and can pose a barrier to entry for potential new entrants.

Q22 (renumbered from repeat of Q21 in Discussion Document): Is the Authority correct to use subscriber numbers as a unit of measure for market share calculation purposes? How else would you calculate market share at this level? What other factors should be analysed to determine the dynamic character of the market?

[20] https://www.dstv.com/en-za/news/dstvnow4newbies-showmax-20170912
[21] https://boxoffice.dstv.com/help
[22] https://www.dstv.com/commerce/paymentplan/pricelock?gclid=Cj0KCQiAjO_QBRC4ARIsAD2FsXMJVQ-KAx0_y6zCNgQr8V_MyNkiwxSe6yb66inGyrEKxOMlWAmHCWsaAkwEEALw_wcB

60 We agree that subscriber numbers should be used for market share calculations at this level. However, we recommend that the Authority does not limit its analysis to only this measure. Specifically, it should also consider subscription share of revenue and advertising share of revenue.

61 Although subscriber numbers provide an unbiased measure of market share calculation, evaluating this alongside revenue market shares may present a useful picture of the dynamic character of the market. For example, if one firm has a revenue market share that exceeds the growth in subscriber number share, then this indicates that they are generating greater revenue per subscriber in relation to the other competitors in the market. This will not be clear from only analysing subscriber market shares.

62 We note that the market shares calculated in Table 3 of the Discussion Document refer to the entire subscription TV market, although separate markets for basic and premium subscription TV are defined. It is therefore recommended that ICASA re-calculate the market shares accordingly. A further analysis which could provide insight into the dynamic functioning of the market is to investigate the subscriber churn between basic and premium options (within DStv's bouquets).

Consideration of Licensees with Significant Market Power

Q23: Do you support the Authority's proposed approach in identifying players with significant market power? Kindly elaborate.

63 Although we note the importance of calculating market shares in the determination of dominance (as per the Competition Act), we disagree with the notion that "a licensee has significant market power if, among other things, it is dominant, within the meaning of the Competition Act", as stated in the ECA. This statement implies that having high market shares bestows market power upon a firm. This market power offers the firm in question "the ability of a firm to control prices, or to exclude competition or to behave to an appreciable extent independently of its competitors, customers or suppliers."

64 As stated at the ICN conference in 2006 by the ICN Working Group on telecommunications, "Overall, defining telecommunications markets is largely case specific, depending on both the particular facts and competition concerns at hand."[23] As such, it is inadvisable to make a priori assumptions regarding the structure of a market and the existence of market power. Such a determination would place significant weight on the market share calculations, which is specifically problematic given our disagreement with the Authority's method for calculating market shares for the content market (as discussed in Q18). As such, making a determination on whether a firm has SMP given its market shares is essentially flawed.

65 Economic theory suggests that even if a firm has high market shares, this may not translate into SMP. The European Commission[24] states that an undertaking has SMP if it enjoys a position of economic strength that affords it the power to behave independently of competitors, customers and consumers (to an appreciable extent). Furthermore, it is pointed out that the existence of a dominant position cannot be established on the sole basis of large market shares.[25] As such, it is recommended that the National Regulators should undergo a thorough analysis of the economic characteristics of the relevant market before concluding on the existence of SMP, including amongst other factors, the presence of barriers to entry, the absence of potential competition, the absence of or low countervailing power, economies of scale/scope, vertical integration and barriers to expansion.

66 As such, we find that although market shares are an important factor in determining whether a firm has SMP, the Authority must assess several other factors that may limit the extent of a firm's market power.

Q24: Does the nature of any licensee's vertical integration in this market raise any competition concerns?

[23] Hodge, Thornton, Sibanda & Carrim. 2006. The state of competition in the telecommunications sector in South Africa.
[24] Commission guidelines on market analysis and the assessment of significant market power under the Community regulatory framework for electronic communications networks and services (2002/C 165/03)
[25] Ibid, para 78.

67 We note that MultiChoice is the only player in the South African subscription broadcasting industry that is fully vertically integrated and as such should be sufficiently investigated to identify any potential competition concerns.

68 At the time of Ofcom's investigation into pay TV, Sky was the dominant broadcaster. In Ofcom's consultation document, it is stated that Sky's unique position in the pay TV industry creates a vicious circle that allows Sky to engage in conduct which is harmful to competitors and consumers. It was suggested that the key features of Sky's position are (i) its vertical integration; (ii) its upstream bottleneck (more specifically, its grasp of attractive content that it purchases on an exclusive basis); and (iii) its downstream bottleneck, which includes its gatekeeper status for the satellite platform (w.r.t. EPG listings and conditional access charges) and its majority share of the retail customer base.[26]

69 Ofcom considered whether vertically integrated operators have an incentive to foreclose potential new retailers and/or platform operators by denying them content. It stated that a provider appears to face a trade-off between an incentive to supply content to all retailers and an incentive to rather favour its own retail operation.

70 From the Ofcom consultation document, four concerns were raised w.r.t. inter-platform competition[27]:

1. There may be significant barriers to entry into the market for premium wholesale channels. These are primarily due to the way in which content rights become contestable only on a staggered basis. These barriers to entry may be exacerbated by the presence of a vertically integrated incumbent, which has an <u>incentive to control access to downstream markets</u>, albeit its ability to do so may be restricted by regulation.
2. Although a vertically integrated incumbent may supply content to established retail competitors, in order to generate wholesale revenues, it may have the ability and <u>incentive to reduce the quality of what it supplies</u>,

[26] Ofcom. 2007. Pay TV market investigation consultation document, para 6.58.
[27] Ofcom. 2007. Pay TV market investigation consultation document, para 6.77.

in order to strengthen its own retail offering relative to its competitors. We acknowledge however that such reductions of quality may also arise naturally, due to technical inter-operability issues.

3. A vertically integrated incumbent may have the <u>incentive and ability to foreclose</u> potential new retailers by denying them content.
4. The prevalence of vertical integration between retail and platform operations may cause this problem to extend to <u>foreclosing the possible development of new platforms</u>.

71 We note that the same concerns arise in the South African market w.r.t. MultiChoice due to its dominant position in the market as a fully vertically integrated firm.

Possible Pro-Competitive Licence Conditions

Q25: Kindly comment on each of the remedies discussed above and indicate their possible applicability in the South African context

- **Shorten exclusive contracts**

72 This is in line with best corporate governance in South Africa and will allow new players a fair opportunity to bid for and acquire key rights. However, unless this is linked to requiring an open and fair bidding process, it will not alone address the problems associated with long term contracts and relationships between incumbents and rights holders. The length of time for such exclusive rights would also probably ideally be negotiated with both content providers and rights holders.

73 What would be regarded as a fair period for exclusive rights will probably vary – depending on the rights (as in Europe where the maximum proposed is five years but some sporting codes are encouraged to limit exclusivity to three year periods).

74 Telkom therefore suggests that ICASA begin discussions with the competition authorities on how they can jointly approach this – as well as ensure it engages with rights holders the so that this is holistically addressed. Some of the other conditions imposed by the European Commission on sports rights holders are also worth considering – such as a bar on automatic renewal of contracts.

75 ICASA should also investigate if it is correct as stated in one submission on the questionnaire that MultiChoice may have on occasion bought both first and second window movie rights to extend its exclusivity period. Such behaviour should be analysed in more depth.

- **Introduce unbundling and rights splitting**

76 These two proposals by ICASA (unbundling and right splitting) are considered together as Telkom is of the view that unbundling is only effective as a remedy to address unfair competition if used together. They have been used effectively in several jurisdictions as ICASA indicates in the Paper. These conditions are generally imposed on rights holders (e.g. sporting codes) and therefore would need the cooperation of the competition authorities and rights holders.

77 Note that ICASA could also explore the approach proposed by the Office of Communications in the UK of, for example, limiting the number of exclusive contracts that a licensee with significant market power may enter into with major Hollywood movie houses.[28]

- **Impose wholesale must** o**ffer**

78 Telkom fully supports the imposition of wholesale must offer in the South African context. The OTT market is not yet developed enough to address the issues and Telkom does not expect it to develop rapidly. This view is confirmed by the projections in the latest Pricewaterhouse Coopers (PwC) Entertainment and Media Outlook (2017-2021 report) which states that South African total revenues for television amounted to 40.9 billion in 2016 (including pay-TV subscriptions, physical home video, internet video, public licence fees, and advertising) and is expected to rise to R51.2 billion by 2021 according to PwC projections:

[28]Note Ofcom proposed that the exclusive contracts with movie houses be investigated by the competition authorities in the UK who initially agreed with the regulator after an investigation but subsequently decided that OTT player such as NetFlix sufficiently countered the threat to fair competition. https://www.whathifi.com/news/competition-commission-rules-out-action-against-bskyb

> *"Satellite has had a monopoly on pay-TV subscriptions, but IPTV and pay-DTT established a minor presence in 2016. By 2021 satellite's dominance will have been squeezed but the sector will still account for 93.6% of subscriptions."*[29]

79 However, as with Ofcom, Telkom would propose that ICASA regularly review this, considering the development of new content services. The approach to regulation of this will have to be carefully considered by ICASA to ensure capacity to impose it.

80 Telkom notes that much of the complaint lodged by StarSat with the CC deals with negotiations between it and MultiChoice in this regard. While ICASA, however, would be developing *ex ante* regulation, it might be useful to consider the views of the Commission on this matter.

Q26. ICASA notes that one way of introducing increased competition may be to place an obligation on a dominant player to open their distribution to other subscription operators. Is the above proposal feasible in the South African market context?

81 Ofcom seems to have successfully addressed concerns about access through such interventions and Telkom supports the notion that ICASA explore this further.

Q27. Kindly comment on competition implications of set top box interoperability.

82 As noted in response to earlier questions, access to the hardware and software of the dominant player and interoperability are crucial to ensuring ease of switching by subscribers – allowing new operators to target both existing and potential customers. This issue has been fought by subscription broadcasters in many jurisdictions (notably BskyB in the UK over many years), but ways have been found to address the consumer issues.

[29] https://businesstech.co.za/news/media/200062/dstv-is-not-going-to-be-threatened-by-netflix-or-amazon-any-time-soon-pwc/

83 The solution seems to deal with this practically, but ICASA should explore which would work best in the South African context and be the quickest and simplest for it and operators.

Q28. What other conditions could be imposed on any licensee having significant market power to remedy market failure in the relevant markets?

84 ICASA should also consider if there are any concessions it can make for new licensees to enable them to better compete. It is noted that M-Net (and therefore DSTV) were given many such advantages over the years – including, for example, guarantees that no other pay TV operator would be licensed for some period and marketing opportunities such as Open Time on SABC channels. Opportunities for marketing on the dominant player's platform could be explored – or a creative form of 'open time' on a DTT channel. ICASA could also consider relaxing key obligations such as South African content until the licensee has some influence (i.e. on signing up a key number of subscribers).

85 ICASA should also, as noted in the introduction, review its own regulations and practices to see if it has (as charged by some submissions) contributed towards unfair competition in television. For example, the introduction of a regulatory regime for IPTV as indicated in the 2007 ICASA Position Paper could have assisted in resulting in more diversity for audiences.

86 Finally, Telkom would like to note, as it has highlighted in the introduction to this submission, that this inquiry is limited as it looks only at the effects of dominance on the subscription television market itself. Ideally this should be dealt with holistically and ICASA should also look at how it addresses for example the undue access by DSTV to advertising which threatens FTA television. Could repeat how should look beyond impact on the subscription television market alone – but also on FTA etc. and then what it can impose to limit access to advertising – or insure no predatory pricing.