Vodafone and Sky: 'veteran lawyer' needs new reading glasses

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Speed Read

On 19 August, an unnamed "veteran lawyer" wrote in the National Business Review that submissions to the Commerce Commission opposing the Sky – Vodafone merger had "failed to land any killer blows".

We think this "veteran lawyer" needs new reading glasses.

In this article, we respond to his points, highlight what the "veteran lawyer" omitted to mention, and explain why the Sky – Vodafone merger will lead to competition and consumer issues in New Zealand, largely due to the problem of key content.

These negative effects are evident from statements made by Sky and Vodafone themselves.

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The Detail

In a recent version of NBR, an unnamed "veteran lawyer" dissed submissions to the Commerce Commission opposing the merger. Surprising stuff, so we will deal with his points, relying only on what he should have read in the submissions, but doesn't refer to, and mostly from what Vodafone and Sky themselves say. From the mouths of babes…

And that theme of not referring to what's been said elsewhere is quite a theme in the Vodafone and Sky application too. For example, you'd think there is no problem for competition and consumers. Quite the opposite.

Vodafone says overseas, as to key content, of which live All Black tests is an example: *"Key content is by its nature exclusive, or put simply a monopoly input, which in any other scenario would be subject to appropriate regulation."*

In the New Zealand application, they say: *"Pay TV offerings do not drive substantial changes in broadband share."*

But Vodafone internationally says the opposite, among the hundreds of pages it has produced opposing pay-TV and telco combos using key content, such as they seek here:

> *"As consumers are increasingly attracted to bundled offers of TV, broadband, fixed and mobile voice services, the control of that exclusive content will increasingly steer their overall purchasing decisions."*

None of the many Vodafone words – outlining competition and consumer harm due to what Vodafone and Sky seek to do here – are referred to in the Vodafone and Sky applications. Vodafone even said internationally but not here in New Zealand, when submitting on the negative effects:

"Ignoring the effects of 'key content' across wider and traditionally unrelated markets, such as mobile or broadband only customers, will have an enduring and irreversible effect, as the focus moves to TV bundled competition."

Vodafone from afar would see this merger producing "enduring and irreversible" negative effects in New Zealand.

Vodafone Global's main concern, where pay-TV is becoming so important in telco bundles, is that key content ("monopoly inputs" as it says), are bundled in triple and quad plays (voice, broadband, fixed line, mobile). Triple and quad plays are a big part of the Vodafone and Sky proposition, as they say.

The problem is that competitors cannot replicate the key content part of the bundles and, as Vodafone states internationally, that leads to consumer and competition harm as markets are distorted. This is a variant on a problem well known to lawyers in this area. Re-monopolisation of telco is a risk here, where the Chorus and Spark split was designed to stop that.

Applying that to the veteran lawyer, he says "*the power of the triple or quad play seems like an idea from the 2000s or even the 1990s.*" Well, Vodafone internationally, for one, doesn't agree with him, given what they've said many times up to 2016. As above, the problems are alive and well.

Next, the Vet says video on demand (VOD) services such as Netflix are hitting Sky TV's customer base, so that's a competitive constraint. Well, you wouldn't think so from Vodafone's international utterings. You also wouldn't think so from what the Sky chief executive has said in June 2016 when saying there is "little crossover" between viewers of Sky's VOD service (NEON) – which the applicants say is just like Netflix, Lightbox, etc –and the Sky TV monthly service. The Sky CEO says NEON is watched by viewers in their 20s and Sky TV is watched by viewers around 50. That's backed up by US and UK data, showing the share in the pay-TV market for VODs such as Netflix is only around 5% so that the US regulator, for example, concluded Netflix had little competitive constraint on monthly pay-TV. Additionally, that regulator said that monthly customers tended to buy Netflix on top of that service, not as a replacement. In other words, VOD has limited competitive constraint on monthly Pay TV.

The Vet says others like Spark and TVNZ can bid for and win the sports rights. But each key sport is locked in with Sky for between four and eight years. All lawyers in this space know the commission generally looks only two years out when assessing the position – sometimes a little more but rarely if ever four to eight years out – so that is irrelevant. The damage is well done by four to eight years away.

The Vet also concludes the submitters are wrong in saying that, if the deal didn't go ahead, Sky would encourage wholesale supply of content to competitors, which would be a better competitive outcome than if the merger goes ahead. He says that, if the deal didn't go ahead, Sky instead would supply broader and better-quality services online direct to consumers and not via wholesaling to telcos. However, if the Vet's right, the merger going ahead would still substantially lessen competition (which is the legal test), relative to Sky selling online direct to consumers, if the merger does not go ahead. For example, in that "without merger" scenario, the pay-TV/telco anti-competitive bundling opportunities, leading to bad outcomes as noted by Vodafone offshore, disappear. So, the same outcome.

OK, we act for parties opposing the merger so "We would say that". That's why we have focused on the straightforward, and what Vodafone and Sky have actually said.

There is plenty more besides.

Vodafone provided some initial comments to the Commission, saying that what it said overseas doesn't apply here. More detail is to follow, they say. They focus on the fact that we have structural separation of Chorus and Spark so the problem doesn't arise here. That is not correct and in fact the position is worse here given more concentrated Pay TV and also mobile markets.

The bottleneck is the key content and that is not solved by more competition in fixed line. To the contrary, the main idea of leveraging key content is to get around that very competitiveness, by getting dominant control in otherwise competitive markets, via an input exclusively held by Vodafone and Sky. This is done by having an input – here, key content – in triple and quad play bundles containing services that are otherwise competitive. The bundle cannot be replicated by competitors, and economists and regulators focus on the anti-competitive effects of such bundles. As does Vodafone in considerable detail and on multiple occasions. The former dominance of Telecom – fixed by structural separation – crops up again by a different path.

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