

# **Consumers'** Association

## **Restricted View**

**The Rights and Wrongs of FA Premier League Broadcasting**

## **Restricted View: The Rights and Wrongs of FA Premier League Broadcasting\***

by

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## Foreword

Consumers' Association commissioned two leading experts in the field of the economics of sports and broadcasting, Professor Stefan Szymanski and Dr David Harbord, to review the current structure of the pay-TV FA Premier League deal in the UK.

We commissioned this work for the simple reason that this market is of enormous importance to a very large number of consumers. It is also a market that has been the subject of review by a number of competition authorities, and indeed is currently under review by the European Commission. Before taking a view of the issues we felt compelled to have an expert view of the deal that focused the arguments on what the current Premier League-BSkyB deal means to consumers and ordinary fans. We were also keen to review the current arrangements in the light of the continuing instability in the finances of football clubs with a view to ensuring that no view we took would further exacerbate these problems.

While the views and conclusions of the authors are their own and were arrived at independently, Consumers' Association thinks that the report highlights a number of key issues for regulators.

### **1. The FA Premier League-BSkyB exclusive deal is anti-consumer, anti-fan and anti-competitive**

For a fan to watch a Premier League match on TV there will soon be no choice but to subscribe to BSkyB. All Premier League live games are exclusively sold to one Pay-TV broadcaster. This increases costs for consumers and restricts choice.

### **2. The current way of collectively selling live games is anti-club**

The FA Premier League is, in the words of the authors, an 'inefficient cartel'. Collective selling as it is currently controlled stops individual clubs selling live games that are not in pre-set packages. This stops them earning money by selling their games to, for example, a local commercial broadcaster. The current deal is anti-club.

### **3. Collective selling does not protect the small clubs**

The Premier League cartel justifies its anti-competitive deal on the basis of a limited redistribution of funds between clubs. We agree that this is a laudable aim. However, it cannot be used to justify anti-competitive and anti-fan abuse of market power. Indeed collective selling, with a ban on individual deals for games outside the packages, makes the financial position of individual clubs more precarious and prone to sudden shocks (like the ITV Digital collapse). The Premier League should be compelled to find a less market distorting way of redistributing money. For example, it could share gate money more evenly or establish a common fund for merchandise sales. There are enough examples from other countries and sports to provide a more stable, just and effective solution.

However, we recognize that the clubs may find it difficult at first to deal with a new, freer environment, and thus some form of transitional regime may be appropriate.

It is clear to us that the current exclusive deal between the FA Premier League and a single pay-TV broadcaster, BSkyB is as anti-competitive as it is anti-consumer. The key question must be what can be done to limit its negative impacts. We think that there are three workable solutions:

#### **1. No one broadcaster should have exclusive rights to all games**

The current arrangement allows one inefficient cartel of clubs to sell all their broadcast packages to one efficient monopoly broadcaster. This must be ruled illegal. At a bare minimum the least attractive Bronze package of games either side of the Saturday 3pm window should be stripped from the current deal and sold to a free-to-air broadcaster.

**2. Individual clubs should be allowed to sell games not in a pre-set package**

The financial viability of all clubs, particularly the smaller ones, will be enhanced if they are free to sell the rights to broadcast those home matches that are not in a pre-set package of live games.

**3. The Premier League should create a less market distorting means of redistributing income**

Redistributing money between the richest and poorest Premier League clubs is a laudable aim. It cannot, however, be used to justify such a gross abuse of market power as this exclusive and restrictive broadcasting deal. Other countries and sports show that collective selling of merchandise and more equitable distribution of gate takings can help ameliorate funding inequalities.

It is clear to us that the current FA Premier League-BSkyB exclusive deal cannot be allowed to stand. The European Commission has an ideal opportunity to stand up for Britain's football fans and consumers and rule the current deal illegal. The twin pincers of the inefficient Premier League cartel and efficient monopoly broadcaster cannot be allowed to rig the market against the interests of consumers and the clubs themselves.

We think that this paper presents an unanswerable case that this deal is bad for consumers, bad for all fans, bad for clubs and bad for the long-term financial viability of the national game. We also think that this paper presents some clear avenues that the European Commission can explore in making this market work better for all players in this enormously important market.

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## Section 1: Introduction

In December 2002, the European Commission issued a 'Statement of Objections' concerning the FA Premier League's sale of live football broadcasting rights in Britain. Particular concern was expressed at the FA Premier League's collective selling arrangements, which the Commission argued were tantamount to price-fixing.<sup>1</sup> According to the Commission, joint selling - when coupled with exclusivity - means that only big media groups can afford the acquisition and exploitation of the bundle of rights. This leads to higher prices and the shutting out competitors from key content. In turn this means that football fans are also potentially harmed since they are offered less football on TV, or no coverage at all if they do not subscribe to pay-TV.<sup>2</sup>

It is widely accepted that live sport is among the most attractive programming available to either free-to-air channels or pay-TV broadcasters. The significance of some sporting events, such as the soccer World Cup, the Wimbledon tennis championship and the Olympic Games is so great that legislators have forced the rights owners to ensure that they can be viewed on free-to-air television, rather than obliging consumers to take out a subscription to watch them. In the UK, despite the fact that there are few forms of sports programming that are as attractive to consumers<sup>3</sup>, Premier League soccer is not protected in this way.

Since the formation of the Premier League in 1992 the right to broadcast live Premier League football matches has been offered in periodic auctions occurring every three or four years.<sup>4</sup> After the bids are received, the Premier League members (the twenty clubs that belong to the league at the time the auction takes place) vote on which offer to accept. The sale is managed collectively by the Premier League, with a different auction format being adopted each time the rights have been sold. In every auction the rights to broadcast live Premier League games have been sold exclusively to a single TV broadcaster, BSkyB.

In June 2003 under pressure from the European Commission the FA Premier League changed the format of its auction for the broadcasting rights to live Premier League games. It did this by splitting the TV rights into three packages: a Gold and a Silver package with 38 games each, and a Bronze package of 62 less valuable games.<sup>5</sup> Further pressure from the Commission in July 2003 resulted in a split of the Bronze package into two equal-sized packages. The Commission's purpose was to ensure that there would be genuine competition for the packages, and that not all of the live rights would end up under the control of single pay-TV broadcaster - in this case BSkyB.

However, all of this was to no avail. In August the FA Premier League announced that BSkyB had again secured all of the live rights for a price of £1.024 billion, compared with the £1.2 billion it paid for 66 live games per season under the previous deal. Reportedly there had been no competition at all for the Gold and Silver packages, and very little for the Bronze packages<sup>6</sup>. In October, BSkyB was subsequently awarded the rights to broadcast live FA Premier League matches over the internet, and also won the rights to broadcast the 242 games not covered by its £1.024 billion deal on a delayed basis, for a reported additional £60 million.

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<sup>1</sup> The FA Premier League sells packages of media rights on behalf of the League clubs to television companies in Britain and Ireland on an exclusive basis. Under the arrangements, clubs are prevented from selling any rights on their own, even those that are not included in the packages. In practice, this has meant that until recently only 25% of the Premier League matches have been broadcast live. See the Commission's Press Release, 20 December 2002, "Commission opens proceedings into joint selling of media rights to the English Premier League."

<sup>2</sup> Commission also noted that lack of competition may limit the packages of rights available for new media technologies, such as the internet and 3G mobile phones.

<sup>3</sup> See Monopolies and Mergers Commission (1999) for evidence

<sup>4</sup> Binmore and Harbord (2000) discuss previous auctions

<sup>5</sup> The Gold package consisted of 38 games to be played on Sunday at 4pm, the Silver package of 38 Monday night games, and the Bronze package of 62 games on Saturday at kick-off times of 1pm and 5.15pm.

<sup>6</sup> The Observer, 7 September 2003, "EC to probe Premier 'price fix'."

It is hard to see how the Premier League's recent auctions will have assuaged the Commission's concerns, even though the number of live matches sold has increased from 28% to 36% of the matches played. In 2001 the Commission had raised similar objections to UEFA's collective selling arrangements for the Champion's League competition. Under the UEFA deal<sup>7</sup>, Champion's League live broadcasting rights are also split into packages. However, the split is done in a way that prevents any single broadcaster from acquiring all of the packages, typically by splitting the 'free-to-air' and pay-TV rights into separate packages. In addition, individual clubs can auction off any unsold rights, thus avoiding the recent FA Premier League debacle.<sup>8</sup>

BSkyB has now won the exclusive rights to broadcast live Premier League football in four consecutive auctions beginning in 1992, and the European Commission's interventions have so far had no effect. In September, Competition Commissioner Mario Monti declared that the deals were bad for consumers and, if anything, strengthened BSKyB's monopoly position in the broadcasting of premium sports content in Britain, an issue which has already been at the heart of numerous UK competition authority investigations.<sup>9</sup> So what, if anything, should the Commission do now?

In this paper we focus on two key competition problems created by the FA Premier League's collective selling arrangements and suggest possible remedies which in our view may work better than anything so far proposed by the Commission. Our approach is to identify the sources of consumer welfare losses created by the FA Premier League's joint selling and exclusive contracting arrangements, and to identify potential solutions to those problems.

The first issue is the restriction of choice created by collective selling itself. As noted by the Commission, the FA Premier League acts as a tight cartel which sells the rights to the matches played by all of the Premier League clubs and shares the revenues between them according to a fixed formula. Individual clubs cannot sell the rights to the matches they play on their own behalf, even if the matches will not otherwise be broadcast. This has resulted in nearly two thirds of all FA Premier League matches not being made available for live broadcast, including some of those which are most attractive to viewers<sup>10</sup>.

In a free market, on the other hand, clubs would sell these rights to other broadcasters (either free-to-air or pay TV). In addition, the fact that the live rights are sold in large packages has meant that they can only be sold to a pay-TV broadcaster, since free-to-air broadcasters face capacity constraints and can broadcast a limited number of live matches per season. This represents a significant additional restriction on the availability of matches to consumers.

In the paper we estimate the economic cost to consumers of these restrictions using data on matches broadcast. The relative popularity of matches is relatively easy to forecast. Analysis of viewing data shows that the most popular games involving Premier League teams each season attract between two and three million viewers on Sky and around 10 -13 mn on free-to-air TV (FA Cup matches). Moreover, each additional game broadcast on each platform attracts an audience around two per cent smaller (on Sky) or six per cent smaller (on free-to-air) than the previous game. We can use these estimates to calculate the potential viewership if a less restrictive set of packages were available. We estimate that the cost to consumers arising from their inability to watch their programming of choice is in the region of £1 bn per year.

One remedy for this problem is to simply strike down the agreement between the Premier League clubs that prevents them from selling individually what they agree *not* to sell collectively. This highlights the point that the problem is not collective selling *per se*. Indeed some collective

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<sup>7</sup> See Commission Decision, COMP/C.2-37.398, "Joint selling of the commercial rights of the UEFA Champions League," 23/07/ 2003.

<sup>8</sup> One problem for the Commission, however, is that a "UEFA-style" approach is unlikely to work well in the current UK environment. With the collapse of ITV Digital in April 2002, and the financial troubles of Telewest and NTL, there may now be too few bidders left in the game willing to bid for rights.

<sup>9</sup> For example, the Competition Commission's investigation into BSKyB's takeover bid for Manchester United, 1998/9, the Office of Fair Trading's 1999 Restrictive Trade Practices Court case against the Premier League, and the Office of Fair Trading's Competition Act investigation into BSKyB, 2001/2002.

<sup>10</sup> For example, about one third of the matches of top teams such as Manchester United, Arsenal and Chelsea are not offered for live broadcast.

selling may be welfare enhancing if it gives consumers access to attractive packages of games. What cannot be in the public interest is the rule that restricts clubs from selling attractive individual matches even when these matches are not included in the collective packages.

The second issue focuses on the nature of the exclusive contracts for broadcasting rights, such as for live Premier League matches, and how these are exploited by BSkyB in the UK pay-TV market. As noted by both the Monopolies and Mergers Commission and the Office of Fair Trading, BSkyB is a virtual monopolist in the provision of 'premium' programming content in Britain, having acquired the exclusive broadcasting rights to practically all of the Hollywood studios' first-run films, and to the majority of the major sports events available to pay-TV. BSkyB purchases these rights under exclusive contracts with upstream rights sellers and then resells the programming to its downstream competitors (i.e. the cable companies) for variable, or per-subscriber, fees. The implications of these contractual arrangements for competition and consumer welfare in the pay-TV market are key to understanding the issues in the Commission's current proceedings against the FA Premier League.

For example, BSkyB acquires the exclusive rights to broadcast live Premier League matches for a lump-sum fee, and sells the programming to its own subscribers and to its competitors (via sales of its Sky Sports channels) for a per-subscriber monthly fee. Resale of the rights for per-subscriber fees allows BSkyB to prevent the dissipation of monopoly profits by increasing the marginal cost of its competitors, that is by *raising rivals' costs*, while simultaneously increasing the *opportunity cost* of serving its own customers. The resale price thus acts as an effective mechanism for both weakening downstream price competition and extracting consumer surplus from the premium product, depriving consumers of the benefits of competition.

If instead the premium programming were sold by downstream firms who faced "uninflated" marginal costs, i.e. if each firm acquired the *nonexclusive* rights for a lump-sum fee from the rights seller, fierce downstream competition to sell the programming to consumers would result in these profits being competed away, and the benefits captured by consumers.

These observations suggest that the Commission may be tackling the 'wrong kind' of exclusivity in adopting a 'UEFA-style' approach to the Premier League case. Splitting the broadcasting rights between multiple broadcasters does not necessarily address the problem of monopolistic pricing. In contrast, a ban on the sale of exclusive rights (that is, forcing the FA Premier League to sell its rights nonexclusively to each broadcaster or platform), would ensure that each pay-TV broadcaster had access to the programming on the same terms as its competitors. Consumers would then benefit from competition to 'sell' the programming in the downstream TV market<sup>11</sup>.

In the following sections we expand on the economic implications of these issues. Section 2 argues that the FA Premier League is an inefficient cartel, restricting output and consumer choice. Importantly it provides an estimate of the cost imposed on consumers by these restrictions in terms of the viewership lost and the value of that viewership to consumers. Section 3 discusses the nature of competition in the pay-TV market and how this is distorted by the sale and exploitation of exclusive rights. Section 4 concludes.

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<sup>11</sup> The nonexclusive sale of rights is not as novel as it may appear, and has occurred already in the sale of FA Premier League pay-per-view rights. There are also many cases where the competition authorities have intervened both to prevent the use of an exclusive distribution channel to raise prices and restrict consumer choice, and to force the owner of a monopoly right to create a competitive distribution system.

## Section 2: Collective Selling, Inefficient Cartels and Welfare Losses from the Restriction of Choice

As noted by the European Commission, the FA Premier League acts as a tight cartel which sells the rights to the matches played by all of the Premier League clubs and shares the revenues between them according to a fixed formula. Individual clubs cannot sell the rights to the matches they play on their own behalf, even if the matches will not otherwise be broadcast.

In defence of its output restriction, the FA Premier League has long argued that any increase in revenues from selling additional rights would be offset by loss of gate receipts at the matches as attendance would fall. Yet the history of the live TV football in recent years has been one of increasing live coverage and increasing attendance at matches. Attendance at League matches in the top division of English soccer declined from a peak of 17.9m in 1948/49 to a post war low of 7.9m in 1989/90. Since that date attendance has increased by 65 per cent to over 13m. Live top division football was not broadcast in the UK until 1983, and until the creation of the FA Premier League a limited number of matches were shown. As the number of matches broadcast has increased over the years, so has attendance at live football. By the end of the 1990s most Premier League games were in fact sell-outs, suggesting that unsatisfied demand existed even when matches were broadcast live. Thus, if anything, it would appear that live broadcasting has stimulated match attendance rather than undermined it, probably because live coverage provides such an attractive showcase for clubs.

Nor can it be said that this increase in attendance has been at the expense of clubs in the lower divisions. Attendance in these divisions fell more or continuously after the Second World War until the mid 1980s, since when it has recovered significantly. Since the advent of the Premier League attendance at lower division football has risen from 10.6m to 14.8m, an increase of 40 per cent.

The issue of the impact of broadcasting on match attendance has been the subject of a study by Forrest et al. (2003) who provide econometric evidence to show that live broadcasting has a negligible impact on attendance at the matches shown. They show that the additional revenues generated by selling more broadcasts would likely far exceed any plausible opportunity cost. If this argument is correct, the FA Premier League is not only restricting consumer choice it is also clearly failing to maximise the joint profits of its member clubs.

One of the reasons for this apparent short changing of its own members is that the FA Premier League's own distribution formula pays only 25 per cent of broadcasting income to home teams - a sum which the clubs do not consider large enough to justify the risk of lost gate receipts. In effect, the FA Premier League is running an inefficient cartel<sup>12</sup>. This conclusion implies that the European Commission should be wary of any remedy that preserves the right of the FA Premier League to control which matches are and are not broadcast.

### Welfare Losses from the Restriction of Choice

Since 1992 the Premier League has sold the rights to the live broadcast of their matches exclusively to BSkyB. Consumers have suffered from this arrangement in two ways:

- **Subscriber fees:** to watch live Premier League soccer consumers have had to subscribe to a pay-TV service that carries Sky Sports (either BSkyB or a cable service). Because of the construction of programming bundles they have been forced to purchase a bundle of content including much more than live Premier League soccer, whether desired or not simply to access the football matches.

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<sup>12</sup> See also Ross and Szymanski (2000).



- **Limited choice:** even after subscribing to pay-TV, they have been offered only a very limited selection of the Premier League games played

Clearly these arrangements have restricted the choice and access of consumers. If matches were shown on free-to-air TV, or if more matches were shown on pay-TV, then consumer welfare would have been higher. How much higher we can estimate by calculating:

- (a) the number of viewers that would have watched live football if all matches had been available on pay TV; and
- (b) the number that would have watched if all matches had been available on free-to-air TV.

To estimate these numbers we can use the viewership figures for matches that were shown and then extrapolate to estimate the viewership numbers when more matches are shown on either pay or free-to-air TV.

Estimates of viewership numbers for matches shown on Sky Sports are available from reliable industry sources. Table 1 shows the number of viewers for 55 of the 66 matches shown in the 2000/2001 football season. The table indicates that matches vary quite considerably in popularity, with the highest viewership (Arsenal v. Manchester United, 1.94 mn) more than three times as great as the lowest (Southampton v. Ipswich Town, 616,000). The average viewership for these games was 1.1 mn, and given 66 matches shown the total viewership for the season was in the region of 73 mn.

In order to consider the impact of alternative arrangements we also estimate the viewership that would be expected if a free-to-air broadcaster had won the right show at least some of the packages on offer. Finally, we make an estimate of the value of lost viewership relative to these alternatives.

- (a) *The number of viewers that would have watched if all matches had been available on pay TV*

We begin by estimating the viewership that there would have been if all 380 matches played in the Premier League had been shown on pay TV. At one extreme we might assume that matches currently not shown would on average attract an audience as large as those currently shown (an average of 1.1 mn per match). On this assumption total viewership would have been 418 mn. This is more than five times larger than the actual viewership.

However, this calculation assumes that the average popularity of the matches not shown would have been the same as the average popularity of the matches shown. In practice Sky is allowed to select the matches that it broadcasts in advance and presumably does so in way which is expected to maximise the audience. Therefore it can be argued that matches not currently shown would attract smaller average audiences. Moreover, it is possible that increasing coverage of football on TV would produce a saturation effect, meaning that audiences for minor games might be negligible.

If we rank viewership of matches shown from the highest to the lowest we can produce a chart like Figure 1.

**Table 1: Viewership for Matches Broadcast on Sky Sports**

<b>Fixture Date</b>	<b>Fixture</b>	<b>Audience</b>
01-Oct-2000	Arsenal vs Man Utd	1,940,000
25-Feb-2001	Man Utd vs Arsenal	1,785,000
19-Nov-2000	Spurs vs Liverpool	1,715,000
12-Nov-2000	Chelsea vs Leeds Utd	1,545,000
31-Mar-2001	Liverpool vs Man Utd	1,541,000
18-Mar-2001	Aston Villa vs Arsenal	1,523,000
26-Dec-2000	Aston Villa vs Man Utd	1,482,000
18-Dec-2000	Spurs vs Arsenal	1,475,000
21-Jan-2001	Sunderland vs Bradford City	1,474,000
17-Dec-2000	Man Utd vs Liverpool	1,464,000
01-Jan-2001	Man Utd vs West Ham Utd	1,440,000
11-Feb-2001	Charlton Athletic vs Newcastle Utd	1,413,000
16-Apr-2001	Everton vs Liverpool	1,395,000
03-Mar-2001	Leeds Utd vs Man Utd	1,371,000
21-Apr-2001	Man Utd vs Man City	1,321,000
29-Oct-2000	Bradford City vs Leeds Utd	1,308,000
18-Nov-2000	Man City vs Man Utd	1,274,000
14-Jan-2001	Ipswich Town vs Leicester City	1,265,000
08-May-2001	Liverpool vs Chelsea	1,256,000
10-Dec-2000	Coventry City vs Leicester City	1,198,000
14-Apr-2001	Man Utd vs Coventry City	1,176,000
20-Aug-2000	Man Utd vs Newcastle Utd	1,174,000
05-Nov-2000	Everton vs Aston Villa	1,160,000
23-Dec-2000	Liverpool vs Arsenal	1,132,000
21-Aug-2000	Arsenal vs Liverpool	1,103,000
24-Sep-2000	Leicester City vs Everton	1,065,000
13-Apr-2001	Liverpool vs Leeds Utd	1,035,000
22-Oct-2000	Aston Villa vs Sunderland	1,016,000
06-Sep-2000	Chelsea vs Arsenal	1,014,000
04-Mar-2001	Ipswich Town vs Bradford City	982,000
23-Sep-2000	Man Utd vs Chelsea	981,000
12-Feb-2001	West Ham Utd vs Coventry City	979,000
15-Oct-2000	Derby County vs Liverpool	978,000
27-Dec-2000	Southampton vs Spurs	976,000
27-Aug-2000	Aston Villa vs Chelsea	957,000
11-Sep-2000	Spurs vs West Ham Utd	953,000
17-Sep-2000	Man City vs Middlesbrough	941,000
21-Oct-2000	Man Utd vs Leeds Utd	941,000
21-Apr-2001	Sunderland vs Newcastle Utd	935,000
04-Nov-2000	Leeds Utd vs Liverpool	888,000
28-Apr-2001	Leeds Utd vs Chelsea	876,000
22-Jan-2001	Charlton Athletic vs West Ham Utd	865,000
05-Mar-2001	Sunderland vs Aston Villa	857,000

01-Apr-2001	Charlton Athletic vs Leicester City	795,000
07-May-2001	Ipswich Town vs Man City	793,000
04-Dec-2000	Sunderland vs Everton	791,000
30-Apr-2001	Charlton Athletic vs Ipswich Town	750,000
09-Apr-2001	Middlesbrough vs Sunderland	744,000
16-Oct-2000	Middlesbrough vs Newcastle Utd	726,000
06-Nov-2000	Derby County vs West Ham Utd	717,000
30-Dec-2000	Ipswich Town vs Spurs	696,000
23-Oct-2000	Southampton vs Man City	655,000
19-May-2001	Charlton Athletic vs Liverpool	654,000
10-Sep-2000	Derby County vs Charlton Athletic	621,000
02-Apr-2001	Southampton vs Ipswich Town	616,000

Source: TV Sports Markets

Figure 1: Premier League viewership 2000/2001

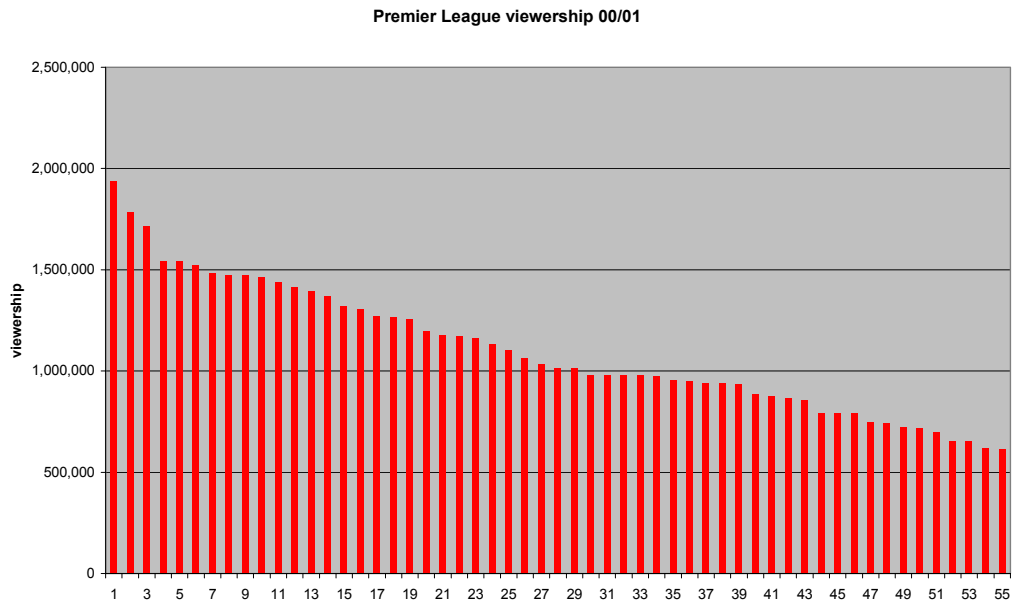
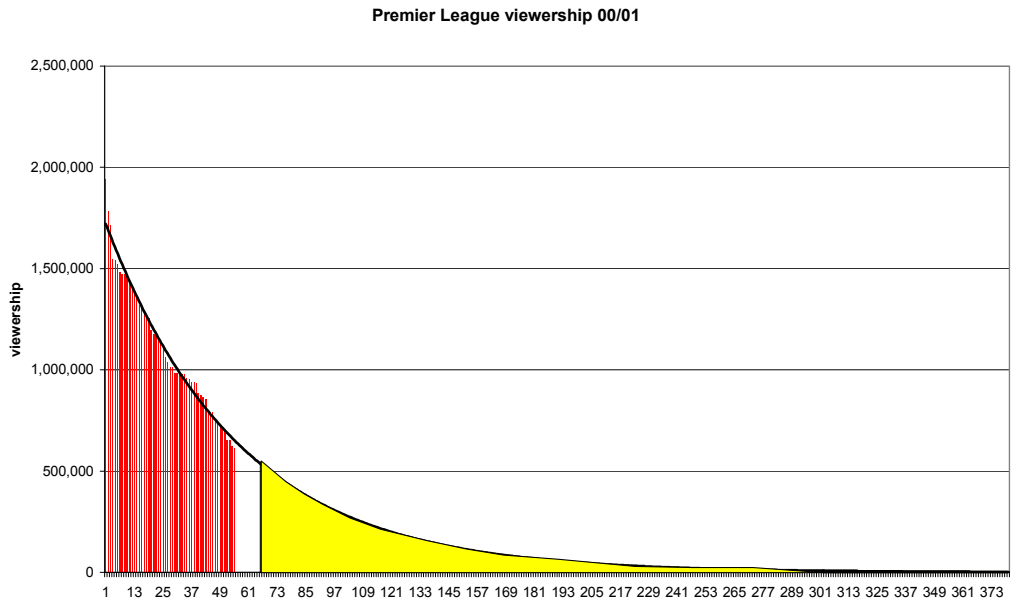


Figure 1 shows that there is a fairly steady and predictable decline in attendance as we move from the most popular games to the least popular. We can use this information to construct an estimate of the viewership of the remaining games, *assuming that the games selected were in fact the most popular ones*. This is illustrated in Figure 2.

**Figure 2 Estimated TV viewership for all games 2000/2001**



In Figure 2 we have taken the data for actual viewership for games broadcast and then extrapolated the potential viewership for all games. This extrapolation assumes that viewing figures decline at a constant percentage rate, namely that each successive game attracts an audience roughly two per cent smaller than the previous one, starting from the most popular and working down to the least popular. The lightly shaded area that runs from between the 61 and 380 figures on the x axis in Figure 2 is the estimated lost viewership that would have watched live football on TV if all games were broadcast. This adds up to 24 mn viewers, equivalent to one third of the total viewership in that season. In reality, this figure is probably an underestimate, since there were many games that would have been more popular than some of those actually shown.

This analysis provides us with both an upper and lower limit for the total viewership lost by restricting live football output to pay-TV showing just 66 out of the 380 live matches. The lower bound is 24 mn and the upper bound is 345 mn.

*(b) Total viewership if all matches had been available on free-to-air TV*

While we now have a figure for the number of viewers lost from restricting numbers on pay-TV we also need to assess the lost viewers from broadcasting games on pay-TV rather than free-to-air TV. The last time that live matches played in the top division of English soccer were shown on free-to-air TV was in the 1991/92 season when the contract to broadcast then First Division matches was held by ITV. Since then the only games involving exclusively English teams that have been broadcast live have been Cup games, mostly in the FA Cup. The Monopolies and Merger Commission report on the proposed merger of BSKyB and Manchester United provided some data on FA Cup match viewership

**Table 2: FA Cup Viewership on free-to-air, 1996-1998**

<b>Date</b>	<b>Fixture</b>	<b>Broadcaster</b>	<b>Viewership ('000s)</b>
11/05/1996	Manchester United v. Liverpool	BBC	13,219
18/02/1996	Manchester United v. Manchester City	BBC	11,594
17/05/1997	Chelsea v. Middlesbrough	BBC	10,929
05/01/1997	Manchester United v. Tottenham	BBC	10,552
26/01/1997	Chelsea v. Liverpool	BBC	10,237
07/01/1996	Chelsea v. Newcastle United	BBC	8,721
16/02/1997	Leicester City v. Chelsea	BBC	8,699
16/05/1998	Arsenal v. Newcastle Utd	ITV	8,080
10/03/1996	Leeds Utd v. Liverpool	BBC	7,993
28/01/1996	Sheffield Utd v. Aston Villa	BBC	7,882
31/03/1996	Chelsea v. Manchester Utd	BBC	7,651
09/03/1997	Sheffield Wednesday v. Wimbledon	BBC	6,783
04/01/1998	Everton v. Newcastle Utd	ITV	6,590
13/04/1997	Chelsea v. Wimbledon	BBC	6,220
08/03/1998	Arsenal v. West Ham	ITV	5,670
05/04/1998	Arsenal v. Wolves	ITV	5,180
25/01/1998	Manchester City v. West Ham	ITV	5,120
15/02/1998	Arsenal v. Crystal Palace	ITV	4,530

Source: MMC report on proposed merger of Manchester United and BSkyB

The average viewership for these games played and shown free-to-air was just over 8 mn. During the same period 30 FA cup matches were broadcast on Sky Sports with an average viewership of 1.5 mn. The 30 most popular Premier League matches shown on Sky Sports had an average viewership of just over 1.3 mn. It therefore seems reasonable to suppose that

- (i) FA Cup matches on free-to-air television are more or less as popular as Premier League games; and
- (ii) it is legitimate to extrapolate the viewership for FA Cup matches on free-to-air to estimate what free-to-air viewership of Premier League games would be if matches were shown this way.

**Figure 3 FA Cup viewership on free-to-air TV, 1996-1998**

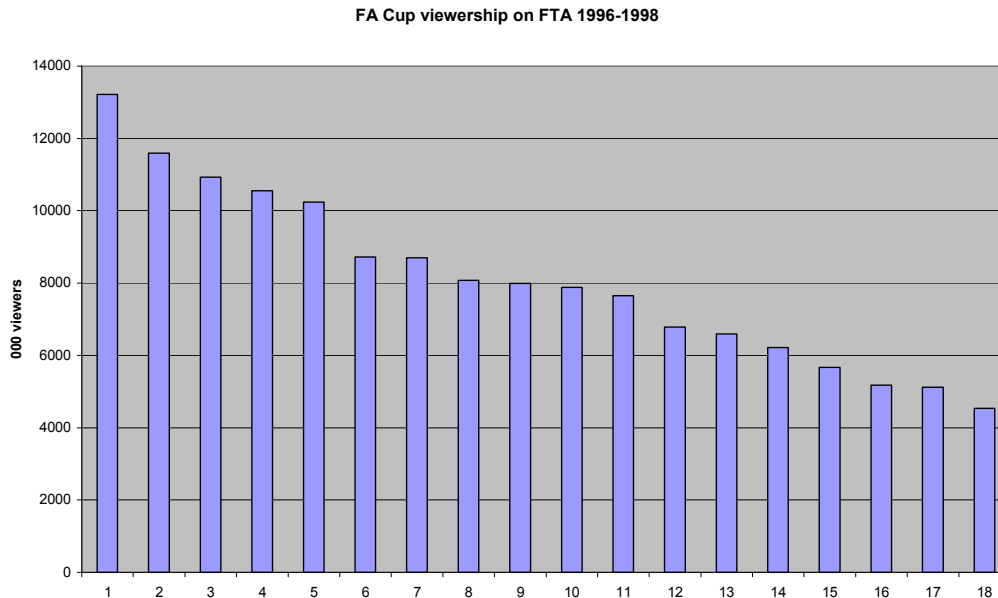


Figure 3 shows the distribution of viewership on free-to-air for the FA Cup. As we have argued above we can reasonably assume that the viewership for these matches is representative of the sort of viewership we would have for Premier League matches.

If we assume that the average viewership for Premier League matches would be the same as for free-to-air FA Cup matches then total viewership would equal 3,074 mn. This estimate can be considered an upper limit for the number of viewers lost by not having free-to-air broadcast of live Premier League matches. At almost exactly 3 bn this upper bound on lost viewership is more than forty times larger than the actual pay TV viewership.

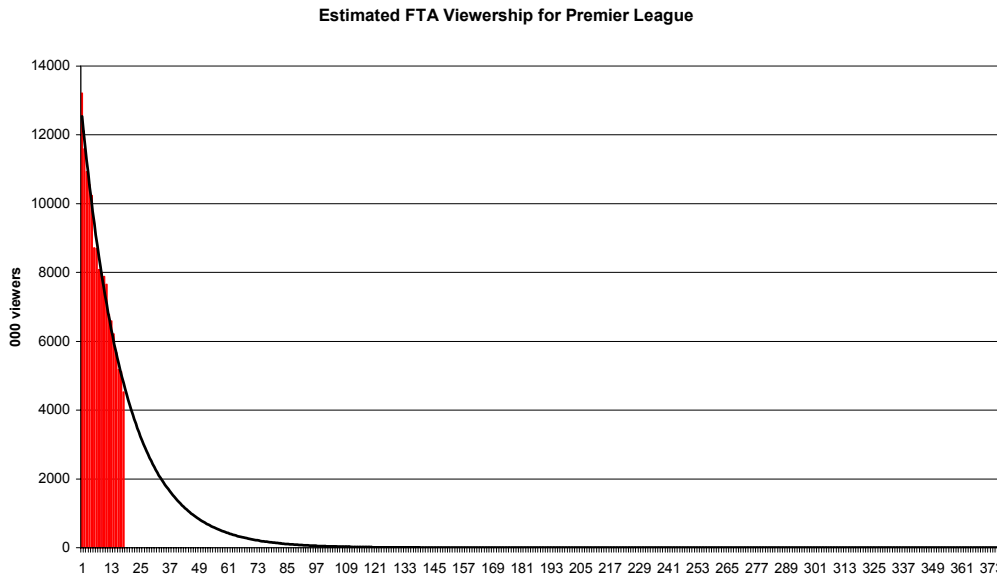
More plausibly there would be a significant fall-off of viewership as the number of live matches on free-to-air increased. We can estimate a figure for this fall-off by assuming that the viewership of the FA Cup matches shown equated to the viewership that would have been achieved by the most popular Premier League games.

Comparing Tables 1 and 2 it is clear that the rate of decline in viewership is greater for FA Cup matches on free-to-air than for Premier League matches on pay TV. This is probably because the best FA Cup games (Final and Semi-Finals) are a lot more attractive than matches in the earlier rounds, while the Premier League produces a larger range of attractive matches<sup>13</sup>. Extrapolating viewership from FA Cup matches will therefore tend to understate the potential viewership of less popular Premier League matches.

The extrapolation is illustrated in Figure 4. The shaded area in Figure 4 is the actual viewership for the FA Cup matches. The potential viewership if all Premier League soccer were broadcast on free-to-air is the total area underneath the curve. This amounts to some 228 mn viewers. Comparing this to the actual pay TV viewership of 73 mn implies a lost viewership of 155 mn. This then is the lower limit for lost viewership due the absence of free-to-air broadcasting.

<sup>13</sup> See Szymanski (2001) for evidence on the relative decline of the FA Cup, which is there attributed to relative competitive imbalance of FA Cup matches compared to Premier League matches.

**Figure 4 Estimated free-to-air viewership for live Premier League football**



*(c) Estimating viewership for Premier League under alternative outcomes to the 2003 auction*

The above calculations give us a sense of the upper and lower limits for lost viewership from not having live Premier League matches on free-to-air TV. While this exercise is important it is also useful to bring this assessment to the actual broadcast packages made available to broadcasters by the Premier League. This will give us a clear idea of lost viewership from the actual packages offered and an idea of the likely gains from different regulatory interventions available to the European Commission.

As we discussed above, the Premier League auctioned three separate packages of rights in 2003, labelled Gold, Silver and Bronze. The Gold package consisted of 38 live matches played at 4pm on a Sunday, the Silver package consisted of 38 Monday evening live games and the Bronze package consisted of 62 live games played on a Saturday either side of the Saturday afternoon window (with 1pm or 5.15pm kick-off). Since all of these packages were acquired by BSkyB, we can estimate the viewership for 138 live matches on pay TV using the data from Figure 2. The estimated lower limit for viewership is 89 mn.

Of course, alternative estimates depend on which kind of broadcaster might own the rights. If we suppose that the Gold and Silver packages went to pay TV broadcasters while the third Bronze package went to a free-to-air broadcaster then we get the following viewership estimates. The lower limit for estimated viewership for 76 live matches on pay TV is 72 mn. For the third Bronze package the lower limit of estimated viewership for 62 live free-to-air matches is 220 mn. This yields a total estimated viewership of 292 mn.

It is then useful to compare the estimated lower limit for exclusive pay-TV (Gold, Silver and Bronze Packages) viewers of 89 mn and the lower limit of combined pay-TV (Gold and Silver packages) and free-to-air (Bronze package) viewers at 292 mn. If we do this we have a lower limit for lost viewership of 203 mn caused by three-package exclusivity. It should be noted that this estimate implies an average viewership on free-to-air television for these matches at 3.5 mn per match. This is actually about 1 mn less per match than the lowest viewership for any of the broadcast FA Cup matches reported in the MMC inquiry.

This is just one feasible configuration of the broadcast packages. Table 3 illustrates the estimated viewership losses under each of the possible ownership arrangements.

**Table 3: Estimated Viewership when live rights are broadcast by different platforms (millions of viewers)**

<i>Platforms and packages</i>	<i>Pay TV viewership</i>	<i>free-to-air viewership</i>	<i>Total viewership</i>
<b>Pay:</b> Gold, Silver, Bronze <b>Free-to-air:</b>	89	-	89
<b>Pay:</b> Gold, Silver <b>Free-to-air:</b> Bronze	72	220	292
<b>Pay:</b> Gold <b>Free-to-air:</b> Silver, Bronze	48	227	275
<b>Pay:</b> Silver, Bronze <b>Free-to-air:</b> Gold	81	201	282
<b>Pay:</b> <b>Free-to-air:</b> Gold, Silver, Bronze	-	228	228

This table illustrates, not surprisingly, that if free-to-air broadcasters had obtained any combination of packages in the rights auction then viewership would be expected to be significantly higher than in the situation where all the rights were held by pay TV broadcasters exclusively.

It is interesting to note that the highest aggregate viewership is expected when only the Bronze package of 62 games played on a Saturday is on free-to-air while the Sunday and Monday packages remain with pay TV. The reason for this is that showing 62 games on free-to-air more or less exhausts free-to-air demand. According to the data audiences decline much faster as the number of live broadcasts on free-to-air increases than they do on pay TV. For free-to-air television each extra game has an audience five per cent smaller than the next most popular match, compared to only two per cent for pay-TV. This seems plausible, given that on average subscribers to pay TV are more likely than free-to-air viewers to be dedicated fans.

*(d) Placing a value on lost viewership*

Having an estimate of the number of viewers lost because of exclusive rights for pay-TV allows us an idea of how many times consumers are disadvantaged. However, we can also estimate what the cost to consumers from exclusivity. We can assume that the amount of leisure time involved in each match is two hours. If all matches were shown on pay-TV they would account for 178 mn hours of leisure time. If the Gold and Silver packages were shown on pay TV and the Bronze package on free-to-air they would account for 584 mn hours, that is 406 mn more hours.

The value to consumers of the lost viewership depends on the comparison between the value consumers place on watching live football on TV and the value they place on the alternative activities they undertake when this option is not available. The estimates of viewership in the previous section rely on the implicit assumption that if matches were available consumers would switch to watching these matches from something else. That (next best) alternative activity could be watching other TV programmes, reading the newspaper, going shopping or any number of other leisure activities.

The value of leisure time in general is typically estimated using hourly wage rates. The logic of this is that a utility maximising individual will choose the number of hours of work which makes the marginal benefit of an hour of work, that is the wage rate, equal to the marginal benefit of an hour of leisure. Taking an average hourly wage rate of £13 for the UK, this suggests that the value of the lost viewership comes to £5,278 mn, less the value of the leisure time spent in the



alternative activity. The value of time spent in the alternative activity is unlikely to be zero, but is equally unlikely to be equal to 100 per cent of the value of time spent watching live matches. If we were to make the generous assumption that consumers valued their next best alternative at 80 per cent of the value of watching live football on TV, this would still give an estimate of over £1,000 mn per year for the value of the lost viewership, or about £5 per consumer per match.

### **Collective Selling versus Individual Selling of Matches**

We have already argued that the FA Premier League is an inefficient cartel which restricts consumer choice, i.e. it manages to impose welfare losses on consumers while failing to maximise the revenues of its members. One remedy for these inefficiencies would be an outright ban on selling broadcasting rights collectively, that is a finding that the FA Premier League is an illegal cartel. Clubs would then be forced to sell the media rights to their games individually. Individual selling of rights could be achieved in a number of ways:

- (A) Clubs could offer their matches directly to distributors for sale as pay-per-view matches;
- (B) Each club could set up its own club channel and sign a distribution deal with distribution platforms, that is satellite and cable; or
- (C) Each club could sell its rights in a wholesale market to intermediaries who would then assemble rights packages for sale to distribution platforms.

Option (A) is essentially what occurs in Italy, where all matches are made available as pay-per-view.<sup>14</sup> Option (B) is like the situation in Major League Baseball in the United States, where some clubs run their own channels. Option (C) is as yet untested, but might prove difficult to implement unless there is genuine competition among broadcasters.

Not surprisingly, the FA Premier League has argued that individual selling of rights would have severe adverse consequences for the distribution of income between football clubs, even suggesting that some smaller clubs might fold entirely under such a remedy. However, there is no necessary connection between collective selling and income redistribution. Teams in other sports have chosen to redistribute income in other ways, for example in the NFL (American Football) teams have traditionally agreed to share the gate money, with 40 per cent going to the visiting team<sup>15</sup>. In Major League Baseball teams have agreed a luxury tax to penalise teams that spend over a fixed limit. Both in America and Europe sports leagues have managed to introduce other mechanisms to maintain competitive balance, such as roster limits (limiting the number of squad members) and salary caps. In these and other cases clubs act to preserve competitive balance because they perceive that this is in the long term interests of all the teams. If this were also true for the members of the Premier League, then they would similarly agree to share income. In some instances the clubs have argued that without collective selling as a basis for redistribution they would refuse to share income. This, however, must be an empty threat if sharing is in the interests of the teams.

In reality, the strong clubs in English soccer have done little to redistribute income is largely because they see no need to, and this is because the extreme imbalances of the Premier League do not seem to undermine interest in the Premier League. Thus the dominance of Manchester United in the 1990s did not bring about a decline in attendance. More generally, the demand for “competitive balance” does not seem to be that great in European soccer as a whole, largely because there are so many other attractive dimensions to the sport, for example, promotion and relegation, competition for entry into the Champions League, Cup competitions, etc.

Another defence of collective selling derives from the claim that broadcasting income used to redistribute resources to the grass roots. It is a fundamental principle of competition law that a

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<sup>14</sup> Originally, the Italian government passed legislation to oblige these rights to be divided between at least two platforms (with no platform controlling more than 60 per cent), but now they have permitted the two satellite platforms Telepiu and Stream to merge.

<sup>15</sup> William McGregor, the founder of the Football League, proposed in 1888 that teams should share gate income equally with the visitors, but his proposal was voted down by the other clubs

restraint cannot be justified merely because part of profit arising from the restraint is used in a good cause. Yet the Premier League and several of its most vocal supporters have used precisely this argument. In the Restrictive Practices Court case referred to above it is reported that David Mellor, then chairman of the Football Task Force appointed by the government, agreed to testify on behalf of the Premier League in return for the agreement by the latter to a 10 per cent levy to be distributed to lower division football<sup>16</sup>.

But as with the argument about competitive balance, there is no necessary connection between collective selling and redistribution, which can be based on any measure of income. Indeed, it might be argued that a more sensible basis for redistribution would be a measure such as total income.

In any case, the central issue in the European Commission's investigation is not collective selling per se, but the FA Premier League's restriction on the number of matches sold. If the FA Premier League agreed to make available all of its matches for live broadcast, or allowed individual clubs to license any unsold rights (as in the UEFA deal), the Commission might agree to the continuation of the collective selling arrangement. What seems harder to imagine is that the Commission can accept the status quo in which nearly two thirds of matches cannot be shown live, including some of those which are most attractive to viewers.

If we work on the assumption that clubs were free to sell off any unsold live rights on their own behalf, teams might reach agreements in which

- the home team owns the broadcast rights, as has been established in several other jurisdictions such as the Netherlands and the US;
- some packages of rights might be sold on a collective basis in order to give an overview of the championship as a whole (e.g. the Gold, Silver and Bronze packages presently offered);
- some fraction of revenues generated by individual selling could be shared between the teams.

The sort of agreements outlined above would clearly preserve the claimed principal benefits of the current collective selling arrangements. On this basis it would be reasonable to conclude that the current collective selling arrangements are not indispensable and should be ruled illegal. It would then be open to the Premier League to advance a less restrictive arrangement.

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<sup>16</sup> See *Broken Dreams* by Tom Bower (2003, Simon and Schuster), p 139.

### Section 3: Contracts, Rights Selling and Competition in the Pay-TV Market

The Premier League's collective selling arrangements, and in particular the restriction on the right of clubs to sell matches which are not sold collectively, reduces the number of live matches available to TV broadcasters and directly reduces consumer welfare. Removal of these restrictions, and hence an increase in the number of live matches made available for broadcast, should be a *sine qua non* of any resolution of the case accepted by the Commission.

A second set of issues arise, however, from the nature of the exclusive contracts agreed between the FA Premier League and BSkyB and the impact of these agreements on competition in the downstream pay-TV market. The Commission's objections to date have focused on the sale of *all* of the Premier League's (or UEFA's) live broadcasting rights *exclusively* to a single broadcaster. Absent this form of monopolisation, it has otherwise declared itself content that any rights sold should be exploited *exclusively by the broadcaster that purchases them*.<sup>17</sup> That is, it is not that the broadcasting rights are exclusive to the broadcaster which acquires them that has concerned the Commission, rather that a single broadcaster should end up as the owner of all of the rights available.

But does splitting the *exclusive rights* into multiple packages really achieve anything, even if more than one company comes away with a package of rights? Some recent economic analysis suggests that the answer to this question may be no, and it is instructive to understand why this is the case. This in turn requires some prior understanding of the way in which exclusive broadcasting rights are already being exploited by BSkyB in the British pay-TV market.

#### Exclusive Rights and the Pay-TV Market

The pay-TV market can be thought of as comprising three vertically related layers:

- (i) the original production of programming content, for example sports events, movies, news programs etc. (This is the 'upstream rights seller layer');
- (ii) the creation of broadcasts, or TV channels, from original programming content (the 'broadcaster layer'); and
- (iii) the distribution and retailing of channels and programs to consumers (the 'retail distribution layer').

The uppermost layer produces the content desired by viewers, for example Premier League football matches, the Olympic games and Hollywood movies and sells the rights to this content 'downstream' to the broadcasting layer for packaging into channels and ultimately transmission to viewers. The retailing layer purchases programming and channels from broadcasters and sells these directly to viewers, along with a transmission mechanism (i.e. satellite or cable). The broadcasting layer purchases broadcasting rights, 'creates' programming and packages this programming into channels for sale to downstream retailers. Figure 5 depicts the industry structure.

BSkyB is the only fully vertically integrated pay-TV company in Britain, and is active at each level in the vertical structure, although it operates primarily in the broadcasting and retailing layers. Its main activity is the purchase of rights to programming content from original rights owners – such as major sports events and Hollywood movies - for direct distribution to its own satellite subscribers, and for resale to its downstream competitors in distribution<sup>18</sup>.

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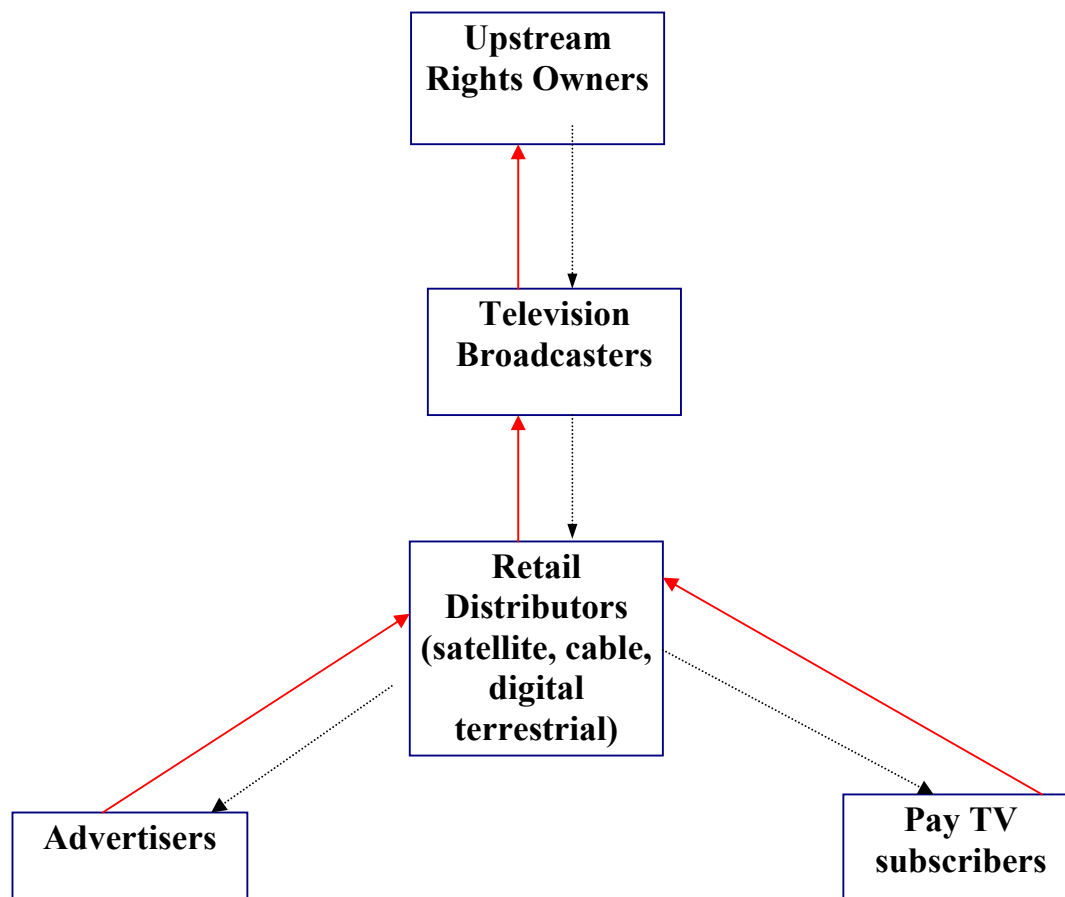
<sup>17</sup> See, for example, Torben Toft "TV Rights of Sports Events," Brussels, 15 January 2003 and Miguel Mendes Pereira "Scope and Duration of Media Rights Agreements: Balancing Contractual Rights and Competition Law Concerns," Brussels, 10 October 2003.

<sup>18</sup> BSkyB's downstream competitors, on the other hand – the cable companies and formerly ITV Digital - have taken only limited steps to enter the broadcasting layer, and with very limited success. Telewest purchased the broadcasting company Flextech in April 2000 which produces a number of 'basic' pay-TV channels such as Bravo and Screen Shop. ITV Digital acquired the rights to Football League matches and some other sports

At the distribution level BSkyB is the largest operator with 66.7 per cent of subscribers, up from 54 per cent since the collapse of ITV Digital in April 2002. At the broadcasting level there are a number of suppliers of pay-TV channels and more than 100 pay-TV channels are currently available to UK subscribers. Only ten of these channels are wholly owned and produced by BSkyB.

It is widely acknowledged, however, that it is 'premium' programming content which drives subscriptions to pay-TV services. Since BSkyB owns the exclusive broadcasting rights to practically all of the Hollywood studios' first-run films, and to the majority of the major sports events available to pay-TV, it is a near-monopolist in the premium content market<sup>19</sup>. As premium programming content is available in strictly limited supply, and BSkyB has had exclusive control over most of this content since the early 1990's, it is primarily at this level in the vertical structure that problems of abuse of market power arise.

**Figure 5 Vertical Structure in Pay TV**



**Explanation of Figure 5:** the black dotted arrows follow the sales of rights, or programming, downstream. The solid arrows follow the flow of values upstream.

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events, such as the UEFA Champions League, and unsuccessfully launched a sports channel, ITV Sport. NTL acquired Premier League football 'pay per view' rights in 2000, but was reportedly unable to negotiate a carriage agreement with BSkyB and returned the rights for re-auctioning.

<sup>19</sup> These broadcasting rights have been used to create the Sky film and sports 'premium' channels, Sky Sports 1, 2, and 3 and the Sky Movie channels.

because previously noted, BSkyB purchases broadcasting rights under exclusive vertical contracts with upstream rights sellers, such as the Premier League, and then resells the programming to its downstream competitors (that is the cable companies) for variable, or per subscriber, fees. The economic implications of these contractual arrangements for competition in the pay-TV market have been debated fiercely - and often - in various regulatory inquiries, but until recently have not been well-understood.

Harbord and Ottaviani (2001) addressed these issues in an economic analysis of competition in the pay-TV market using a model inspired by the current market situation in the UK<sup>20</sup>. Their point of departure was a recent paper by Oxford economist Mark Armstrong (1999), which analyses competition in the pay-TV market in the context of a classic Hotelling model of duopoly price competition<sup>21</sup>. This model captures quite well a number of the key features of the pay-TV market, and of the market for premium programming in particular:

- (i) downstream price competition is between firms with differentiated products;
- (ii) the acquisition of premium programming increases the attractiveness of a company's package to subscribers; and
- (iii) failure to obtain access to premium programming when other firms do have access results in a loss because other firms' products become relatively more attractive and they attract a larger share of subscribers.

In Armstrong's model, pay-TV companies compete initially to sell basic programming to customers. One firm - the "industry leader" - is assumed either more efficient than its rival, or else to have previously acquired a more attractive package of basic programming. When the rights to some type of premium programming (e.g. Premier League football matches) becomes available in an upstream market, the outcome of the sale of the rights has a substantial impact on the competitive balance in the downstream retail market.

A pay-TV firm which acquires the *exclusive* rights to the premium programming obtains a significant competitive advantage over its rival, and the rival suffers a loss - a "negative externality" in economist's parlance. Competition to purchase the rights can therefore be modelled as an auction with "externalities" in which downstream competition is affected by the outcome of the auction<sup>22</sup>.

In the absence of the resale of premium programming, the industry leader's willingness to pay for the rights in the upstream market exceeds that of its smaller rival, hence it will always acquire the rights in an auction. Armstrong considers what would happen if the industry leader were able to resell the programming to its downstream retail competitor for a fixed fee, that is a lump sum payment. He concludes that reselling would *never* take place since it would reduce the competitive advantage of the industry leader. Although the smaller downstream firm, and its consumers, would benefit from having access to the premium product, this gain is less than the industry leader's loss in competitive advantage from reselling. Hence reselling will typically be welfare enhancing, but not privately profitable, when resale contracts are restricted in this fashion.

Harbord and Ottaviani (2001) extended Armstrong's analysis by allowing downstream pay-TV retailers to resell premium programming obtained under an exclusive vertical contract for variable, or *per subscriber* fees, and obtained strikingly different conclusions. They found that reselling via per subscriber fees *will always occur* when the exclusive rights are originally purchased for either lump sum or per subscriber fees from the upstream rights seller, and that this can have profound effects on the nature of competition in the pay-TV market. Their analysis thus predicts that reselling will take place under precisely the conditions observed in the UK market. Like Armstrong's analysis, the model also predicts that the upstream rights seller will prefer exclusive to nonexclusive contracts with downstream firms.

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<sup>20</sup> See Harbord and Ottaviani (2002) for a similar discussion.

<sup>21</sup> The Hotelling model is widely used by economists to study competition in a variety of market settings, and most recently, network access pricing. See especially Laffont, Rey and Tirole (1998).

<sup>22</sup> See Jehiel and Moldovanu (2000) for an analysis of such auctions.

### **The Effects of Resale Contracts on Downstream Competition**

The key result of the analysis is that downstream competition to supply premium programming to consumers will be *ineffective* when resale contracts specify per subscriber rather than lump sum, that is fixed, fees. Reselling for per subscriber fees means that all consumers in the market will be served, thus avoiding one of the contracting inefficiencies identified by Armstrong. It does so, however, in a manner which does not dissipate the monopoly rents available from the sale of premium programming. Resale for per-subscriber fees allows a downstream firm which acquires the exclusive rights to prevent the dissipation of downstream profits by increasing the marginal cost of its competitor, in other words by *raising rivals' costs*, while simultaneously increasing the *opportunity cost* of serving its own customers. This increased opportunity cost has exactly the same effect as an increase in the marginal costs of the reselling firm, and gives both firms an incentive to increase their retail prices to monopolistic levels.

The intuition behind the opportunity cost effect is easily explained. Given a resale contract, any revenues the reselling firm could earn from reducing its retail price in order to attract its rivals customers come at the expense of the resale revenue it would otherwise have received from its rivals subscribers. This reduction in resale revenues - an opportunity cost - has exactly the same effect as an increase in the reselling firms marginal costs, giving it a strong incentive to maintain a high retail price in equilibrium.

The resale price thus acts as an effective mechanism for relaxing downstream price competition and extracting consumer surplus from the premium product. In fact, in the Harbord and Ottaviani analysis, the highest resale fee which can be implemented extracts all of the surplus available from selling the premium good to consumers, and this surplus accrues initially to the reselling firm. Consumers are therefore deprived of the benefits of competition. It is as if the premium programming market were monopolized by a single firm, and consumers would prefer a ban on resale contracts, even though this typically reduces social welfare<sup>23</sup>.

If instead the premium programming were sold by both downstream firms who faced "uninflated" marginal costs, that is if both firms acquired the rights for a lump sum fee, fierce downstream competition to sell the programming to consumers would result in these profits being competed away, and the benefits captured by consumers. This observation suggests that one remedy for the competition problem identified in the Premier League case would be to regulate the way in which premium programming rights are sold and resold.

### **The Effects of Resale Contracts on Upstream Competition**

Another conclusion of the Harbord and Ottaviani analysis is that an upstream rights seller such as the UK Premier League will usually prefer to sell programming rights exclusively to one downstream firm, rather than nonexclusively to all firms. Exclusive sale - followed by resale - maximises the monopoly rents available for distribution between the upstream seller and the downstream retailer which acquires the rights, thus increasing downstream firms' willingness to pay. Nonexclusive sale, on the other hand, typically extracts less surplus for both the upstream rights seller and the downstream firms.

Given that sports and other programming rights are almost always sold under exclusive contracts to pay-TV companies, this analysis therefore predicts two key features of competition in the UK pay-TV market; the form of the premium programming rights sale and resale contracts.

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<sup>23</sup> These conclusions are not entirely novel, and similar effects have been shown to hold in some closely related economic models, such as in the literature on 'raising rivals' costs' and in the patent licensing literature. See, for example, Krattenmaker and Salop (1986), Salop and Scheffman (1983)(1987), Katz and Shapiro (1985) and Shapiro (1995).

## Remedies

Harbord and Ottaviani's analysis identified a clear competition policy concern in BSkyB's resale contracts with its retail competitors in the pay-TV market. The key competition problem is that premium programming, such as Premier League football, endows monopoly power upon upstream rights owners. Exclusive vertical contracts then allow this monopoly power to be transferred downstream, resulting in higher prices and lower consumer welfare. Indeed, when exclusive rights are resold for per-subscriber fees, consumers are worse off in aggregate than they would be in the absence of any reselling. A number of possible competition policy remedies were considered, the two most relevant to the current inquiry being:

- i. 'Rights splitting', or forced divestiture of premium programming rights, i.e. a 'UEFA-type' remedy in which exclusive rights are split between multiple broadcasters; and
- ii. A ban on the sale of exclusive rights, so that each broadcaster is offered nonexclusive access to the rights on the same terms as its competitors

We briefly discuss each of these remedies in turn.

### Forced rights splitting

Both the UK regulatory authorities and the European Commission have displayed a preference for forcing upstream rights sellers to make exclusive packages of rights available to a number of different downstream firms. For example, in the 2000 Premier League auctions the broadcasting rights were split into a package of pay-per-view rights and a package of non pay-per-view rights after an intervention by the Office of Fair Trading, with no pay TV company permitted to win the auctions for both packages<sup>24</sup>. Similarly, under the UEFA agreement Champion's League broadcasting rights are split into packages and sold separately to pay-TV and free-to-air broadcasters.

It is unclear, however, why the splitting of broadcasting rights into separate exclusive packages should be expected to have any significant pro-competitive effect, especially when all of the rights are sold to pay-TV broadcasters. To address this issue Harbord and Ottaviani (2001) considered two alternative ways in which rights could be separated into packages. First, *rights splitting* requires the upstream rights' seller to split the rights into separate exclusive packages and sell them to different downstream broadcasters. Alternatively, *forced rights divestiture* requires the downstream firm which has acquired the exclusive package of rights to divest itself of a fraction of the rights by selling them for a lump-sum fee to its competitor. The two remedies therefore operate at different levels in the vertical supply chain.

The welfare consequences of both rights splitting and forced rights divestiture, however, do not differ from the case where the rights are sold exclusively to a single firm. That is, splitting the rights between pay-TV broadcasters simply creates two or more downstream monopolies in the place of one, and consumers are made no better off as a result<sup>25</sup>. Neither has any effect on competition, consumer surplus or welfare in the analysis.

### Nonexclusive rights selling or forced rights sharing

Resale of exclusive programming rights for a per-subscriber fee results in downstream firms charging monopolistic prices for premium programming, such as Premier League football, and consumers receive no competitive benefits. If instead the rights were acquired by each downstream firm for a lump-sum fee, downstream firms would make no additional profits from the premium programming, and intense competition between firms would reduce prices and increase consumer surplus. This suggests that a more effective remedy for the monopolistic pricing of the premium product, such as Premier League football matches, would be to force

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<sup>24</sup> Cave and Crandall (2001) also suggest that the rationale behind the OFT's 1999 challenge of Premier League collective selling practices in the Restrictive Trade Practices Court, was that the Premier League should make more rights packages available.

<sup>25</sup> While forced rights splitting has no effect on consumer surplus or total welfare, it may effect how much the upstream rights seller receives for the rights. See Harbord and Ottaviani (2001), Section 5.3.

firms to resell programming rights to each other for lump-sum fees. Alternatively, rights could be sold nonexclusively by the upstream rights seller to each downstream firm, for a lump-sum fee.

When the rights are sold in this way, that is if each firm acquired the *nonexclusive* rights for a lump-sum fee from the rights seller, fierce downstream competition to sell the programming to consumers results in supra-normal profits being competed away, and the benefits from the premium programming captured by consumers.

Hence a more effective remedy for the competition problems identified by the Commission might be to regulate the way in which FA Premier League rights are sold and resold. Imposing a ban on the sale of exclusive rights would ensure that every pay-TV broadcaster had access to the programming on the same terms as its competitors, and consumers would benefit from competition to 'sell' the programming in the downstream TV market.

### **Some implications of the model**

The Harbord and Ottaviani analysis of competition in the pay-TV market predicts that premium programming rights will be sold originally under exclusive vertical contracts and then resold by the acquiring firm for per-subscriber fees to its competitors. The resale of premium programming for per-subscriber fees has the effect of relaxing downstream price competition, providing incentives for both downstream firms to increase their prices at the expense of consumers. The profits created by these contractual arrangements are initially captured by the reselling firm, and then at least partially transferred upstream to the original rights monopolist.

The model thus predicts a number of the key features of competition in the UK pay-TV market, and in particular the form of the rights selling and resale contracts. The key conclusion for competition policy purposes is that these vertical and horizontal contracts may actually harm consumers compared to the case of no resale, in which some consumers do not get served.

In an extension of this analysis they considered what happens when resale contracts specify wholesale prices for premium programming which are proportional to retail prices, as occurs under the so-called 'Direct-To-Home linkage' in BSkyB's contracts with its competitors (see Office of Fair Trading, 1996). They found that such 'retail price proportional' resale contracts are worse for consumers than the simpler resale contracts we considered initially. When the reselling firm is able to commit itself to a proportional resale pricing scheme this results in even higher equilibrium profits and prices and lower consumer welfare. This is because when the reselling firm reduces its retail price in order to attract its rival's customers, this not only results in a reduction in its resale revenue via the opportunity cost effect described above, it also reduces the resale price directly via the Direct To Home linkage. This makes price competition to gain market share at the expense of rivals still more costly, and hence less attractive.

Proportional resale pricing, as currently practised by BSkyB, therefore appears to be an even more effective mechanism for softening downstream price competition and extracting consumer surplus from both premium and basic programming. Indeed, under this type of resale pricing consumers may actually be worse off than they would have been had the premium programming never been made available.

The clear message for the European Commission investigation is that not just the collective selling arrangements, but the form of the exclusive rights selling contracts themselves – both upstream and downstream – lie at the heart of the competition problem, and need to be addressed.



## Section 4: Conclusions

The rights to broadcast live Premier League football matches are among the most lucrative sporting rights in the world. Since 1992 these rights have been used by BSkyB, in the words of Rupert Murdoch, as a “battering ram” to develop and control the pay-TV market in the UK, despite numerous interventions by the UK regulatory and competition authorities. The way in which these rights have been sold – and resold – has been the source of significant competition problems in the pay-TV market, and associated consumer welfare losses.

The FA Premier League’s collective selling arrangements lie at the heart of the problem. The Premier League acts as an inefficient cartel, restricting output and depriving consumers of the benefits of viewing more football matches. The FA Premier League makes available only a fraction of the live games which could be broadcast, and does so in a way that only pay-TV companies can afford to purchase them. It also prevents individual clubs from selling the rights to their own games, even though these will not otherwise be broadcast. In other countries, such as Italy and Spain, football clubs sell their matches individually.

According to the estimates presented in this paper, the lost viewership from the FA Premier League restrictions may be as much as 200 mn over the year, equivalent to about nine matches per household per season, and the welfare cost of the order of £1bn, a substantial loss by any standards. Hence reforms which fail to ensure that the majority – if not all – of Premier League matches are available on live TV will have stopped short of achieving their goal.

Added to this consumer welfare loss from the pure restriction of choice, is the loss from the restriction on competition made possible by the FA Premier League’s exclusive contracting arrangements. As recognised by the UK competition authorities, the source of BSkyB’s market power lies in its stranglehold over the rights to broadcast key premium content such as Premier League football. Upstream rights sellers, like the Premier League, achieve maximum monopoly rents when the content they provide is exploited exclusively by a single downstream broadcaster. Exclusive sale, followed by resale, maximises the monopoly rents available for distribution between the upstream seller and the downstream retailer which acquires the rights. It does so however, by softening downstream price competition, thus preventing consumers from realising the benefits of competition between multiple downstream retailers.

The Commission’s “UEFA-style” approach to the reform of rights selling arrangements, however, is unlikely to have much effect on competition or consumer welfare in the UK pay-TV market, even if it succeeds in distributing Premier League rights amongst multiple broadcasting companies. From one large monopoly, two or three smaller monopolies will have been created and consumers may be made no better off as a result.

The problem is that the Commission may be tackling the wrong kind of exclusivity. In order to improve matters significantly, not only must the rights not be sold exclusively to a single broadcaster, but *the same rights must be licensed nonexclusively to multiple broadcasters* (for example to each pay-TV company or platform). Absent this remedy, consumers are unlikely to benefit greatly from a reformed Premier League selling procedure.

What should Commission do now? The Premier League argues, in defence of its output restriction, that any increase in revenues from selling additional rights would be offset by loss of gate receipts at the matches. However, in recent years we have observed both increasing live coverage of football and increasing attendance at matches. The FA Premier League also argues that individual selling of rights would have adverse consequences for the distribution of income between football clubs, suggesting that some smaller clubs might collapse if collective selling were prohibited. But there is no necessary connection between collective selling and income redistribution, and in other sports redistribution of income occurs in other ways. In America and Europe sports leagues have introduced other mechanisms to maintain a competitive balance, because they perceive that this is in the long term interests of all the teams.

Finally, English football is less stable financially today than it was before the first BSkyB deal in 1992. The collapse of a collectively negotiated broadcasting deal with ITV Digital plunged many

First Division clubs into crisis, and this would have been less likely to occur in a world of individually negotiated broadcast deals. Financial instability in the Premier League appears to be primarily a consequence of the very large losses of broadcasting income that clubs experience when they are relegated, and collective selling only enhances this effect.

In our view, a reformed Premier League selling procedure must include two elements. First, the restriction on output must be alleviated, even if this involves the total prohibition of collective selling. Second, the Commission should eschew any solution which leaves all of the rights in the hands of a single pay-TV broadcaster. Consumers will be best served by reforms which permit real competition to develop between both pay-TV and free-to-air broadcasters in showing live football matches.

In the short term, the Commission's objectives might be partially achieved by a requirement that some live rights be sold to free-to-air broadcasters, such as ITV or the BBC. At least from the point of view of consumers this would allow them to view some football matches for free, thus reducing their reliance on, and hence willingness to pay for, pay-TV. However, free-to-air broadcasters face severe capacity constraints and can broadcast only a small number of live matches per season. The bulk of the rights will of necessity remain with one or more pay-TV operators, a constraint which needs to be recognised in evaluating any long-term remedy for the competition problems identified by the Commission

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**Annex: Methodology for estimating viewership**

To estimate the lower bound for lost viewership we have estimated the following regression using the data available:

$$\text{Log (viewership)} = a + b N$$

where N is the rank of the match according to viewership in that season. Using the estimates for the coefficients a and b from the regression it is then possible to produce an estimate of the viewership for any match N between 1 and 380. Below are the two estimated regressions

**1. Estimate for pay TV viewership**

SUMMARY OUTPUT

<i>Regression Statistics</i>	
Multiple R	0.992176
R Square	0.984413
Adjusted R Square	0.984119
Standard Error	0.036552
Observations	55

ANOVA					
	<i>df</i>	<i>SS</i>	<i>MS</i>	<i>F</i>	<i>Significance F</i>
Regression	1	4.472229	4.472229	3347.343	1.41E-49
Residual	53	0.070811	0.001336		
Total	54	4.54304			

	<i>Coefficients</i>	<i>Standard Error</i>	<i>t Stat</i>	<i>P-value</i>	<i>Lower 95%</i>	<i>Upper 95%</i>	<i>Lower 95.0%</i>	<i>Upper 95.0%</i>
a	14.37653	0.009993	1438.612	2.3E-123	14.35648	14.39657	14.35648	14.39657
b	-0.01796	0.00031	-57.8562	1.41E-49	-0.01859	-0.01734	-0.01859	-0.01734

**2. Estimate for free-to-air TV viewership**

SUMMARY OUTPUT

<i>Regression Statistics</i>	
Multiple R	0.991228
R Square	0.982533
Adjusted R Square	0.981441
Standard Error	0.041548
Observations	18

ANOVA					
	<i>df</i>	<i>SS</i>	<i>MS</i>	<i>F</i>	<i>Significance F</i>
Regression	1	1.553588	1.553588	899.9869	1.72E-15
Residual	16	0.02762	0.001726		
Total	17	1.581208			

	<i>Coefficients</i>	<i>Standard Error</i>	<i>t Stat</i>	<i>P-value</i>	<i>Lower 95%</i>	<i>Upper 95%</i>	<i>Lower 95.0%</i>	<i>Upper 95.0%</i>
a	9.493143	0.020432	464.6276	1.79E-34	9.44983	9.536456	9.44983	9.536456
b	-0.05663	0.001888	-29.9998	1.72E-15	-0.06063	-0.05263	-0.06063	-0.05263

## **About the authors**

### **David Harbord**

Since founding Market Analysis Ltd in 1995, David Harbord has completed regulatory studies for the World Bank, the European Commission, the Industry Commission of Australia and the Treasury of New South Wales. He has been an economic adviser to the majority of telecommunications and media companies in the UK and represented energy companies in the UK, Europe and Australia in regulatory proceedings and competition policy litigation. David has been involved in many of the most high-profile regulatory inquiries and antitrust cases of recent years, including the Endesa/Iberdrola merger in the Spanish electricity market, the regulatory review of conditional access pricing in the UK pay-TV market, the Competition Commission's 'calls to mobiles' inquiry and the Office of Fair Trading's Competition Act investigation into BSkyB.

David's academic research focuses on electricity auctions, the markets for sports rights and the analysis of contracts in the pay-TV market. He has recently published articles in the Economic Journal, the International Review of Law and Economics, the European Competition Law Review and the Electricity Journal.

Prior to taking up a career in consulting, David pursued an academic career and held teaching and research positions at the University of Oxford, Stanford University, the University of British Columbia and the London School of Economics.

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As well as publishing academically he has written columns for newspapers such as the Financial Times and Observer and is regular commentator on radio and TV on the business of sport. He has been engaged as a consultant both by regulators such as the OFT (he was an expert witness in the Premier League Broadcasting case) and by governing bodies such as the FIA in motor sport and International Cricket Council.