

News Corporation/ British Sky Broadcasting

Preliminary Briefing to Office of Fair Trading

1. INTRODUCTION

- 1.1 This briefing paper is provided by News Corporation ("News") in respect of the possible offer by News to acquire the entire issued and to be issued share capital of British Sky Broadcasting Group plc ("Sky") that News does not already own (the "Transaction").
- 1.2 The Transaction is a concentration with a Union dimension and is therefore subject to mandatory notification to, and approval by, the European Commission (the "Commission") under the EU Merger Regulation ("EUMR"). Pre-notification contacts are underway with the Commission.
- 1.3 The Transaction would be subject to the UK City Code on Takeovers and Mergers. It is therefore important for transaction planning and financeability purposes that the parties can ensure, as far as possible, an efficient and speedy review of the Transaction under relevant merger control rules.
- 1.4 The purpose of this briefing paper is to provide the OFT with background information on the Transaction and its UK context.
- 1.5 For the reasons set out below, News believes that the potential impact of the Transaction on competition should be appropriately reviewed by the Commission in its entirety. In summary:
 - (a) The general principle underlying the allocation of merger control cases between the Commission and national authorities is that cases should lie where they fall according to the thresholds laid down under the EUMR, unless there are exceptional reasons to transfer jurisdiction from one authority to another. Where, as here, a transaction falls to be reviewed by the Commission, Article 9 EUMR provides for referral back only if specified pre-conditions are met. None of the conditions in Article 9(2)(a) and 9(2)(b) EUMR are met in this case. The Transaction does not pose any threat to competition in any distinct national market, so there is no ground for the OFT or any other national authority to seek a referral back.
 - (b) The parties are active in more than one Member State (for example, the UK, Ireland, Germany and Italy) and the affected markets may be broader than national in scope. The TV channels provided by Sky and News from the UK are provided in substantially the same form to consumers in the UK and Ireland and the two territories comprise a single language unit. Therefore, the Commission is the best placed authority to review the effects of the Transaction across more than one Member State.
 - (c) None of the factors in the OFT's own jurisdictional and procedural guidance which indicate when the OFT would normally request a referral back apply in this case. The Transaction concerns more than one EU Member State and the affected markets may be broader than national in scope. Under these conditions, it is appropriate for a single authority, i.e. the Commission, to review the Transaction in order to achieve a full appraisal of the competitive context and effects of the Transaction.
 - (d) There are no other material public interest issues from the UK perspective that would need to be coordinated with any competition law review of the Transaction.

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Even if there were material public interest issues, such issues could be addressed by the UK authorities without any referral back under Article 9 EUMR.

- 1.6 As the OFT will appreciate, the matters disclosed in this briefing paper are highly sensitive. Therefore, the information provided should not be disclosed to third parties beyond the OFT case team who are dealing with this matter without News' prior written consent.

2. OVERVIEW OF THE TRANSACTION

The Parties

- 2.1 **News:** News is a diversified global media company with operations in eight industry segments: filmed entertainment; television; cable network programming; direct broadcast satellite television; integrated marketing services; newspapers and information services; book publishing; and other. News had total assets as of 30 June 2010 of approximately US\$54 billion and total annual revenues of approximately US\$33 billion for the fiscal year ended 30 June 2010.
- 2.2 The activities of News are conducted principally in the United States, Continental Europe, the United Kingdom, Australia, Asia and Latin America.
- 2.3 News is a Delaware corporation whose shares are listed on the New York and Australian Stock Exchanges. News has a secondary listing on the London Stock Exchange.
- 2.4 News owns 39.14% of the shares in Sky, which entitle it to exercise 37.19% of the voting rights in Sky. According to the UK Competition Commission, News at present enjoys an ability materially to influence the policy of Sky.¹
- 2.5 **Sky:** Sky is a holding company for a number of subsidiaries, which are active in a variety of economic sectors in the UK and Ireland, including:
- (a) the creation of "linear" TV channels (i.e., channels offering a series of programmes which are available to view at a scheduled time of broadcast). Sky's linear pay TV channels are supplied on a wholesale basis to cable, DTT, and IPTV operators for them to retail to their subscribers in the UK and Ireland. Sky also broadcasts a number of its TV channels FTA (or free-to-view) via digital direct to home ("DTH") satellite and via digital terrestrial TV ("DTT");
 - (b) the retail distribution of Sky's and third parties' linear pay TV channels via DTH, IPTV, the Internet (via *Sky Player*),² and mobile technologies;
 - (c) the retail distribution of Sky's and third parties' "audiovisual programming" (referring to all types of content that satisfies consumers' demand for audiovisual services, regardless of how they are made available to consumers) via the services known as *Sky Anytime* and *Sky Player*. *Sky Anytime* is available to Sky DTH subscribers via a compatible Sky DTH set top box, and offers viewers at any one time a collection of about 30 hours of audiovisual programming "on-demand" (i.e., available for viewing at the time of the viewer's choosing, also called "video on demand" or "VOD");
 - (d) the provision of retail telephony and broadband services to Sky's residential DTH subscribers;

¹ Acquisition by British Sky Broadcasting Group Plc of 17.9% of the shares in ITV Plc, 14 December 2007.

² *Sky Player* is an online application available over the Internet via PCs, games consoles and other consumer electronic devices.

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- (e) the provision of conditional access, access control, and electronic programme guide ("EPG") services to broadcasters and interactive service providers on Sky's DTH platform;
- (f) through Sky's advertising sales house, Sky Media, the sale of advertising and sponsorship on Sky's and third parties' channels, advertising around audiovisual programming available on *Sky Anytime* and *Sky Player*, and the sale of advertising space and sponsorship to companies wishing to advertise on or sponsor Sky's websites and certain third party websites, including the sale of goods and services on those websites;
 - (i) interactive services on Sky's DTH platform;
 - (ii) the provision of fixed-odds betting services; and
 - (iii) small business and corporate network services.

2.6 Sky is a public company whose shares are listed on the London Stock Exchange.

Rationale of the Transaction

- 2.7 Sky has achieved significant success over the years and News believes that the business would continue to have a successful future under News' outright ownership.
- 2.8 The acquisition of the entire share capital of Sky constitutes an opportunity for News to achieve financial consolidation for a company with which it has been closely associated for a long time, and which is mainly active in a sector (pay TV), which constitutes a core business for News. The Transaction will also allow News to diversify the geographic scope of its activities, as well as its earning base, whilst reducing its exposure to cyclical advertising revenues and increasing its direct consumer subscription revenues.

The Transaction structure

- 2.9 The Transaction contemplates the acquisition by News of up to 100% of Sky's shares. After the implementation of the Transaction, News would exercise sole control over Sky.
- 2.10 The Transaction would be subject to the City Code on Takeovers and Mergers and would be implemented by way of a public offer or court approved scheme of arrangement.

Timetable and regulatory review

- 2.11 On 15 June 2010, News made an announcement pursuant to Rule 2.4 of the City Code on Takeovers and Mergers of a possible offer to acquire the entire issued and to be issued share capital of Sky that News does not already own.
- 2.12 Pursuant to a Cooperation Agreement entered into by News and Sky on 15 June 2010, Sky has agreed to co-operate with News in seeking any necessary merger clearances in relation to the Transaction from the relevant merger control authorities.
- 2.13 For further details, please refer to the News press release dated 15 June 2010 at **Annex I**.

3. JURISDICTION

- 3.1 The Transaction would be a concentration with a Union dimension which would be subject to mandatory notification to the Commission.

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- (a) News does not currently exercise decisive influence over Sky for the purposes of the EUMR. In particular, based on the attendance at Sky's last four general shareholder meetings, News' current 37.19% of the voting rights would not allow News to exercise the majority of the voting rights at the next meeting and/ or to block any strategic decision.
- (b) The jurisdictional thresholds under the EUMR are satisfied since:
 - (i) the combined worldwide turnover of News and Sky exceeded Euro 5 billion in the most recent financial year;
 - (ii) each of News and Sky generated turnover in the European Union exceeding Euro 250 million in the most recent financial year;
 - (iii) News and Sky did not generate more than two thirds of their Union-wide turnover in one and the same Member State in the most recent financial year.

4. REVIEW BY BEST PLACED AUTHORITY

- 4.1 News submits that the proposed Transaction should be appropriately reviewed in its entirety by the Commission as the best placed authority and that a request for referral for review by the OFT pursuant to Article 9 EUMR would not be justified, for the following reasons:
- (a) the criteria for a potential referral back under Article 9 EUMR are exceptional and are not met in this case;
 - (b) the Transaction relates to economic activities in more than one Member State, which are best addressed by the Commission;
 - (c) no relevant factor in OFT guidance when requesting referral back is present in this Transaction; and
 - (d) there are no UK public interest issues that would require a coordinated review of both competition and other public interest factors.

The criteria for a referral back under Article 9 EUMR are exceptional and not met in this case

- 4.2 The general principle underlying the allocation of merger control cases between the Commission and national authorities is that cases should lie where they fall according to the thresholds laid down under the EUMR, unless there are exceptional reasons to transfer jurisdiction from one authority to another.
- 4.3 Where, as here, a transaction falls to be reviewed by the Commission, Article 9 EUMR provides for referral back only if specified pre-conditions are met. The criteria for a referral under Article 9(2)(a) EUMR are not met, since the Transaction does not pose any threat to competition in any distinct national market. The criteria for a referral under Article 9(2)(b) EUMR are not met either, since the Transaction affects markets which are UK wide at the narrowest and constitute a "substantial part of the common market". Therefore, there is no ground for the OFT or any other national authority to seek referral back, nor any ground on which the Commission might properly grant a referral back.

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The Transaction relates to economic activities in more than one Member State

- 4.4 The parties are active in more than one Member State (for example, the UK, Ireland, Germany and Italy) and the affected markets may be broader than national in scope. The TV channels provided by Sky and News from the UK are provided in substantially the same form to consumers in the UK and Ireland and the two territories comprise a single language unit. Therefore, the Commission is the best placed authority to review the effects of the Transaction across more than one Member State.

No factor in OFT guidance when requesting a referral is present in this Transaction

- 4.5 The OFT's own jurisdictional and procedural guidance³ sets out detailed guidance on the factors to be taken into account by the OFT in deciding whether to request that a case be referred back from the Commission. None of the relevant factors are present in this case.
- (a) UK dimension: The Transaction concerns more than one EU Member State and markets that may be broader than national in scope. It is therefore appropriate for a single authority, i.e. the Commission, to review the Transaction in order to achieve a full appraisal of the competitive context and effects of the Transaction.
 - (b) Experience: The Commission has recently examined transactions relating to News and has relevant experience in dealing with transactions in the broadcasting sector, transactions concerning News and transactions in the pay TV sector in particular.⁴
 - (c) Other transactions: The parties are not aware of any similar transaction in the same sector that is being reviewed or will be subject to review by the UK competition authorities in the near future.
 - (d) Remedies: There are no substantive competition concerns in this case that would justify remedial action by the OFT, as set out in more detail in section 5 below.

No public interest issues from the UK perspective

- 4.6 The Transaction does not give rise to any concerns justifying intervention on public interest grounds under UK law for the following reasons:
- (a) the Transaction does not fall under any scenario contemplated by the relevant UK policy on intervention in media public interest cases⁵;
 - (b) there will be no material effect on the range or quality of plurality of news media available to any relevant audience;
 - (c) even if the Secretary of State for Business, Innovation and Skills ("SoS") were to consider that there would be a reduction in plurality as a result of the acquisition of *de jure* control following the Transaction, there will be a sufficient number and diversity of sources of news to protect plurality; and
 - (d) the regulatory framework contains further safeguards of plurality.

³ Mergers: Jurisdictional and procedural guidance (OFT 527).

⁴ For example, Case COMP/M.2876, *News Corp/Telepiù*, 2 April 2003. On 20 July 2010, the Commission announced that it has relieved Sky Italia from one of the commitments given in the context of the 2003 News Corp/Telepiù merger in order to allow it to bid in the tender for the allocation of digital terrestrial multiplexes in Italy. See, also, Case COMP/M.5121, *News Corp/Premiere*, 15 June 2008.

⁵ Enterprise Act 2002: Public Interest Intervention in Media Mergers, Guidance on the operation of the public interest merger provisions relating to newspaper and other media mergers, May 2004.

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- 4.7 Even if there were material non-competition issues, such issues could be addressed by the UK authorities without any Article 9 referral.
- 4.8 Therefore, there is no basis for UK reviews on competition and public interest grounds to be coordinated and no additional factor that the OFT should take into account when deciding whether to request a referral back under Article 9 EUMR.
- 4.9 The parties have provided the Department of Business, Innovation and Skills with a briefing setting out the absence of issues which would justify the SoS intervening in the Transaction on public interest grounds.

5. UK COMPETITIVE CONTEXT OF THE TRANSACTION – ABSENCE OF COMPETITION CONCERNS

- 5.1 News is engaged in pre-notification discussions with the Commission. In order to give advance notice to the OFT of the competitive analysis to be addressed in the Form CO, News sets out below the potential effects of the Transaction by reference to a number of different frames of reference, even though some of the sectors identified in the Form CO are likely to be too narrowly defined to constitute relevant economic markets.⁶
- 5.2 News has identified the following sectors as being of potential relevance to the Commission's assessment of the Transaction:
- (a) the licensing/acquisition of audiovisual content;
 - (b) the wholesale supply/acquisition of TV channels;
 - (c) the provision of audiovisual content to end users;
 - (d) the provision of pay TV technical services;
 - (e) the provision of advertising space;
 - (f) the provision of fixed telephony services; and
 - (g) the provision of broadband Internet services.
- 5.3 News will submit to the Commission that it is not necessary to conclude on the appropriate market definition for the purposes of the competitive assessment of the Transaction. On any plausible approach to market definition, the Transaction cannot be expected to lead to a significant impediment to effective competition.
- 5.4 For the reasons set out below, News will argue in the Form CO that the Transaction does not give rise to material horizontal or non-horizontal competition concerns as regards any possible market segment.

Absence of horizontal competition concerns

- 5.5 News submits and will invite the Commission to conclude that, even if narrow market definitions were adopted in respect of segments of the various activities identified above, **the Transaction does not give rise to material horizontal competition concerns as regards any possible market segment.** For the purposes of its competitive assessment, News will examine, in the Form CO, market segments in the UK and Ireland

⁶ When considering the competitive context of the Transaction, News draws to the attention of the OFT the conclusion of the Competition Commission in its assessment of Sky's proposed acquisition of a 17.9% interest in ITV, namely that the relevant market in which Sky operates is a UK market for all TV, which includes both pay TV and free to air services. (Acquisition by British Sky Broadcasting Group Plc of 17.9% of the shares in ITV Plc, 14 December 2007, para.4.37)

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where the parties overlap or might be considered to overlap, recognising that certain of the markets may be wider than national.

- 5.6 Although both News and Sky are active in the licensing and in the acquisition of audiovisual content in the UK, there is no overlap between News and Sky in the licensing and acquisition of broadcasting rights for films and/or sports. With respect to the licensing and acquisition of broadcasting rights for other (non-film, non-sport) TV content, their combined market shares are very limited.
- 5.7 There is an overlap between the parties' activities in the wholesale supply of TV channels in the UK and Ireland; however, in light of News' very small share in the UK (both in terms of viewer share and of revenues) and the *de minimis* market share increase deriving from the Transaction, the Transaction will not give rise to horizontal competition concerns.
- 5.8 In addition, News is not a potential competitor in the other segments of the UK TV sector in which Sky is active. In particular: (1) News has no plans to enter these sectors on a stand-alone basis, nor is News "uniquely well placed" as "the most significant potential source of competitive constraint" in these sectors; and (2) all relevant markets within the TV sector are characterised by intense and dynamic competition.

Absence of non-horizontal competition concerns

- 5.9 Based on the above market segmentations and available information on the parties' relevant activities, News submits and will invite the Commission to conclude that, even if narrow market definitions were adopted in respect of segments of the various activities identified above, **the Transaction does not give rise to material non-horizontal competition concerns as regards any possible market segment.** For the purposes of the current competitive assessment, News has examined relevant market segments in the UK, recognising that certain of the markets may be wider than national.

5.10 In summary:

- (a) The Transaction will not give rise to any non-horizontal anti-competitive effects in any of the following potentially relevant markets: (1) *licensing/acquisition of audiovisual content (and, in particular, film content)*; (2) *wholesale supply/acquisition of TV channels*; (3) *provision of audiovisual content to end users*; (4) *provision of pay TV technical services and, in particular, conditional access system services and middleware*; and/or (5) *provision of online news content*.
- (b) With respect to the *licensing/acquisition of audiovisual content*, the Transaction will not give News the ability or incentive to limit competitor access to audiovisual content supply (i.e. input foreclosure) since, *inter alia*, News does not hold any market power in the licensing of audiovisual content, including films and/or other TV content. Moreover, post-Transaction, the market will continue to be characterised by the presence of strong competitors with at least equally attractive content.
- (c) The Transaction will not give rise to any customer foreclosure effect either, since, *inter alia*, post-Transaction, Sky will continue to have a strong incentive to source TV content (other than TV channels) from licensors other than News. Given News' very limited market position in the supply of TV content and the fact that, in order to continue to be successful, Sky will need to provide to end users as much interesting content as possible, it is simply implausible that, post-Transaction, Sky would stop sourcing TV content from third parties.

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- (d) Similar considerations to those outlined above with respect to the lack of input and customer foreclosure with respect to News' TV content equally apply to the market for the *wholesale supply/acquisition of TV channels*. Post-Transaction, the market for the wholesale supply of TV channels will continue to be characterised by the presence of strong competitors, such as, *inter alia*, ESPN, Discovery, Viacom, and Disney, which excludes any input foreclosure concern. Moreover, News will not have the ability (due to Sky's obligation to grant third party channel broadcasters access to its DTH platform) and/or the incentive (since Sky's continued success will depend on its ability to offer viewers the broadest variety of channels) to exclude third party channel broadcasters from Sky's platform or to stop sourcing TV channels from third parties.
- (e) With respect to the *provision of audiovisual content to end users* since the Transaction will not enhance Sky's access to third party and/or News content in the UK, Ireland, or elsewhere, it will not have any material impact on Sky's position in the provision of audiovisual content to end users.
- (f) With respect to the *provision of pay TV technical services and, in particular, conditional access system services and middleware*, the Transaction will also not have any anti-competitive effects. News will not have the ability or incentive to reserve NDS' conditional access system services and middleware for the merged entity (i.e. no input foreclosure). NDS' market share in the provision of both conditional access services and middleware is below 30% and there are a number of competing providers. Moreover, NDS' other jointly controlling shareholder, Permira, will not allow News to use NDS in such a way that may benefit the News group entities to the detriment of NDS' best interest. Furthermore, Sky's set-top-boxes are currently produced exclusively for Sky's captive use.
- (g) Even if the merged entity sourced all of its pay TV technical services requirements only from News, this would not significantly affect the available customer base or competing pay TV technical services providers (i.e. no customer foreclosure).
- (h) Finally, the Transaction would not give rise to any non-horizontal anti-competitive effect as a result of the combination of the parties' activities in the provision of TV services and News' *publishing activities* and, in particular, the provision of on-line newspaper subscriptions. First, any possible offer of packaged deals including Sky's pay TV services and News' on-line newspaper subscriptions would not have any foreclosure effect and, in fact, would likely increase competition. Secondly, post-Transaction, News will not have the ability and/or the incentive to engage in any tying practice between these services.

No adverse or material change in the competitive dynamic between the parties in the UK

- 5.11 In assessing the competitive context of the Transaction, it is relevant to note that the Transaction does not give rise to an adverse or material change in the competitive dynamic between the parties in the UK, given the *de minimis* overlap between their activities and the limited non-horizontal relationship between their activities.
- 5.12 For completeness, News notes that the Commission will also be able effectively to review the Transaction in its entirety in parallel with the Competition Commission's investigation of the pay TV movies sector, and in parallel with the Competition Appeal Tribunal's review of Ofcom's decision to regulate Sky's sports channel offerings pursuant to its Broadcasting Act powers. The currency of these other proceedings does not justify a referral back under Article 9 EUMR.

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6. CONCLUSION

6.1 In conclusion, News submits that the proposed Transaction should be appropriately reviewed in its entirety by the Commission as the best placed authority and that there is no basis on which the OFT should request a referral back under Article 9 EUMR, on the basis that:

- (a) the criteria for a potential referral back under Article 9 EUMR are exceptional and are not met in this case;
- (b) the Transaction relates to economic activities in more than one Member State, which are best addressed by the Commission;
- (c) no relevant factor in OFT guidance when requesting referral back is present in this Transaction; and
- (d) there are no UK public interest issues that would require a coordinated review of both competition and other public interest factors.

6.2 News would be happy to provide further information to the OFT in relation to any of the points raised above.

6.3 Should you have any questions, please do not hesitate to contact John Pheasant (on direct line [REDACTED] or email at [REDACTED]) or Suzanne Rab (on direct line [REDACTED] or email at [REDACTED]) or Andrea Appella at News (on direct line [REDACTED] or email at [REDACTED]).

17 August 2010

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Annex I

News' Press release dated 15 June 2010

News Corporation Proposes To The Board Of British Sky Broadcasting Group Plc A Cash Offer Of 700 Pence Per Share For The British Sky Broadcasting Group Plc Shares It Does Not Already Own