Bundling of telecom services and content in the Netherlands

Analysis of the possible consequences for competition

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Authority for Consumers & Markets

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1 Introduction

Over the past 10 years, the bundling of telecom services has played an increasingly important role in the Netherlands, as in many other European countries. In recent years, particularly in 2015 and 2016, in addition to tripleplay packages comprising internet, fixed telephony and television, mobile services have increasingly been included, leading to the emergence of quadplay.

Many telecom service providers are vertically integrated and operate on multiple levels of the distribution chain. That means they not only provide services for consumers and businesses, but also operate as suppliers and buyers in wholesale markets. A number of large providers in the Netherlands not only bundle fixed and mobile telecom services, but also add content to their bundles (for example certain sports broadcasts on premium TV channels).

ACM expects these developments to have a major impact on the telecom landscape and competition. The purpose of this study is to investigate the impact of fixed-mobile bundling and content integration on competition in the telecom markets. Although bundling can be advantageous for consumers, ACM also identifies various risks resulting from this trend. In this report, ACM describes the current market situation, i.e. with access regulation in force.

ACM has already examined the bundling of telecom services (particularly dualplay and tripleplay) in past market analyses. ACM monitors these multiplay offers in its Telecom Monitor. The relationship between telecom services and content markets is more recent, and ACM has not previously studied its impact on competition. It aims to further deepen its knowledge of the integration of content with telecom markets by means of this study.

This study fits within the theme of *The Online Consumer* that is part of ACM's agenda for 2016-2017. ACM believes it is important that there is fair competition and that consumers have sufficient choice. To guarantee this, it is important to be well-informed about developments in the market. This enables ACM to identify any problems at an early stage.

In order to compile this report, ACM spoke to a large number of market participants, including telecom service providers, content providers and OTT operators. It also spoke to the Ministry of Economic Affairs and the Ministry of Education, Culture and Science.

This report will show that it is not possible to define an all-embracing assessment framework and that determining whether particular conduct is pro-competitive or anti-competitive is no easy matter. This depends on the specific situation and must be analyzed on a case-by-case basis. In this report, ACM describes the factors that must be included in an assessment.

Responses

ACM requested the parties concerned to respond to an earlier draft of its analysis, and asked specific consultation questions. In total, ACM received 11 responses from the parties concerned, on the basis of which it amended its analysis. In sections 3.1.3 and 3.2.3, it summarizes how the parties view the effects of bundling and the vertical relationships of internet/TV providers with content. ACM draws interim conclusions in sections 3.1.4 and 3.2.4, followed by a final conclusion in chapter 4.

2 Description of the offer and market developments

2.1 Description of the Dutch telecom landscape

2.1.1 Internet service providers

A characteristic feature of the Netherlands is that there are two major internet service providers[1] (hereinafter: ISPs), each operating almost nationwide networks. These are KPN and VodafoneZiggo. Like most other providers, these ISPs offer a wide range of services, such as internet, television and fixed telephony, as well as bundles containing these components. In the retail broadband market, KPN and VodafoneZiggo both have market shares of 40-45% based on the number of connections. In the television market, KPN's market share is lower than that of VodafoneZiggo (figure 1), but KPN's share is growing. In the mobile market, there are four providers, each operating their own network. KPN is the largest in this market, followed at some distance by VodafoneZiggo (see figure 2).

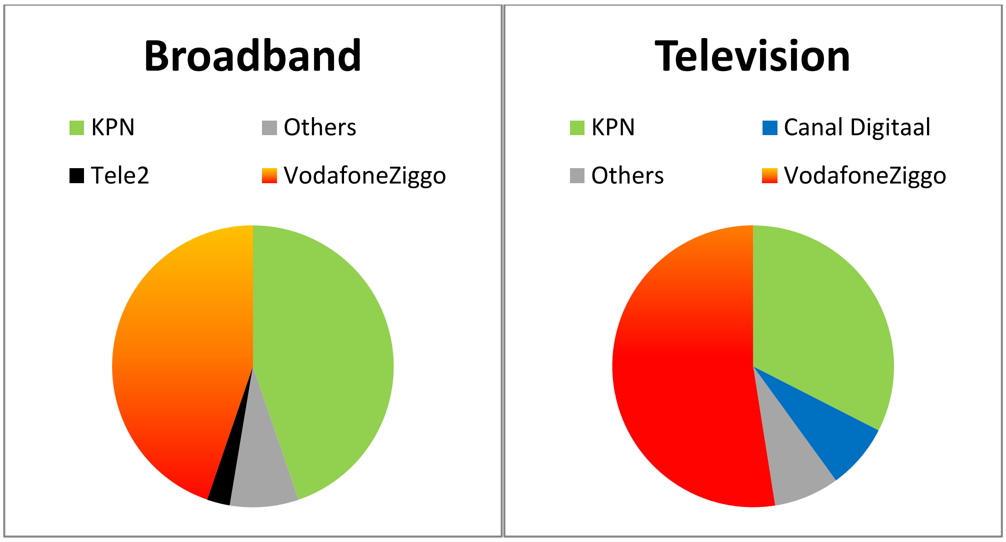

Figure 1: Retail market shares of broadband and television connections in Q4 2016, source: ACM Telecom Monitor[2]

[1] In this study, the term 'internet service provider' means an operator that provides access to the internet by means of a cable, copper or fiber-optic network.
[2] The Telecom Monitor shows market shares within a 5% range. For this chart, the mid-point of the range has therefore been used in each case (e.g. 40-45% is shown as 42.5%).

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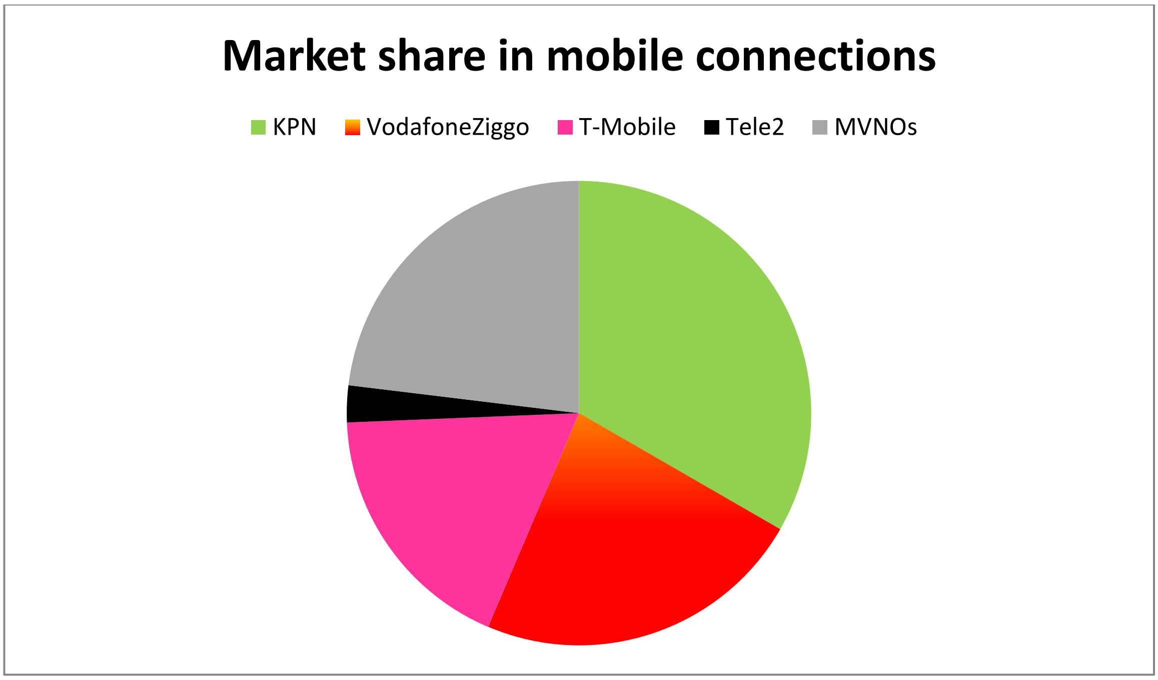

Figure 2: Retail market share in mobile connections in Q4 2016, source: ACM Telecom Monitor

2.1.2 Providers without their own network

Competition in the broadband market is maintained by means of access regulation. KPN is required to open its network to other market participants, so that they can also use that network to serve customers. The largest providers purchasing wholesale access are Tele2, T-Mobile and Online. These ISPs' fixed-line activities would not be possible without access to KPN. That means they depend on continued regulation or the goodwill of KPN or VodafoneZiggo in allowing competitors to access their networks.

Providers without their own network also operate in the mobile market. These are various MVNOs, largely operating in the prepaid segment. There is no access regulation in the case of mobile networks, because there are already four competing networks. All access agreements in this market have therefore been concluded on the basis of commercial considerations.

2.1.3 Market entry

Both the mobile and fixed markets involve high network investment costs. In the fixed market, the required investments are even so high that it would be impossible for a provider to enter the market by building its own network from scratch. A provider could roll out its own network to a limited extent, but access to existing infrastructures is essential in order to provide national coverage.

In the mobile market, too, providers enter the market almost exclusively by purchasing access from providers that have their own network. An exception to this is entering the mobile market by means of an auction, as Tele2 did several years ago in the 4G frequency auction.

2.2 Quadplay

Tripleplay packages have been available for many years. Quadplay packages have been available since the beginning of 2013. KPN now reports that it is supplying quadplay to more than a million households (see figure 3). VodafoneZiggo also started offering quadplay at the beginning of 2017. T-Mobile is expected to introduce a quadplay offer.

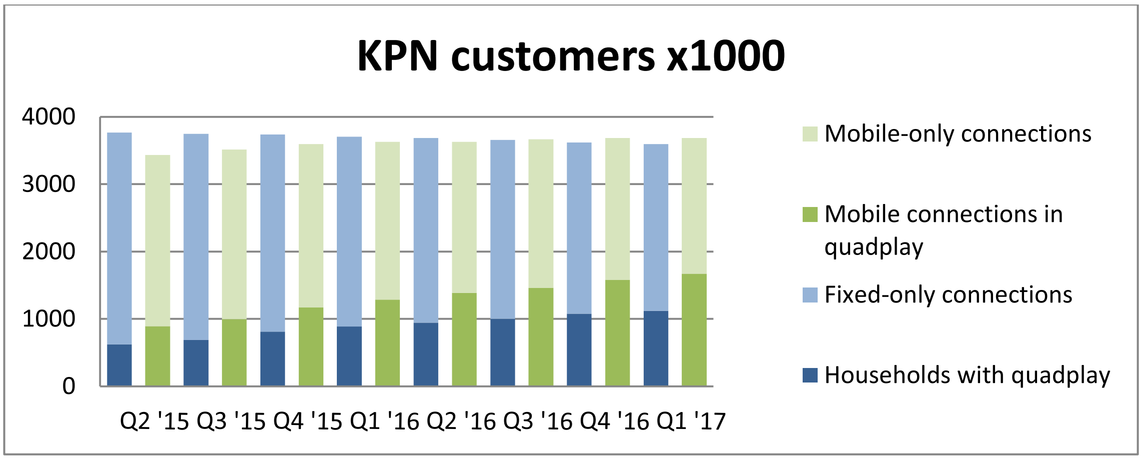

Figure 3: Number of KPN customers with and without quadplay, source: fact sheets at ir.kpn.nl. (N.B.: customers have an average of almost 1.5 mobile connections in their quadplay package. That means the number of mobile connections in quadplay exceeds the number of households with quadplay).

2.2.1 Quadplay offer

KPN offers an extensive package of benefits for customers purchasing both mobile and fixed services. Customers receive a €5 discount on mobile, a doubling of the mobile data bundle, free calls within the household and a choice of various television packages. The VodafoneZiggo offer is almost the same. The only difference is that VodafoneZiggo does not provide free calls among users, but does offer an online security package.

It is important to note that, in all cases, there are two (or more) separate contracts. Currently there is no provider offering a customer both fixed and mobile services under the same contract. However, customers do not always have a choice of which products to purchase. A VodafoneZiggo customer, for example, cannot purchase an internet connection without a television connection, while in the case of all DSL providers the opposite applies. A combination of mobile and fixed or vice versa is never compulsory, however.

2.3 Content

In addition to standalone or bundled mobile and fixed services, ISPs are also increasingly investing in content. These investments are not a new phenomenon. KPN invested in Sport7 back in the mid-1990s.[3] ISPs have also invested in content over the past few years. In particular, Ziggo's parent company Liberty Global (LG) does this on a large scale. It owns the Formula 1 rights, for example, for which it can sell the broadcast rights. LG's owner is also the majority shareholder in Discovery. LG also acquires many sports rights and broadcasts the coverage through its channels *Ziggo Sport* (free for Ziggo customers) and *Ziggo Sport Totaal* (paid channel that is also available to customers of other ISPs).

There have recently been various cases in which regulators viewed the acquisition of content as problematic. In the United Kingdom, for example, the British telecom regulator Ofcom compelled Sky to make the Premier League football rights it had acquired available to other market participants at regulated wholesale rates in 2010. This obligation was introduced to allow other ISPs to access important input in order to compete. Ofcom withdrew this obligation at the end of 2015 because BT was then providing sufficient competition with its own sports channel and because Sky itself signed commercial agreements with other distributors.[4]

A relatively new feature in the Netherlands is that both VodafoneZiggo and KPN are currently offering certain content exclusively to their customers. VodafoneZiggo, for example, signed a contract with HBO to offer its content on an exclusive basis. VodafoneZiggo customers can also watch certain sports content free on *Ziggo Sport*, while customers of other ISPs only have access to this content if they subscribe to *Ziggo Sport Totaal*. KPN has started making a number of in-house productions that are available exclusively to its own customers on the *KPN Presenteert* channel. This channel is also available to customers of other ISPs if they are prepared to subscribe additionally to the *KPN Play* OTT TV service. Providers are also increasingly adding extra content to their packages. KPN and VodafoneZiggo, for example, are giving customers access to extra content with quadplay. VodafoneZiggo and T-Mobile are also including certain extra content in the basic package (*Ziggo Sport* in the case of Ziggo and *Fox Sports Eredivisie* in the case of T-Mobile). ISPs are thus increasingly seeking to distinguish themselves from each other through content. Nevertheless, ACM also sees risks that this development could reduce competition, particularly as it seems to be taking place mainly among ISPs with large market shares. ACM has also received indications that vertical relationships between ISPs and content providers are giving rise to problems due to ISPs offering content on an exclusive basis. ACM will discuss the possible risks in greater detail in the following chapter.

[3] https://nl.wikipedia.org/wiki/Sport_7.
[4] Ofcom (2015), "*Review of the pay TV wholesale must-offer obligation*".

2.3.1 Relationships between content providers and ISPs

Content can reach the user in two ways:

1. Through the ISP, for example when NPO 1 (which is one of the main Dutch public broadcasting channels) is broadcast on linear television.
2. Directly via the internet (this is referred to as an over-the-top, or OTT, service), the best-known example being Netflix.

Certain content is available on both channels. That is the case, for example, of NPO, which broadcasts most of its programs both on television and on the internet. A list of the various providers in the chain can be found in figure 4.

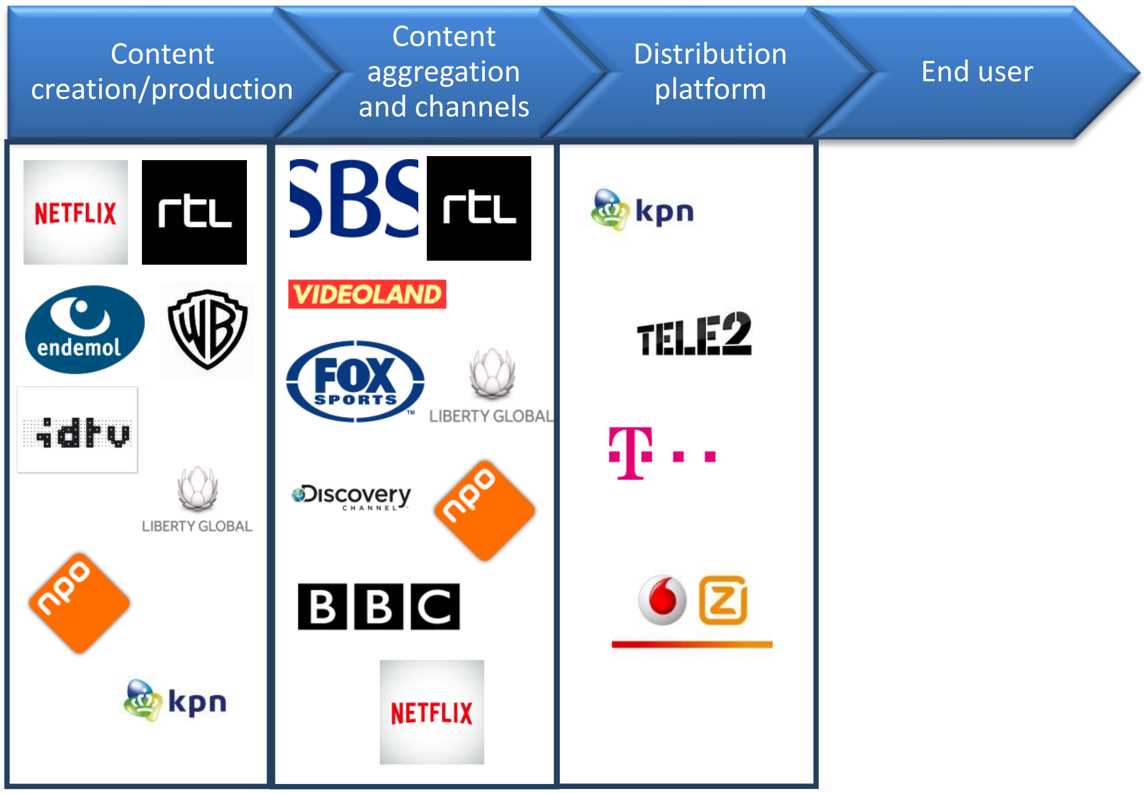

Figure 4: Content value chain

2.3.2 The Dutch Media Act

To ensure that consumers have access to certain highly valuable content, the Dutch Media Act includes a list of events. This list contains events which must be broadcast on an open network, such as highlights of the Eredivisie, which is the top division of the Dutch football league. An open network is a channel that can be received by at least 75% of all households in the Netherlands.

The list also includes events that only have to be available on an open network if they are broadcast live, for example the football World Cup and the Olympic Games. Since there is no ISP in the Netherlands with a market share of at least 75%, an ISP that has the rights to content on the events list will not be able to make it available to its customers on an exclusive basis.

The Dutch Media Act also includes a must-carry obligation. All television providers with more than 100,000 subscribers must comply with this obligation. This means, among other things, that they must include at least 30 channels in their basic package. Certain channels, such as those of NPO, must be part of the package.

Except with regard to premium channels, customers of most ISPs are not able to compose their own TV package. As a result, when taking out a basic package they receive more channels than the minimum specified in the Dutch Media Act. Research by the Dutch Media Authority shows that, if consumers themselves were able to compose their own TV package, they would include fewer channels than is currently the case.[5]

[5] http://www.mediamonitor.nl/tvpakketten/televisie-a-la-carte-2016/#.

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3 Effect of fixed-mobile bundling and exclusive content on competition

3.1 Fixed-mobile bundles in the Netherlands

In this section, ACM describes the possible consequences of fixed-mobile bundles in the Netherlands. In section 3.1.1, ACM provides the theoretical framework in which the possible advantages and disadvantages of bundling are described. Section 3.1.2 describes potential market distortions resulting from fixed-mobile bundles. In section 3.1.3, ACM provides an overview of market participants' responses to a previous draft of this analysis, followed by a conclusion in section 3.1.4.

3.1.1 Introduction to bundling

The economic literature distinguishes three types of bundling: i. pure bundling, ii. tying and iii. mixed bundling. Pure bundling is where an end-user can only purchase products A and B together and products A and B are not available separately. Tying is where the end user can purchase products A and B together, but one of these products is also available separately. Mixed bundling is where products A and B can be purchased separately, but the sum of the prices of the separate products exceeds the price of the bundled product.

In the case of telecom services, there is mixed bundling and tying. Quadplay offers are an example of mixed bundling in which end-users receive discounts or additional benefits if they purchase fixed and mobile services. Tying normally takes place in the case of fixed telecom services, for example if an internet service has to be purchased whenever the customer wishes to purchase a television service or vice versa.

Providers frequently offer their services as a bundle because that can generate cost advantages. In the case of tripleplay packages, for example, providers can save costs in areas such as marketing, supply, sales and invoicing, and end-users can be given a discount.

The cost benefits for a provider are less evident in the bundling of fixed and mobile services. For the provider, this bundling appears in particular to be a commercial consideration that contributes to customer retention. Quadplay is attractive for end-users due to the lower price.

In discussions with ACM, providers confirmed that the introduction of quadplay reduces switching by customers. Fixed-mobile bundling is used precisely to reduce switching behavior. This relationship between bundling and consumers' switching behavior is also described in the literature.[6]

[6] On this see *inter alia* Prince (2012), "*The dynamic effects of triple play bundling in telecommunications*", Time Warner Cable, *Research program on digital communications,* Report Series Winter 2012. This publication is available online at: http://twcresearchprogram.org/pdf/TWC_PrinceReport.pdf.

In addition to any cost benefits, a possible reason for bundling is that it allows price discrimination through which providers seek to increase their profit and that it can lead to greater usage of services. End-users can also benefit from this, but that does not always happen.[7] Suppose a group of television fans has €15 to spend on television and €5 to spend on voice calls, whereas the reverse applies in the case of a group of frequent callers. If the provider were to offer both products individually for €15, only the television fans would take out a television plan and only the frequent callers would take out a fixed telephony plan. With a price of €20 for a bundle, both groups of end-users will sign up for both products, leading to greater consumer welfare, under the realistic assumption that the marginal costs of television and fixed telephony are lower than €15 and €5 respectively.[8] If the products were sold individually, there would be underconsumption.

	Television	**Fixed telephony**
Television fans	€15	€5
Frequent callers	€5	€15

Table 1: Example of consumer valuation for different telecom services

This positive effect cannot be readily assumed in the bundling of fixed and mobile services. Consumers who are prepared to pay for fixed services generally also purchase mobile services. Providers do not therefore have to use bundling to increase demand.

Bundling and tying can also have negative effects on consumer welfare if they are used by providers with market power to limit entry or foreclose competitors. In these cases, bundling can be used to transfer market power from one market to another. However, this does require the provider to have market power in at least one of the markets. As long as a provider does not have market power, there will still be other providers. End-users then have sufficient options to purchase their individual services or bundles from other providers.

3.1.2 Possible market distortions as a result of fixed-mobile bundling

<u>i. fixed-mobile bundling reduces transparency</u>

Transparency is an important precondition for a well-functioning market. It means that end-users are able to compare the various services in terms of price and quality. As a result, they can make a considered choice based on the elements of the service that are important to them. A significant consequence of this is that providers are forced to offer attractive services at competitive prices. They are therefore disciplined by transparency.

[7] In general, price discrimination can be both advantageous and disadvantageous for consumers as a group.
[8] In this example, the consumer fares equally well with and without a bundle because in both cases the price of the product (television, fixed telephony, or the bundle) that he purchases is equal to his valuation.

Now that mobile plans are increasingly being offered in combination with fixed services, new propositions are emerging. It is becoming more difficult to compare prices, since there are now more price points, and the discounts apply to combinations of multiple products. After all, the various fixed and mobile services are generally still offered separately. Moreover, customers must compare mobile and fixed services at the same time in order to make the right choice.

In the case of bundled *fixed* services, making a good comparison was already complex due to the wide variety of services (download speeds, television channels, add-ons). Research conducted by SAMR on behalf of ACM shows that over two-thirds of all consumers find it difficult to compare bundle prices properly because the products are different.[9] In the case of separate fixed and mobile services, there are often good comparison sites where consumers can compare offers from multiple providers, but this is not (or not yet) the case for fixed-mobile bundles.

With fixed-mobile bundling, the complexity will increase even further if the consumer also has to include mobile services in his comparison. Not only does the number of price points increase, but the consumer can receive a bundle discount in different ways (e.g. additional television channels or a discount on the bill). In addition, in the case of fixed-mobile bundling, new parameters must also be included in the comparison, such as call minutes, data volumes and mobile devices. This makes comparisons of products (including those from different providers) even less straightforward, and may also make it more difficult to select the most suitable product from a particular provider.

ii. Reduced competition due to increased switching costs

In addition to transparency, it is important that consumers can switch easily. If it is possible to switch provider without great difficulty (and high cost), providers are forced to offer attractive services at competitive prices. Otherwise they run the risk that their customers will switch to a competing offer.

If it becomes more difficult to switch, this will not only lead to less competition between existing providers, which could demand higher prices, for example, but potential competition will also be impeded. After all, smaller providers and entrants are less able to gain customers as there are barriers to switching.

A consequence of the bundling of fixed and mobile services is that switching becomes more difficult. This is due, among other things, to the greater lack of transparency as described above. End-users have to invest more time and effort in finding an offer that is favorable for them. This leads to search costs.

Another barrier to switching is of an administrative nature. If a consumer wishes to switch to another

[9] SAMR (2016), *Een op de vijf consumenten switcht binnen telecommarkt",* 14 June 2016. p. 48. Available online at ACM.nl https://www.acm.nl/nl/publicaties/publicatie/16709/Rapportage-consumentenonderzoek-telecommarkt-2016/.

provider for a fixed-mobile offer, he must terminate two contracts and take out two new contracts. Although in practice that often proves less difficult than expected, consumers are generally reluctant to face such administrative hassle.

The main barrier to switching for customers purchasing a fixed-mobile bundle is that they lose their discount or additional services when they switch. Switching providers may then be unattractive particularly when the fixed and mobile contracts are of different lengths. For example, a consumer may have had the same plan for many years and be entitled to terminate it at one month's notice. But if he took out a two-year mobile contract only six months ago, he is stuck with his current provider. Switching for part of the bundle is then unattractive because he loses his discount.

A lower number of switchers as a result of barriers to switching is mainly of interest to large providers that want to retain their strong position. Smaller providers or entrants, meanwhile, have an interest in gaining customers in a more dynamic market. This becomes more difficult as the number of combinations of fixed-mobile services increases. In addition, smaller providers have not yet had the opportunity to build up a strong name. Although less switching behavior is not necessarily a sign of less competition, ACM believes it creates an impediment that stops competitors entering the market and growing.

iii. Risk of fixed-mobile bundling reducing competition by weakening smaller market participants

Since the current access regulation system means there is no party with a dominant position that can behave independently of competitors and end-users, there will be no exclusion due to tying. Regulated access is available under competitive conditions.

In addition to the problems set out above, ACM nevertheless sees a further risk to competition from the growing importance of fixed-mobile bundles. Market participants that only have a mobile network or market participants that have no infrastructure of their own and have to purchase it may be weakened to such an extent that they have to leave the market. That is because providers that depend on wholesale access, such as Tele2 and T-Mobile, incur greater risk and generally have lower margins than providers that have their own networks (KPN and VodafoneZiggo).

There is also a risk that providers having only a very limited telecom infrastructure of their own, i.e. those that also do not have their own mobile network, for example, may disappear from the market. This can mean that consumers who currently take advantage of attractive offers may face higher prices in the longer term if small providers have been weakened or leave the market.

ACM expects this to be a real risk due to the growing importance of quadplay and the good starting positions of KPN and VodafoneZiggo. There is strong growth in quadplay plans, as described in chapter 2. This is particularly because quadplay is attractive to users, due to the convenience and discounts. According to ACM's Telecom Monitor, the number of households with a four-in-one package grew by 6% in the second quarter of 2016 compared with the previous quarter. As was already seen in figure 3, more than a million households now have a plan in which fixed and mobile services are bundled. ACM believes this is due to marketing campaigns by telecom providers. They incentivize customers to take all services from a single provider with attractive discount offers or additional channels. Figure 5 below shows, for example, that consumers who purchase their fixed and mobile services as a bundle from KPN receive a more favorable mobile offer than KPN's mobile-only customers. In its bundled offer, KPN positions itself at a level comparable to that of Tele2 and T-Mobile.

If they have a large customer base, providers can use their existing relationships as a fairly easy way to provide additional services for customers. They consequently start from a better position than small players or entrants. Since smaller providers have a smaller customer base, they have fewer opportunities for cross-selling.

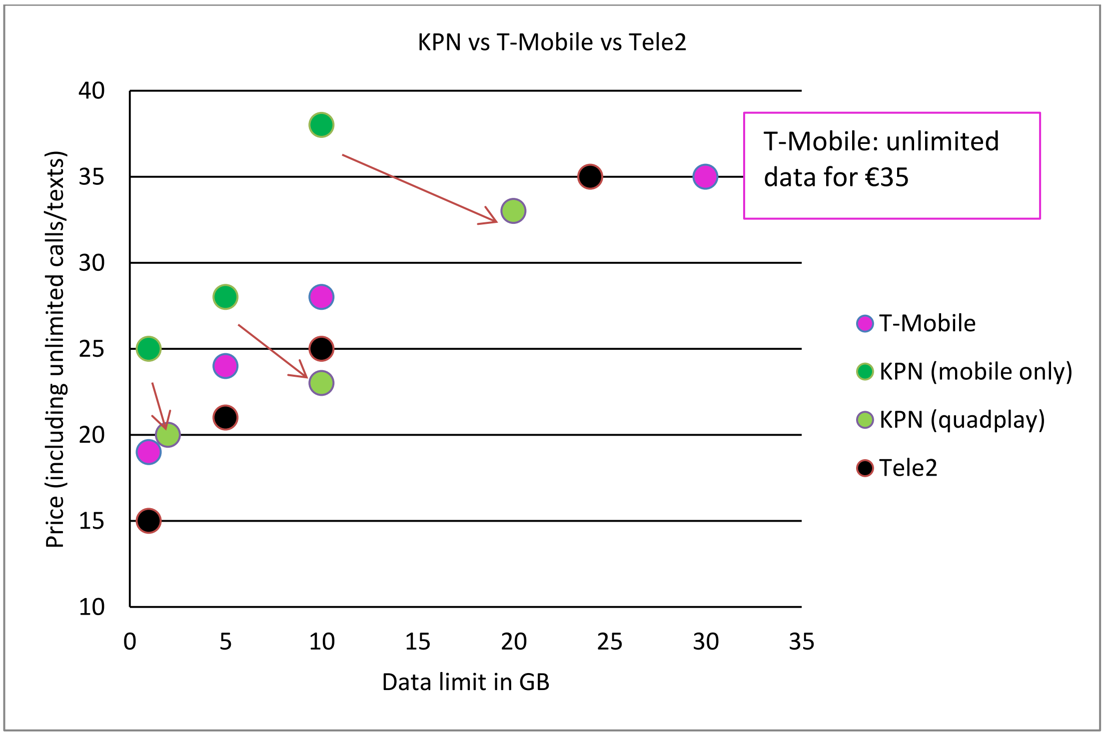

Figure 5: KPN prices with and without quadplay compared to T-Mobile and Tele2 prices (Sources: KPN.com, T-Mobile.nl and Tele2.nl on 22 February 2017).

In practice, ACM finds that smaller providers also have further growth potential. With its acquisition of Vodafone's fixed services, T-Mobile is committing to quadplay and is also expected to grow in the fixed segment. T-Mobile has already been able to achieve strong growth in mobile (postpaid customers) in the past two quarters. T-Mobile is also making a profit in the Netherlands, albeit less than previously, presumably as a result of chasing a bigger market share. ACM's Telecom Monitor also shows that Tele2 is rapidly gaining market share at present. Tele2 is recording losses in the mobile segment, but has only been operating in it for a few years. Tele2 is currently still investing heavily.

Another indication that the risk currently remains limited is the fact that mobile services (i.e. mobile telephony and mobile internet) are as yet no substitute for fixed services. Most consumers purchase both fixed and mobile services. ACM has therefore concluded that fixed and mobile belong to different relevant markets. There are still a large number of services on offer in which fixed and mobile services are not combined and these products still have a disciplining effect on fixed-mobile bundles.

3.1.3 Responses to the consultation

The parties involved in the consultation gave responses on the possible market distortions indicated by ACM. No other notable distortions were cited in the field of fixed-mobile bundling. In their responses, the market participants stated particularly the extent to which they did or did not endorse the risks of market distortions. KPN and VodafoneZiggo also question the importance of bundles of fixed and mobile services. They believe a large part of the market will continue to purchase fixed and mobile services separately.

<u>Transparency</u>

Most responses confirm that the bundling of fixed and mobile services reduces transparency, although some voice doubts as to whether this actually leads to problems. Various market participants state that Dutch consumers are very good at comparing different products online. KPN also stresses that, in the case of fixed-mobile bundles, a consumer only has to compare once rather than twice (for fixed and mobile services separately).

On the basis of the responses, ACM notes that a lack of transparency is not the biggest risk in fixed-mobile bundling. If the trend continues, however, ACM does believe it would be useful if consumers were ultimately able to compare fixed-mobile bundles on independent comparison sites.

<u>Barriers to switching</u>

In their responses to the consultation, most market participants state that barriers to switching pose a substantial risk. The general picture emerging from the responses is that fixed-mobile bundling limits consumers' switching behavior. Various market participants also cite other specific examples of barriers to switching. RTL, which states that it shares ACM's analysis and argues that these barriers do indeed benefit larger providers, points to a number of practical and technical aspects, such as changing passwords, devices, set-top boxes and e-mail addresses when switching to another provider. Tele2 cites barriers linked more specifically to switching in the case of fixed-mobile bundles, such as a lack of clarity on the contract term, supply uncertainty and reliability of the switching, as well as the loss of discounts and exclusive content.

On a related matter, Tele2 points out that mobile plans are not included in the switching service implemented among the various providers. If an end-user with a fixed-mobile bundle wishes to switch, two switching processes are currently involved, and these are not coordinated. That increases the risk of errors. NLConnect[10] suggests in this connection that providers should enter into agreements on switching between fixed-mobile bundles that specify how any differences in fixed and mobile contract lengths will be dealt with.

[10] The NL Connect association has 13 members providing services over fiber-optic or cable networks. The association represents a large number of smaller ISPs.

KPN and VodafoneZiggo state in their responses that a decrease in consumers' switching behavior should not necessarily be seen as a lack of competition. They state that a major reason for a decrease in switching by end-users is rising customer satisfaction, eliminating the need for end-users to switch.

ACM will continue to monitor the extent of switching and, if it detects actual problems, will investigate ways of lowering the barriers.

<u>Less competition due to weakening of smaller providers</u>
In their responses to the consultation, almost all providers consider the relationship between wholesale access and the degree to which any problems could arise. KPN and VodafoneZiggo stress that there is access to KPN's network, so they do not recognize the risk described by ACM. They argue that market participants dependent on wholesale access are also well able to offer quadplay.

Smaller providers that purchase this access confirm the risks outlined by ACM. Online states that the vertically integrated providers with their own networks have a different cost structure than those requiring access. For the latter group, the gross margins are lower as they have to contend with higher variable costs. In addition, barriers to entry have grown due to the emergence of quadplay, as new providers have to purchase more services than was previously the case.

NLConnect emphasizes that small providers with a fixed network also find that it is not easy to negotiate with mobile providers.

On this specific subject, ACM has received little in the way of concrete new input from market participants, but considers that this point poses the biggest risk to competition in the long term. ACM believes that KPN and VodafoneZiggo refer too readily to the access that KPN would offer, even without ACM imposing any access obligations. This is despite the fact that ACM receives regular indications that, even with regulated access, buyers are finding it difficult to gain competitive strength from this access, partly due to the need for closer coordination and costly consultation in relation to the size of the customer base. ACM will monitor closely the position of smaller providers and the risk of it being weakened. This subject will also play an important role in the market analysis on unbundled access, which ACM is currently conducting. In the analysis, ACM is investigating whether it will also be necessary to guarantee wholesale access by means of regulation in the years ahead.

3.1.4 Conclusion

On the basis of the above, ACM notes that the bundling of fixed and mobile services can be advantageous for consumers, particularly because they receive a discount on the services as a whole. For providers, the main reason for offering quadplay appears to be that it helps them retain customers. That is because, in the first place, the market is becoming less transparent due to the introduction of fixed-mobile bundles. A bigger risk is posed by the higher barriers to switching, particularly because consumers lose their discount if they switch part of their services.

The biggest risk is that smaller providers may be weakened or forced to leave the market as a result of quadplay. These providers often rely in part on the infrastructure of other providers, so they find it more difficult to come up with a competitive offer. Although we currently consider that smaller providers also have further growth potential, because many standalone services are still being sold, their position may ultimately come under pressure. ACM will therefore monitor these developments closely. Steps must be taken to prevent the short-term benefits of bundling, such as lower prices and extra services, ultimately disappearing if smaller competitors are weakened and, in the most unfavorable scenario, actually leave the market. That is not a desirable outcome from the competition perspective, because it will lead to higher prices. ACM will devote attention to this in the current unbundled access market analysis.

3.2 Vertical relationships of internet/TV providers with content

In this section, ACM describes the possible impact of exclusive content on competition, having regard to the current market situation in the Netherlands. Section 3.2.1 starts with the theoretical framework for vertical relationships. Section 3.2.2 analyzes the plausibility of three market outcomes resulting from exclusive content. In section 3.2.3, ACM summarizes market participants' responses to a previous draft of this analysis. The conclusion follows in section 3.2.4.

3.2.1 Introduction to vertical relationships

An ISP has two options when it comes to offering content. It can conclude a (vertical) agreement with a content provider or produce the content itself. In the case of an agreement, an ISP must agree on a broadcast license with a content provider. Content providers can be producers without their own sales channels, but also broadcast groups such as RTL, SBS and NPO. These broadcast groups often provide their own content in multichannel packages. If an ISP produces content itself within the group, it is deemed to be a vertically integrated provider (see figure 6). It can do so, for example, by acquiring or merging with content producers or content distributors. However, an ISP can also start developing activities independently to produce content. In both cases, there is a vertically integrated provider that is active in the wholesale market as a content provider and as a distribution platform.

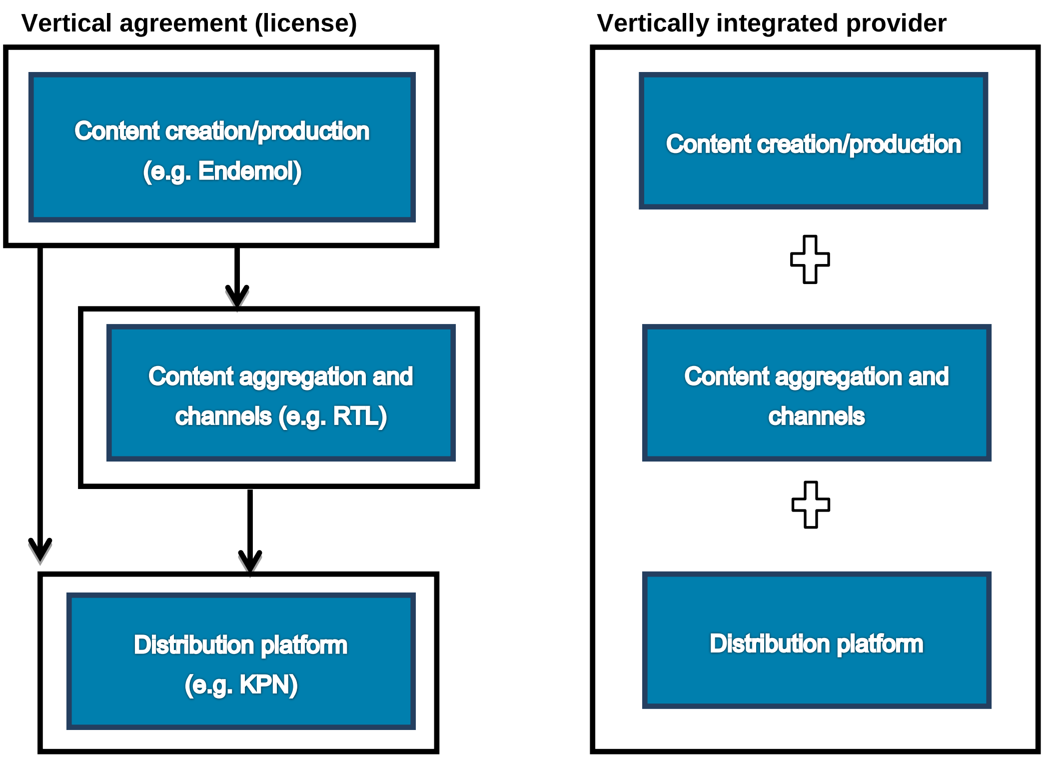

Figure 6: Vertical agreement vs. vertical integration

A closer look at vertical agreements

Some vertical agreements can have negative consequences for competition. An exclusivity clause between an ISP and a content provider could, for example, weaken competition among both content providers and ISPs.

However, vertical agreements are generally speaking not as often anticompetitive as are agreements between competitors (horizontal agreements). Vertical agreements often also have positive consequences for competition and consumers. For example, they can promote economic efficiency in a production or distribution chain by allowing better coordination between undertakings. In particular, they can reduce the market participants' transaction costs and distribution costs, and optimize the level of their sales and investments.[11]

An independent content provider will generally have an incentive to grant multiple licenses, because it has an interest in reaching the largest possible audience. After all, it does not have its own distribution channel. The greater its reach, the more it can increase the value of its content. It is also in a content owner's interest to have multiple ISPs operating in the market, so that the negotiating power is not entirely in the hands of one or two ISPs. The incentives for independent content providers therefore generally appear to be satisfactory. A content provider may nevertheless decide to enter into an exclusive agreement with an ISP. It will do this if the price received exceeds the income it would receive if it granted the license to multiple ISPs without such exclusivity. When licenses are granted for sports content, they usually include exclusivity clauses. We see this to a lesser extent in licenses for movies (premium or otherwise) and series. If the content is made available exclusively to a provider without its own distribution platform, this provider must enter into transfer agreements with one or more ISPs, so that consumers can receive the content. In such a situation, it is possible that (small) ISPs will nevertheless decide not to purchase the content due to high transfer charges.

ACM can assess vertical agreements on the basis of Section 6 of the Dutch Competition Act and/or Article 101 of the Treaty on the Functioning of the European Union (TFEU).

A closer look at vertical integration

A vertically integrated ISP will have more incentive than an independent content provider to secure content exclusively in order to persuade customers of other ISPs to switch because of this content. An ISP then loses income in the short term since it no longer sells the content to competitors. But it does assume that the income will be higher in the longer term since it can attract additional customers to its own network.

If an ISP secures content as a result of an acquisition or merger with a content provider, ACM can assess it within the framework set out by the European Commission in its Guidelines on non-

[11] European Commission Communication of 19 May 2010, Guidelines on Vertical Restraints, OJ 2010/C 130/01 (hereinafter: Guidelines on Vertical Restraints).

horizontal mergers.[12] If an ISP already has its own content and this vertically integrated provider has a dominant position in one of the markets in which it operates, ACM can assess this ISP's practices on the basis of Section 24 of the Dutch Competition Act or Article 102 TFEU and the Guidelines on exclusionary conduct to determine whether a dominant position is being abused.[13]

3.2.2 Possible market outcomes as a result of exclusive content

As already described in section 2.3, most content in the Netherlands is currently available to all ISPs. An exception to this is HBO content, which since 1 January 2017 has been available exclusively to customers of VodafoneZiggo.[14]

In the remainder of this section, ACM will deal particularly with exclusivity and the question of which of the three market outcomes below can result from it:

i. **Increase in competition**
ii. **Exclusion**
iii. **Higher prices**

Even if there is no exclusivity clause and the content is available to all providers, significant price increases can mean that, for small providers particularly, it is no longer profitable to purchase this content. ACM has received indications from providers that they are having to contend with price increases. This is already a problem now according to small providers. A number of these providers that ACM has spoken to in the course of this investigation also consider that broadcasting groups give the larger ISPs more leeway in contract negotiations due to their large volumes. ACM has so far received insufficient concrete information on this matter to include it in the analysis.

<u>i. Exclusive content leads to more competition</u>

ISPs' ability to offer exclusive content can have a positive impact on the competitive relationships in the market. This is because exclusive content enables an ISP to stand out from the rest of the market. In the short term, at any rate, this can benefit consumers, because it generates more competition between providers. As a result of opting for exclusivity, the ISP must gain market share in the retail market to offset the loss of income in the wholesale market. The rest of the market will respond to this (for example with price reductions or by offering extra content), so competition will increase further. For consumers this could mean, for example, that the amount of available content in

[12] European Commission Communication, Guidelines on the assessment of non-horizontal mergers under the Council Regulation on the control of concentrations between undertakings, OJ 2008 C 265/6.
[13] European Commission Communication, Guidance on the Commission's enforcement priorities in applying Article 82 (now 102) of the EC Treaty to abusive exclusionary conduct by dominant undertakings, OJ 2009, C 45/7.
[14] https://www.nrc.nl/nieuws/2016/11/01/hbo-series-naar-nieuw-kanaal-exclusief-voor-klanten-ziggo-a1529603..

the market increases, possibly at more attractive prices than was previously the case. This is currently also reflected in market practice to a certain extent. Various ISPs have expanded the content offering in their basic package to include purchased content or own productions. The content is also increasingly being made available to consumers via non-linear channels.

ii. Exclusive content leads to exclusion

The exclusive offering of content by an ISP could lead to exclusion and thus ultimately even to the departure of ISPs that would not or would no longer have access to this content. This may happen if ISPs are unable to compensate in some way for the lack of important content. This is particularly a risk for small ISPs. The result is that consumers ultimately have fewer ISPs to choose from and the competition in the market decreases. This is contingent on the content or the collection of content to which an ISP has exclusive access being 'must-have'. Views differ as to what constitutes must-have content. A possible definition of must-have content is content or a collection of content that ISPs need in order to compete in the market. Not having this content greatly impairs an ISP's competitiveness. In the most extreme case, this could lead to the exclusion of the ISP concerned.

The existence of must-have content must be analyzed on a case-by-case basis. Moreover, this may change over time. Discussions with market participants, but also reports from foreign regulators such as Ofcom[15], show that must-have content can arise particularly in the case of live sport. The only ISP that currently owns broadcast rights/licenses for sports content is Ziggo within the Liberty Global group. As stated above, this content is also made available to customers of other ISPs through the premium channel *Ziggo Sport Totaal*. This channel also has more sports content than the *Ziggo Sport* channel that is not available to customers of other ISPs. Research by Telecompaper shows that, for 14% of Ziggo customers, *Ziggo Sport* was a reason for not switching to another provider.[16] According to Ziggo, 20% of new customers state that Ziggo *Sport* was a reason for switching to Ziggo.[17] So far, however, *Ziggo Sport* and *Ziggo Sport Totaal* have not led to a significant shift in the television market.

With regard to premium film content, only HBO content can currently be viewed exclusively through a single ISP, namely VodafoneZiggo. Whether the HBO content can be considered must-have depends on the extent to which customers will switch to VodafoneZiggo in order to keep HBO. At present, it is still too early to see the effect of this on the market positions. It is only since 1 January 2017 that Ziggo has offered HBO exclusively to its customers. ACM is already seeing other ISPs reacting to the new situation, however. KPN appears to be compensating its customers for the loss of

[15] Ofcom (2015), "*Review of the pay TV wholesale must-offer obligation*".
[16] http://www.telecompaper.com/achtergrond/ziggo-sport-voor-14-ziggo-klanten-reden-om-te-blijven--1128445..
[17] Liberty Global, Press release, Fiscal 2015 Fixed Income Release, https://www.ziggo.com/resources/documents-new/Quarterly_Reports/Ziggo-Fixed-Income-Q4-2015-Report-Final.pdf.

HBO, for example, by expanding its channel offering in the plus package with extra content.[18] Other ISPs, including Delta[19] and Sparql,[20] are compensating for the loss of HBO in their channel offering with price reductions and/or replacement with other content (e.g. Film1 and Fox Eredivisie).

It is also possible that certain content is not seen as must-have in itself, but is seen as must-have when combined with other content. The more content an ISP acquires, the more likely it is that an overall package will be deemed to be must-have. An ISP can acquire so many major, exclusive content rights that it becomes very attractive for customers to purchase their services from this ISP. The power that this ISP has in the content market can also strengthen its position in neighboring markets. If an ISP acquires more content of the same type (e.g. sport or movies), there is a greater risk that it might abuse its dominant position. Vertical integration between content owners/producers and an ISP increases this risk.

ACM does not currently think it likely that, in the present market situation, the content offered exclusively by ISPs will lead to exclusion and hence to providers leaving the market.

<u>iii. Exclusive content leads to higher prices</u>

A third possible consequence of exclusive content is that offering it will lead to higher prices for consumers. This is because exclusivity gives rise to considerable product differentiation, reducing competition in the market. Since content is mainly offered as part of a bundle with other services of ISPs, this also affects the competition between ISPs in multiple markets.

A possible additional effect is that it might negatively impact the matching of supply and demand in the market. Consumers can no longer receive the content they want to see from all ISPs. This is particularly a problem for customers of ISPs who also need content that is only available from a competitor of their current provider. A consumer is unlikely to take out overlapping plans with multiple ISPs to access the content he wants to see. This may lead to a loss of consumer welfare.

3.2.3 Responses to the consultation

The market participants involved in the consultation responded to the market outcomes ACM identified as possible results of exclusive content. They stated particularly how likely they considered the described market outcomes. Market participants did not put forward any other market outcomes for investigation by ACM. Several market participants stated that the scenario in which exclusive content leads to exclusion should be further investigated by ACM. Most market participants also agree that small ISPs are in a worse position than large ISPs in negotiations with content providers.

[18] https://www.telecompaper.com/nieuws/kpn-breidt-pluspakket-uit-voor-wegvallen-hbo--1172663..
[19] See Delta website at https://www.delta.nl/over-delta/nieuws/consument-over-delta/hbo-stopt-bij-delta.
[20] See Sparql website at http://sparql.nl/nieuwe-abonnementen-voor-2017.html.

According to buyers such as Tele2, CAIW and the providers within NLConnect, the content providers' offering is designed to meet the needs of the large customers, so they are often presented with a 'take it or leave it' offer. Moreover, large providers can seek volume discounts, but small providers cannot. In its response, RTL stated that it has an interest in its channels being broadcast as widely as possible in the market and that small ISPs were also important in this regard.

Pro-competitive

Most market participants stated in their response that they did not agree with the market outcome outlined by ACM in which exclusive content leads to more competition. They believe that, due to their scale and financial resources, only KPN and VodafoneZiggo are attractive to content providers as market participants with which to conclude exclusive agreements. Most other market participants believe these two providers will also be better able to compensate for the lack of certain content, for example by means of price reductions or additional content. According to KPN, it is not good for competition in the market if a vertically integrated provider holds exclusive rights to premium content. VodafoneZiggo believes, however, that exclusive content currently has a pro-competitive effect on the market and that this will also be the most likely market outcome in the future. In its response, RTL voices strong doubts about the notion that the amount of content available to consumers will increase as a result of ISPs competing on content. According to RTL, exclusivity will lead in particular to an impoverishment of the content offering, because it will no longer be possible to receive content for consumers through all ISPs.

Exclusion

In their response to the consultation, CAIW, Tele2 and NLConnect state that the small providers in particular will ultimately be forced to leave the market, because they are unable to compete with KPN and VodafoneZiggo with regard to the offering of exclusive content. T-Mobile concurs with this to a certain extent in its response. Furthermore, T-Mobile states that the risk of exclusion is wider than an insufficient ability to offer content, and that this, combined with the effects of fixed-mobile bundling, will lead to further marginalization of small providers. KPN states in its response that this is a realistic market outcome not only for small providers, but that it applies to all competitors of an ISP that own exclusive, must-have content. According to KPN, such an ISP will have an incentive to exclude competitors in order to attract new tripleplay and quadplay customers and retain existing customers. KPN therefore cannot agree with ACM's finding that it is currently unlikely that, in the present market situation, exclusive content will lead to exclusion and hence to the departure of providers from the market. KPN also believes that ACM could have looked more at the incentives available to ISPs to limit competition from other providers.

VodafoneZiggo stated in its response to the consultation that it did not think it likely that exclusive content would lead to exclusion. This is particularly due to the fact that, in the Dutch television market, there is no provider with a dominant position. According to VodafoneZiggo, there is currently a competitive market in which providers are able to react strongly to each other's updated propositions. The purchasing advantages attributed to it on the grounds that it forms part of an international group should also be attributed to providers such as T-Mobile and Tele2. VodafoneZiggo also believes that the events list is an effective means of ensuring that must-have content is not available exclusively from only one ISP.

ACM believes that, although T-Mobile and Tele2 do indeed form part of international groups, they do not have the same clout with content in the Dutch market as VodafoneZiggo. ACM gives detailed consideration to the position of Liberty Global in this report, because this telecom provider actually owns a substantial amount of content. Although VodafoneZiggo states firmly in its response that there are no problems, ACM believes a competition problem could arise with regard to content as a provider acquires more content or the conditions under which content is resold deteriorate. ACM believes this will not result in KPN being squeezed out of the market by VodafoneZiggo, as KPN appears to suggest.

Higher prices

Most providers state in their response to the consultation that exclusive content will ultimately lead to price increases, as described by ACM in the third scenario. According to T-Mobile an ISP that owns exclusive content rights will ultimately be able to increase prices due to reduced competition in the market. Providers such as Tele2, CAIW and NLConnect have similar responses. According to NLConnect, consumers will have to take out overlapping contracts if content is not available from all providers. CAIW, however, like NLConnect, believes that consumers will not take out overlapping contracts. Due to the growing importance of content, the prices for purchasing content will rise and will ultimately be passed on to the consumer. This will be at the expense of consumer welfare. KPN also believes that the costs of content will be passed on to the consumer through a rise in bundle prices. An ISP that owns exclusive content rights will secure a strong position if other market participants are unable to match its offer, and prices may therefore ultimately rise. VodafoneZiggo states in its response that exclusive content will not lead to price increases, because the market situation is highly competitive. As a result ISPs do not have scope to increase prices.

ACM cannot agree with VodafoneZiggo's argument that the consumer will not ultimately foot the bill for the rising costs of content. ISPs will want to recoup these costs. Particularly if the offer of exclusive content is no guarantee of attracting new customers, as VodafoneZiggo states, it is likely that price rises will be necessary in order to recoup the costs. VodafoneZiggo, incidentally, is increasing its prices for fixed services from 1 July 2017, blaming partly the higher costs of series, films and sport on TV.[21]

[21] See Ziggo website, https://www.ziggo.nl/tarieven/prijswijzigingen/.

Future and solutions

All parties agree in their response to the consultation that if, in the future, ACM wishes to determine which market outcome will result from exclusive content, it will have to keep a close eye on the market. ACM must be alert to possible exclusion effects and respond actively to them. To this end, KPN believes it will be necessary to determine whether exclusive content can be classified as essential from the consumer's perspective. Such an investigation would have to be repeated every so often in order to be able to intervene in time if there were found to be anticompetitive effects. According to T-Mobile, ACM will also have to consider, for example, the effect of content on consumers' switching behavior. Tele2 states in its response that ACM should investigate whether it is possible to encourage content suppliers to offer services directly to consumers. According to Tele2, it would also help if the events list were regularly updated. ACM could also propose additions to the Ministry of Education, Culture and Science.

NLConnect believes that any harmful market outcomes could be prevented or solved by including a must-offer provision in the Dutch Media Act, so that must-have content is offered in a non-discriminatory way. NLConnect requests ACM to draw up an assessment framework for exclusive content, in which the HBO content can serve as a case study. Tele2 and KPN also call on ACM to develop a concrete framework for must-have content. Like NLConnect, KPN also argues that providers of premium content must allow other interested distributors to access that content.

Quantis Electronics, a manufacturer of consumer electronics (including decoders, CI+ modules and audio equipment), states in its response that transparency in the tariff structure and unbundling are necessary in order to achieve accelerated and lasting competition in the Dutch market. Quantis Electronics believes consumers should be able to choose from individual services and should be able to compose their own bundle, even if this would mean purchasing services from multiple ISPs. Among other things, this requires a free market for hardware and smartcards and transparency with regard to the costs of bundled services. This also applies to the way in which the discounts are structured for all-in-one bundles. According to Quantis Electronics, content should also be available to consumers separately through OTT services.

3.2.4 Conclusion

ACM considers that the reasons put forward by providers as to why exclusive content would not lead to a pro-competitive market outcome constitute risks particularly in the longer term. In the short term, ACM believes it is more likely that competition based on content will have a pro-competitive effect on the market. This is what ACM is currently also seeing in the market, with ISPs endeavoring to distinguish themselves from each other with their content propositions. The responses from market participants do not lead to any different conclusion.

In its analysis, ACM has examined the current market situation and, on that basis, has come to the conclusion that having regard to the content that is currently being offered exclusively, this is unlikely to lead to the exclusion of providers. Possible exclusionary effects of content will have to be analyzed on a case-by-case basis, and it cannot necessarily be assumed that exclusive content will lead to exclusion. At present, ACM notes that the content that is currently offered exclusively has not hitherto led to major shifts in the market. ACM also has no indications at present that this will be the case in the near future. ACM therefore believes a must-offer provision for premium content would currently be disproportionate. ACM does, however, understand the concerns expressed by a number of market participants.

It will therefore continue to monitor this market. It wishes to avoid a situation in which the identified risks ultimately turn into problems. Furthermore, ACM believes it is important that consumers have sufficient choice with regard to content, with TV packages also being available to them without added premium content. This will mean that cheaper bundles also remain available.

4 Conclusion

ACM notes that the importance of fixed-mobile bundles is increasing. The number of consumers with such bundles is growing, and ACM expects this trend to continue. In addition, ACM sees increasing integration between ISPs and content providers.

Although bundling can be advantageous for consumers, ACM also sees a number of risks to competition in the longer term. Partly as a result of bundling, consumers will switch less quickly, making it difficult for smaller providers to grow. Ultimately it may even lead to departures from the market, resulting in a decrease in competition. ACM wishes to prevent this and will therefore monitor these developments closely. It is important that smaller providers are also able to offer consumers attractive fixed-mobile bundles.

With regard to vertical relationships of ISPs with content providers, ACM currently considers that these can make a positive contribution to the competition. However, if ISPs acquire exclusive content, there is a risk that competition will decrease in the longer term. This could be the case if some ISPs are no longer able to offer their customers must-have content. If this means these providers ultimately have to leave the market, it will probably lead to higher prices and less innovation. ACM also sees a risk that consumers will in future have to take out plans with multiple ISPs to have access to all the content they wish to see.

Due to the identified risks, ACM must continue to monitor the market and examine how the availability of bundles (or individual bundle components) develops. The same applies to the availability of content. The ongoing market analysis will devote explicit attention to the role played by fixed-mobile bundles and the competition potential for smaller providers. The role of content will also be included in that analysis. ACM also believes it is important that consumers have options and are not forced to purchase more expensive ‘enhanced’ packages. It is therefore desirable that TV packages without premium content and unbundled services are also available to them.

If ACM receives concrete indications that particular conduct among market participants is a serious restriction of competition, it will take action.