

Project Canvas

A REPORT ON THE INCENTIVES TO SYNDICATE

Project Canvas is a joint venture (JV) between the BBC, ITV, Channel 4, Five and BT to develop and promote a set of common technical standards that will allow consumers to access video-on-demand (VoD) content through their television using a broadband connection.

As part of BBC Trust's approval process, it has decided to undertake a market impact assessment (MIA) to examine the effect that Project Canvas may have on other market participants. With this in mind, the BBC Trust has asked us to assess whether the parties' incentives to syndicate their content could change as a result of their involvement in Project Canvas.

Our assessment shows that the principles underlying the set up of Canvas should ensure that it would not change the JV partners' incentives to syndicate their content. This conclusion rests on the grounds that the parties will not be able to reach a tacit agreement to restrict syndication via their involvement in Canvas (e.g. through exchanging commercially sensitive information) and that Canvas will be open access and delivered on a cost-recovery basis. We recommend that the BBC Trust considers imposing relevant conditions on the BBC's participation to ensure that these principles are adhered to.

Our assessment relies on information provided by the BBC Trust about how the JV would be expected to operate and a series of interviews with each of the JV partners that are also content owners (BBC¹, ITV, Channel 4 and Five) and also BBC Worldwide.

The remainder of this document is split into three sections:

- Section 1 provides an overview of the features of Canvas relevant to our assessment;
- Section 2 outlines the potential concerns that could arise in relation to the parties' syndication incentives and assesses whether they are likely to materialise given the principles that underlie the set up of Canvas;
- Section 3 provides an overview of the current syndication strategies of the JV partners and whether they expect them to change in the presence of Canvas.

¹ The BBC has a commitment to syndicate its content in accordance with the BBC Syndication Policy. In 2010 the Trust will conduct a review of its policy on syndication, the Executive's guidelines on syndication and the BBC's on-demand activity more generally with a view to ensuring continuing effective implementation of the BBC's duty to make its content widely available.

Section 1: A brief overview of Canvas

Canvas is a technology that will allow VoD to be delivered to consumers through their television, rather than through devices such as PCs or portable devices. It is anticipated that, at least initially, it will be supplied through a set-top box that consumers can purchase.

Canvas will allow consumers to access content through a user interface, similar to the way they currently select linear television channels through an electronic program guide on Sky or Virgin Media. Canvas itself is not an editorial proposition that would retail content and present it for sale to consumers. Content providers will not syndicate content to Canvas, but will offer content directly to consumers through it.

Canvas will be a free-to-air proposition initially available on DTT. This will mean that once consumers purchase a set-top-box, they will face no ongoing costs, other than costs that they may incur in purchasing VoD content.

We understand that content providers and retailers will face a “fair and equal” access regime, which means that access to Canvas will be delivered on a cost-recovery basis and access to the electronic program guide will be non-discriminatory and regulated. We also understand that JV partners will not receive profits from any other elements of the Canvas proposition, including the licensing of Canvas technology, services provided by the Canvas JV or from the sale of Canvas set-top boxes.

Section 2: Potential syndication concerns and whether they are likely to materialise

There are two potential concerns that could arise in relation to the parties’ syndication incentives.

Restricting syndication to soften retail competition

The first potential concern is that the parties could use the Canvas JV as a means to weaken retail competition and engineer unduly high retail prices for their content (for example, by coordinating their retail strategies). If this were the case, the parties may be less likely to syndicate to VoD retailers because this would intensify retail competition and reduce the parties’ retail profits.

However, Canvas is not a VoD retailer and nor is it a direct agreement between the parties to jointly determine retail and/or wholesale prices for their VoD content. This means that the JV partners will continue to compete with each other on Canvas in the same way as they currently compete with each other online either with their own websites or via VoD retailers such as iTunes. The

implication is that there is not a direct mechanism for the parties to engineer unduly high retail prices for their content via their involvement in the JV.

The only remaining potential issue is whether the parties' involvement in the Canvas JV will enable them to reach a tacit agreement to coordinate their retail VoD strategies and restrict syndication.² We would recommend that the BBC Trust considers imposing relevant conditions on the BBC's participation in relation to information exchange and governance structure so as to minimise the potential risk of this arising.

Restricting syndication to attract customers

The second potential concern is that the parties would unilaterally restrict syndication in order to gain customers from other VoD retailers or platform operators. The parties would have an incentive to do this if any additional retail profits (e.g. through higher revenue for advertising or paid-for content) earned as a consequence would offset the lost wholesale profits.

There are, however, two reasons why the parties would not be expected to earn greater retail profits as a consequence of restricting syndication and diverting consumers towards the Canvas platform.

- First, as noted above, access to Canvas will be "fair and equal" and access to the electronic program guide will be "non-discriminatory".

This means that the JV partners should not be able to prevent or limit alternative content providers or VoD retailers from fairly competing for customers on Canvas, or direct customers away from other content providers to their own content.³

The implication is that if the JV partners were to restrict syndication to other platform operators or VoD retailers and succeed in diverting additional consumers towards the Canvas platform, there would be no obvious mechanism to ensure that those customers would increase their consumption of the parties' content at the expense of other content providers. It follows that there is no obvious reason to believe that restricting syndication would generate additional retail profits via the sale of content or advertising on Canvas to offset the lost wholesale profits

² We would not expect that the operation of the Canvas JV would require the parties to exchange commercially sensitive information in relation to VoD retail, since Canvas is not a VoD retailer nor would it engage in the services associated with retailing (e.g. billing, distributing associated revenue etc). Nevertheless, it would be important to ensure that no other information concerning the parties' wholesale or retail VoD strategies were shared (for example, marketing or investment strategies).

³ We note that such a strategy would also reduce the attractiveness of the Canvas platform to consumers.

- Second, as noted above, the Canvas JV will be operated on a cost-recovery basis.

This means that the JV partners will not earn profits from access charges or any other elements of the Canvas proposition, including the licensing of Canvas technology, services provided by the Canvas JV or from the sale of Canvas set-top boxes.

Again, the implication is that if the JV partners were to restrict syndication to other platform operators or VoD retailers, they would not be expected to generate additional profits via Canvas to offset the lost wholesale profits.⁴

Section 3: Current syndication strategies

The analysis set out above suggests that Canvas should not lead to the parties restricting syndication. The analysis is consistent with the views offered by the parties when we interviewed them.

None of the JV parties believed that Canvas would change their syndication strategy. They viewed Canvas as another platform offering them and other firms a new opportunity to present VoD content to consumers. They believed that Canvas would have a positive impact on their revenues from VoD content, but that it would primarily bring new consumers to VoD (who may see Canvas as an upgrade to Freeview), rather than take users away from other services. This is because they believe that many consumers have a preference to watch VoD through a television, rather than a computer and, as a result, many consumers that would value watching VoD currently do not. In addition, they all believed it would take some time for Canvas to reach significant volumes, while other platforms already had large audiences.

The parties said that they would continue to use their standard criteria to assess a deal, which include:

⁴ The Canvas JV may wish to attract additional content providers in order to earn additional access revenues if there was a risk that it would not cover its costs otherwise. A residual concern is that the parties may attempt to do this by restricting syndication to other platforms to weaken their propositions and encourage viewers to switch to Canvas. This would strategy would yield additional access revenues if actual or potential content providers then decided to deliver content via Canvas instead of other platforms.

For this concern to be realised, the following set of circumstances would need to arise: first, the Canvas JV would need to be at risk of not covering its costs; second, the potential increase in access revenues would need to offset the reduction in syndication revenues (and for there to be no more profitable strategy to cover its costs – e.g. raising access prices); and third, it would need to be more profitable for content providers to syndicate only to Canvas and not to the weakened platform (e.g. because the costs associated with coding or recoding content outweigh the revenues associated with syndication).

- whether the deal would maximise revenue generation – including the ability to sell the advertising around the content and the effect that it might have on other deals;
- the strategic fit between the proposed counter-partner and the JV party – whether the JV party would retain editorial control over the proposition and the counter-party's branding; and
- the resources available at the JV party to develop the necessary technology.

The application of these criteria has historically led to the JV partners syndicating their VoD widely. This was either due to commercial necessity and their obligations to rights holders or it was part of their public service remit to make sure that their content was widely accessible to viewers. Most of the parties either already had deals or were in negotiations with between 10 and 15 partners – who ranged from TV platforms (such as Virgin) to online portals (such as YouTube) and console operators (such as Nintendo Wii). None of the parties had ever terminated a syndication deal or syndicated their content exclusively.

None of the parties thought that they would gain any advantage by restricting syndication. This was because they believed they would lose profits by doing so. In addition, some of the parties stated that it would go against their public service remit to restrict syndication. All the parties stated that they would continue to look for profitable VoD syndication opportunities outside Canvas including deals with retailers on platforms such as connected televisions, consoles and portable devices.

Concluding remarks

We conclude that Canvas should not affect the syndication decisions of each of the JV partners provided that it will be open access, delivered on a cost-recovery basis as envisaged and that there is no risk of tacit collusion between the parties in relation to their retail and wholesale VOD strategies. We recommend that the BBC Trust considers imposing relevant conditions on the BBC's participation to ensure that these principles are adhered to.