

Submission to the Competition Commission Consultation on its
Provisional Findings for its Inquiry into
Movies on Pay TV

The British Film Institute

September 2011

Executive Summary

The British Film Institute is the Government's lead body for film. Our ambition is to create a flourishing film environment in which innovation, opportunity and creativity can thrive by, among other things, connecting audiences to the widest choice of British and world cinema.

We are grateful to the Competition Commission for the opportunity to make a short submission in response to the Provisional Findings regarding its investigation into Movies on Pay-TV.

In this short submission, we comment on the impact that the Provisional Findings have on the choice and range of films available to British consumers. The Findings clearly signal that choice and range are reduced by the distortion of the market. We also highlight our concerns about the Provisional Findings in relation to "non-major studios", where the Commission appears to argue that competition is "broadly effective" despite evidence to the contrary in respect of independently-produced and distributed films.

To support this case, we have attached a recent article from the trade paper *Variety* concerning *The King's Speech*, in which the UK Film Council (some of whose functions the BFI has now absorbed) invested money allocated to film from the proceeds of the Lottery. It appears to us that the consequences of this distortion of competition are an adverse effect on the choice and range of films available to audiences, in particular because of the inability of non-major studios to maximise their returns.

2. Comments on Provisional Findings

The BFI only became the lead body for film in April 2011. We have not had the opportunity to respond to earlier consultations by the Commission on this subject. We are aware however that the UK Film Council – some of whose functions were absorbed by the BFI – made two submissions to Ofcom during the period that the regulator was consulting on Pay-TV, before the referral to the Competition Commission.¹ In those submissions, the UK Film Council raised significant concerns regarding the operation of the pay-TV market.

It observed that:

"the current lack of competitive offerings in the premium content market has had an adverse effect on consumers. The latter has appeared to inhibit new entrants, limit choice, discourage innovation and generally dampen competition in all aspects of pay TV to the detriment of many, including the independent film industry (including both independent production and distribution) in the UK."²

¹

http://www.ukfilmcouncil.org.uk/media/pdf/s/c/UK_Film_Council_response_to_Pay_TVfinal29_Feb_2008.pdf
http://www.ukfilmcouncil.org.uk/media/pdf/i/s/UKFCResponse_to_2nd_Ofcom_payTV_condoc.pdf

² http://www.ukfilmcouncil.org.uk/media/pdf/i/s/UKFCResponse_to_2nd_Ofcom_payTV_condoc.pdf. P.2

While the BFI is not in a position to comment on detail on the Competition Commission's detailed Provisional Findings, we are aware that the independent film sector in the UK has consistently raised concerns that the operation of the pay-TV market in the UK is preventing access to a wider range of films. We note the submissions made to the investigation on this topic and the Commission's own analysis.³

We note that the Commission has "provisionally found that Sky's control over pay-TV movie rights in the UK is restricting competition between pay-TV providers, leading to higher prices and reduced choice and innovation for subscribers."⁴

We note in particular that in its Provisional Findings the Commission says that: "In addition, we noted that we would expect the limited innovation which had occurred as a result of the AEC [Adverse Effect on Competition] (see paragraph 37) to have had effects in restricting both the range and quality of movie products available to consumers, and we noted that this detriment may be at least as important as the static detriment on prices which we had quantified."

We believe that the evidence which the UK Film Council submitted to Ofcom helps to explain the restrictions on the range and quality of movie products available to consumers. This restriction on range and quality, created by the AEC represents a significant barrier to the BFI fulfilling its ambition to connect audiences with the widest range of British and world cinema. We welcome therefore the consultation on Possible Remedies which the Commission has consulted on earlier this month, although we are not in a position to comment in detail on those possible remedies.

In particular we note that the Competition Commission says in its Provisional Findings that:

"We also investigated whether the non-major studios suffered lower prices or worse terms for their FSPTW rights compared with the major studios but the evidence was inconclusive. However, we noted that, even if the non-major studios had suffered compared with the major studios, this was unlikely to have affected adversely competition between all studios."⁵

³ http://www.competition-commission.org.uk/inquiries/ref2010/movies_on_pay_tv/pdf/independent_distributor_response.pdf
http://www.competition-commission.org.uk/inquiries/ref2010/movies_on_pay_tv/pdf/wp_19_implications_of_any_monopsony_power_sky_may_hold.pdf

⁴ http://www.competition-commission.org.uk/press_rel/2011/august/pdf/45_11_press_release.pdf

The latter conclusion appears to be based on the assertion that “ Given that studios gain revenues from many windows, not just the FSPTW, and from many geographic markets, not just the UK, it would seem unlikely that any detriment suffered by some non-major studios in the FSPTW in the UK would affect competition between studios overall.”⁶

This significantly under-estimates the value of access to the pay-TV window as a means of offsetting the risks of distribution to cinemas (which is a loss-leader for most films) . It also ignores the fact that many independent distributors, especially the smaller companies, are only operating in the UK. Therefore, any detriment suffered by non-major studios in the FSPTW can be material to competition and choice for consumers. It should also be noted that since, according to the BFI’s Research and Statistics Unit, 80% of the films watched in the UK each year are watched on television, the distortion of competition in the television market has a significantly detrimental impact.⁷ However, as much of the analysis of this issue has had to be redacted by the Commission, it is not possible for the BFI to comment in detail.

The BFI invests Lottery money in film, a function which it absorbed from the UK Film Council. The UK Film Council was an investor in *The King’s Speech*, by far and away the most successful independently produced and distributed British film of recent times. We attach as an annexe to this submission a recent article from the trade paper *Variety* which describes the process by which the independent distributor of the film, Momentum, sold the pay-TV rights to *The King’s Speech* to Sky. The article notes that “the result was worth far less to Momentum, and to the public and private investors in “The King’s Speech,” than any studio would have earned from the same film.”⁸ The analysis in this article appears to us contradict the Commission’s assertion that it has “found no reason to believe that competition between studios for the sale of their FSPTW rights is anything other than broadly effective.”⁹

The inability of the public and private investors to maximise their returns from the film has a direct effect on their ability to invest money in a broad range of films for British audiences in

⁵ http://www.competition-commission.org.uk/inquiries/ref2010/movies_on_pay_tv/pdf/provisional_findings_report.pdf, paragraph 33, p.15.

⁶ http://www.competition-commission.org.uk/inquiries/ref2010/movies_on_pay_tv/pdf/provisional_findings_report.pdf, Section 10, paragraph 66.

⁷ <http://statisticalyearbook11.ry.com/?id=83006>

⁸ <http://www.variety.com/article/VR1118042483?refCatId=19>

⁹ http://www.competition-commission.org.uk/inquiries/ref2010/movies_on_pay_tv/pdf/provisional_findings_report.pdf, paragraph 10.68

the future. This has an impact not just in the pay-TV window but in other windows such as cinema and DVD. The net effect is to reduce choice, range and innovation for consumers.

Annex One – Article from Trade Paper *Variety*

Posted: Sat., Sep. 10, 2011, 4:00am PT

'King's' bling eludes indies

BSkyB dominance muffles earnings for non-studio pix

By Adam Dawtrey

While the copious revenue generated by "The King's Speech" has often been used as an example to illustrate the ins and outs of the biz, it throws a particularly bright light on how BSkyB's dominance of the U.K. pay-TV market has affected Britain's indie film business.

Local distributors argue that the satcaster's monopoly has restricted their ability to compete with the U.S. majors, and limited the upside from British indie hits such as Tom Hooper's multi-Oscar winner.

BSkyB has expensive output deals with all the Hollywood studios, but only rarely buys films from local indies, and then at dramatically lower prices.

"The studios get the highest prices anywhere in the world outside the U.S., and the independents get the lowest," says one exec who has worked in senior positions for both studios and indies. "It's probably the single most debilitating factor for indies in the U.K. -- worse than low cinema rentals and high P&A costs."

The financial gulf is so great that it's more lucrative for an indie to enter a distribution partnership with a studio in order to access vacant slots in its Sky deal than to attempt to sell pay-TV rights direct to the satcaster.

That's why last November, two months before its opening, Momentum Pictures quietly flipped "The King's Speech" to Universal.

Universal offered a Sky slot worth at least \$2 million, with the studio creaming off a 50% fee and Momentum keeping the rest.

At the time, the indie was hoping "The King's Speech" would reach \$15 million at the B.O. Momentum reckoned that might net \$250,000 from a direct sale to Sky. The satcaster

typically pays 4%-5% of gross for an indie action movie, but much less for a period piece.

There was no guarantee, however, that the satcaster would actually buy the film, particularly if it fell short of predictions. Sky never brought previous Oscar winner "The Hurt Locker" from Optimum, for example.

On the other hand, if "King's Speech" turned out to be smash hit, Momentum might not only squeeze top dollar from Sky, but could also use its leverage to sell its whole slate of films, or even secure an output deal.

But Momentum topper Xavier Marchand didn't have the luxury of waiting to see how "King's Speech" performed before making his decision: The fine print varies, but the U.S. majors can only put films through their output deals if they acquire them prior to theatrical release.

In some cases, such as Momentum's separate ongoing relationship with Paramount, the studio must act as co-distributor, handling the theatrical sales for a fee and sharing the credit. But Universal's Sky deal works differently, so Momentum was not required to split the theatrical income or put the studio's name on the film.

"The King's Speech" had already recouped 90% of its equity from foreign sales, so the investors, including the UK Film Council, were willing for Momentum to refuse U's offer and gamble on getting a better deal from Sky after the theatrical release.

But Momentum still had its own advance and its hefty P&A commitment on the line, and the U offer was simply too rich to turn down.

As it turned out, "The King's Speech" grossed \$74 million. Fortunately for Momentum and other "King's Speech" investors, Universal's pay deal is linked to box office by a complex internal formula. The exact value allocated to "The King's Speech" has yet to be fixed, but insiders reckon Momentum's half-share is still likely to end up greater than the indie would have earned by selling direct to Sky.

But pre-selling to U meant that Momentum was unable to use its monster hit to secure better pay TV deals for the rest of its slate, or to take the option of collapsing the pay window and selling direct to free TV for a premium.

In the end, Marchand arguably got the best deal available for "The King's Speech." But he was forced into contortions to do so, and the result was worth far less to Momentum, and to the public and private investors in "The King's Speech," than any studio would have earned from the same film.

No wonder Momentum is now one of several indies negotiating long-term output deals in the pay-TV window with Web streaming services Netflix or Lovefilm. For the first time, BSkyB faces the prospect of real competition for pay-TV rights, with the Web services offering what indies describe as very attractive sums.

<http://www.variety.com/article/VR1118042483?refCatId=19>