

Completed acquisition by Sony Music Entertainment of all of the issued shares of the entities comprising the AWAL and the Kobalt Neighbouring Rights businesses from Kobalt Music Group Limited

Issues Statement

11 October 2021

The reference

1. On 16 September 2021, the Competition and Markets Authority (**CMA**), in exercise of its duty under section 22(1) of the Enterprise Act 2002 (**the Act**), referred the completed acquisition by Sony Music Entertainment (**SME**), a subsidiary of Sony Group Corporation (**Sony**), of all of the issued shares of the entities comprising the AWAL business (**AWAL**) and the Kobalt Neighbouring Rights business (**KNR**) from Kobalt Music Group Limited (**Kobalt**) for further investigation and report by a group of CMA panel members. The completed acquisition by SME of AWAL and KNR is referred to in this issues statement as **the Merger**.
2. In exercise of its duty under section 35(1) of the Act, the CMA must decide:
 - (a) whether a relevant merger situation has been created; and
 - (b) if so, whether the creation of that situation has resulted, or may be expected to result, in a substantial lessening of competition (**SLC**) within any market or markets in the United Kingdom for goods or services.
3. We will apply a 'balance of probabilities' threshold to our analysis. That is, we will decide whether it is more likely than not that the Merger has resulted, or may be expected to result, in an SLC.¹

¹ See Merger Assessment Guidelines (CMA129) (March 2021), paragraph 2.36.

Purpose of this issues statement

4. In this issues statement, we set out the main issues we are likely to consider in reaching our decision on the SLC question (paragraph 2 above), having had regard to the evidence available to us to date, including the evidence obtained in the CMA's phase 1 investigation. This does not preclude the consideration of any other issues which may be identified during the course of our investigation.
5. We are publishing this statement in order to assist parties submitting evidence to our investigation. This statement sets out the issues we currently envisage being relevant to our investigation and we invite parties to notify us if there are any additional relevant issues which they believe we should also consider. The CMA's phase 1 decision² contains much of the detailed background to this issues statement.
6. We intend to use evidence obtained during the phase 1 investigation. However, we will also be gathering and considering further evidence on these and any other issues which may be identified during the course of the investigation.

Impact of Coronavirus (COVID-19) on the inquiry

7. We are publishing this issues statement during the Coronavirus (COVID-19) pandemic which is having significant impacts on consumers and business across the world. The CMA has published a statement on its website on how it has adjusted its working arrangements in response and guidance on key aspects of its practice during the pandemic.
8. Our approach to evidence-gathering will take into account the difficulties that the pandemic may be causing for market participants in this sector. If appropriate, we will also take into account the impact of the pandemic in our assessment of the competitive effects of the Merger, although we are required to look beyond the short-term and consider what lasting structural impacts the Merger might have on the markets at issue.

Background

9. On 18 May 2021, Sony, through its fully owned subsidiary SME, acquired AWAL and KNR for approximately \$430 million (approximately £314 million) in

² See Decision on [CMA webpage](#).

cash. Sony (including SME), AWAL and KNR are collectively referred to as **the Parties**.

The Parties

10. Sony is active globally in various businesses including recorded music and music publishing, motion picture production and distribution, and game and network services for its game console, PlayStation. SME is the recorded music division of Sony. SME is a global distributor of recorded music, an operator of multiple record labels and a supplier of artist and repertoire (**A&R**) services. SME, through its subsidiary The Orchard, EU Limited (**The Orchard**), also supplies artist and label (**A&L**) and distribution services both to artists and to labels. Sony provides neighbouring rights collection through its publishing arm Sony Music Publishing.
11. AWAL and KNR are music businesses which operate globally. AWAL and KNR were formerly owned by Kobalt alongside Kobalt's music publishing business. Kobalt has retained the music publishing business following the Merger.
12. AWAL is a 'multi-tiered' music platform providing A&L and distribution services to artists and labels, as well as offering a 'gated'³ DIY platform through which artists can submit their music to AWAL.
13. KNR collects neighbouring rights royalties arising from the public use of music recordings on behalf of artists.

The industry

14. As set out in the Phase 1 Decision,⁴ the Parties overlap in the UK and globally in the wholesale distribution of recorded music and the supply of neighbouring rights administration services. The Parties overlap in the wholesale physical distribution of recorded music, however, digital mediums, and in particular streaming has become the most frequently used format for customers to receive music. We therefore propose to concentrate on the wholesale digital distribution of recorded music,⁵ particularly streaming.
15. The wholesale digital distribution of recorded music is currently characterised by the presence of three large record companies (Sony, Universal Music Group (**Universal**) and Warner Music Group (**Warner**)), the so-called

³ AWAL's DIY platform is 'gated' meaning that artists provided with distribution services by AWAL must have made a successful merits-based application, assessed by AWAL's expert teams.

⁴ See Decision on [CMA webpage](#) .

⁵ This is also referred to in this issues statement as digital music distribution.

‘majors’, and a number of significantly smaller-scale players, including independent record labels, A&L service providers and DIY platforms. Each type of player is described below.

16. The sector is characterised both by (i) competition between service providers to acquire and retain artist clients, label clients and music catalogues; and (ii) providers negotiating with Digital Service Providers (**DSPs**)⁶ to achieve favourable deal terms for the distribution of digital recorded music. These two aspects of competition are likely to be linked as acquiring a portfolio of successful artists, and/or label clients and/or music catalogues may grant providers greater negotiating power with DSPs. Whether an artist, label, or catalogue is successful in this context may depend upon several factors such as the extent or scale of their audience.
17. The major record labels supply A&R services. These include promotion, marketing, creative development, radio campaigns and tour support for artists, all of which are aimed at increasing distribution. The major record labels scout, sign and support artists on a worldwide basis, some of whom are, or are assisted in becoming, global ‘superstars’.
18. The independent record labels are a large number of smaller players that have historically accounted for a smaller share of the wholesale digital distribution of recorded music. Independent record labels scout, sign and provide A&R services to artists, typically using a business model similar to that of the major record labels. The range of A&R services offered by independent record labels may be more limited due to the resource constraints that these labels operate under. Many independent record labels rely on third-party suppliers for distribution.
19. A&L service providers distribute music on behalf of artists and labels and provide supporting A&L services. Accordingly, A&L services are sometimes referred to as either artist services/services to artists or label services/services to labels to denote the client type being served.
20. A&L services are broadly similar in nature to A&R services, albeit with some significant differences:
 - (a) A&L services are often narrower in scope than A&R services and provided on a smaller scale. For example, like the major record labels, A&L service providers also supply promotion and marketing services but

⁶ A DSP is a company that provides digital music services, such as downloading and streaming. Examples of DSPs include Amazon, Apple, Spotify and YouTube/Google.

are unlikely to be able to supply tour support and capital advances to the same extent.

- (b) Under agreements with A&L service providers, artists typically independently create music and the artist (and/or their label) retain full ownership of the copyright of the recorded music.
 - (c) Agreements with A&L service providers tend to be relatively short-term compared to traditional agreements with major record labels offering A&R services, enabling artists to switch providers more easily.
 - (d) Under agreements with A&L service providers, artists retain a higher portion of earnings from distribution, with the A&L provider receiving a smaller portion of earnings than an A&R provider typically would. The CMA also notes a key difference between how A&L service providers and suppliers using traditional A&R deals fund the costs incurred in supporting artists. In the case of A&L service providers, typically all costs are directly recoupable from the artist's portion of earnings. In contrast, under traditional A&R deals, typically the record label is ultimately responsible for and fully incurs the majority of costs; only a more limited range of costs is recoupable from the artist's portion of earnings.
21. A&L service providers usually serve 'mid-tier' artists,⁷ either as direct customers or through an independent record label. There are, however, notable exceptions to this position.
 22. Each of the major record labels has acquired or developed one or more A&L businesses: Sony (with its The Orchard business), Warner (with its ADA business), and Universal (with its Ingrooves and Virgin businesses).
 23. DIY platforms focus on the digital distribution of recorded music and typically charge artists a fixed fee to upload a set number of songs to the platform. Some DIY platforms also offer limited supporting services such as promotion and marketing on top of distribution.
 24. Neighbouring rights entitle performing artists, and those who own copyright in the related sound recording, to compensation for the public use of the recording (eg a radio broadcast). Artists and copyright owners can collect royalties from Collective Management Organisations (**CMOs**) directly or can

⁷ The term 'artist funnel' is sometimes used in the industry to refer to the full spectrum of artists at different stages of their career. The artist funnel can be segmented into three main tiers, namely (i) lower-tier artists (ie artists at the beginning of their career); (ii) mid-tier artists (ie artists who have already reached a level of commercial success); and (iii) top-tier artists (ie established artists who have reached considerable success).

use the services of suppliers like KNR, which collect neighbouring rights royalties from CMOs on their behalf.

Our inquiry

25. Below we set out some specific areas of our proposed assessment in order to help parties who wish to make representations to us.

Assessment of the competitive effects of the Merger

Jurisdiction

26. The CMA's phase 1 decision found that it is or may be the case that the CMA had jurisdiction to review the Merger on the basis that:
- (a) Sony, AWAL and KNR are enterprises which have ceased to be distinct as a result of the Merger; and
 - (b) the share of supply test in section 23 of the Act is met – the Parties overlap in the wholesale distribution of recorded music in the UK. The Parties estimated their total combined share of the wholesale distribution of recorded music (including both physical and digital) in the UK in 2020 to be [20-30]% (with an increment of [0-5]% brought about by the Merger).
27. We shall consider the question of jurisdiction in our inquiry.

Counterfactual

28. We will compare the prospects for competition resulting from the Merger against the competitive situation without the Merger: this is the counterfactual. The counterfactual is not a statutory test but rather an analytical tool used in answering the question of whether a merger gives rise to an SLC.⁸
29. In the phase 1 decision, the CMA found the pre-Merger conditions of competition to be the relevant counterfactual. As set out in the discussion of the theories of harm, we are considering the future development of the sector and the likely future actions of the Parties and other entities that would have occurred absent the Merger as a basis for comparison. There may therefore be an overlap between the assessment of the counterfactual and an assessment of potential or future competition and more detailed consideration

⁸ [Merger Assessment Guidelines \(CMA129\)](#), paragraph 3.1.

of future competitive conditions may be considered in our competitive assessment.

Theories of harm

30. The CMA assesses the potential competitive effects of mergers by reference to ‘theories of harm’. A theory of harm is a hypothesis about how the process of rivalry could be harmed as a result of a merger. Theories of harm provide a framework for assessing the effects of a merger and whether or not it could lead to an SLC relative to the counterfactual.⁹
31. We set out below the theory of harm that we propose to investigate. We may revise our theory of harm as the inquiry progresses and the identification of a theory of harm does not preclude an SLC being identified on another basis following further work, or receipt of additional evidence.
32. The competition concerns identified in the phase 1 decision¹⁰ related to the loss of potential competition which could arise from the future growth of AWAL in A&L services. While AWAL’s market share was relatively small, it had achieved high rates of growth relative to other A&L providers (and the market overall), it had credible plans for substantial further growth, and both Parties’ internal documents referenced the disruptive nature of AWAL’s business model. This disruption may have, in part at least, prompted the majors to adapt their competitive strategies and developing their own A&L businesses. In particular, absent the Merger, the evidence suggested that SME had intended to grow The Orchard business.

Loss of potential competition in digital music distribution in the UK

33. Taking the approach followed in phase 1 as our starting point, we propose to focus our investigation at phase 2 on a horizontal unilateral effects theory of harm around the loss of potential competition in digital music distribution in the UK.
34. Unilateral effects can arise in a merger where one firm merges with a competitor that provides and/or is expected to provide a competitive constraint. Through the Merger, removing one Party as a competitor might allow the merged entity profitably to raise prices, or degrade non-price aspects of its competitive offering (such as quality, range, service and innovation) on its own and without needing to coordinate with its rivals.¹¹

⁹ [Merger Assessment Guidelines \(CMA129\)](#), paragraph 2.11.

¹⁰ See Decision on [CMA webpage](#).

¹¹ [Merger Assessment Guidelines \(CMA129\)](#), paragraph 4.1.

Unilateral effects may arise from the elimination of potential competition where 'potential competition' refers to competitive interactions involving at least one firm that has the potential to enter or expand in competition with other firms. Potential competition is relevant to the assessment of the competitive effects of a merger where, absent the merger, entry or expansion by either or both merger firms may have resulted in new or increased competition between them.¹² As well as increased future competition after the potential entrant would have entered or expanded, a merger could lead to a loss of dynamic competition where existing firms and potential competitors - either entering or expanding - interact in an ongoing dynamic competitive process.¹³ For example, the possibility of future expansion may lead incumbents to improve their own competitive offering to mitigate the risk of losing future profits.

35. The consequences of such a loss of competition could be harm to customers (artists and labels) arising from:
- (a) less choice in the variety of business and contractual models available to artists and labels, eg in respect of ownership of the copyright of their recorded music;
 - (b) higher commission fees/poorer royalty terms or lower advances;
 - (c) lower quality, eg poorer promotional or management services;
 - (d) a narrower range of services being offered or a lower quality of A&L service levels (staffing levels, marketing spend); and/or
 - (e) less innovation in additional services and a slow-down in the evolution of the sector and new contractual models.
36. In respect of DSPs, the consequences of a loss of competition in the supply of wholesale digital distribution of recorded music could include increased fees or reduced quality and innovation in the provision of music to them.
37. In order to investigate this theory of harm, we will first investigate how competition is currently working within this sector and the nature of the existing competitive constraints. The impact of a potential entrant or of potential expansion on competition is likely to be more significant when: there are fewer strong existing competitive constraints on the other merger firm; where the other merger firm would already have market power absent the merger (with greater market power being associated with a greater likelihood

¹² [Merger Assessment Guidelines \(CMA129\)](#), paragraph 5.1.

¹³ [Merger Assessment Guidelines \(CMA129\)](#), paragraphs 5.2 and 5.3.

of an entrant having a bigger impact on competition); and/or where there are few other potential constraints. Where one merger firm has a strong position in the market and there are few significant potential competitors, even small increments in market power may give rise to competition concerns.¹⁴

38. We will consider:
- (a) the recent developments in the sector and areas of growth;
 - (b) the nature and intensity of competition between the majors, independent record labels, A&L providers and DIY gateways;
 - (c) how competition for signing new artists or labels takes place, and around which contractual terms competition occurs;
 - (d) whether there have been new business models and/or shifts in the approaches offered and the extent to which these changes have been driven by competition from A&L providers and AWAL in particular;
 - (e) whether there is segmentation of the relevant market, between for example, artist and label services, and between high-tier, mid-tier and other artists;
 - (f) how competitive dynamics differ between the tiers and whether the mid-tier segment is expanding; and
 - (g) how competition for the distribution of music through DSPs takes place.
39. We will investigate the current and potential (future and dynamic) competition specifically between the Parties. We will consider:
- (a) how AWAL has achieved growth (above general market growth);
 - (b) how The Orchard complements and differs from SME's activities;
 - (c) the current overlap and differences in activities and capabilities between the Parties; and
 - (d) the closeness of competition between the Parties (for example, including the views of customers and competitors, how the Parties monitor each other and the level of attention the Parties pay to different competitors, evidence of customer switching, and whether there is evidence of the

¹⁴ [Merger Assessment Guidelines \(CMA129\)](#), paragraph 5.15.

Parties respond to each other by varying advances, terms, service levels, rights ownerships etc.);

- (e) evidence of dynamic competition, ie is AWAL's competitive presence and its potential for greater future competitive impact already resulting in competitive responses from SME (and other providers), and how this would be expected to develop over time;
- (f) how the Parties would have developed absent the Merger, for example:
 - (i) whether SME would have expanded the activities of The Orchard and broadened its A&L activities for both artists and labels, and whether SME and The Orchard would have changed their competitive approach to compete more closely with A&L providers;
 - (ii) whether AWAL would have expanded in size and in the range of activities it undertakes, and whether it would have changed its competitive approach.¹⁵
- (g) in relation to (f) we will consider for the wholesale distribution of recorded music in the UK and in particular in relation to A&L services:
 - (i) how well-developed are each of the Parties' plans, or the extent to which they were already making efforts to expand; and
 - (ii) whether each Party has the ability and resources to expand.

40. In order to address the theory of harm, we will consider whether AWAL has had or is expected to have particular significance in its past, current and future presence in the sector as a competitive influence through, for example, disrupting established approaches to offering services, innovation and pricing. We will consider:

- (a) whether AWAL's model is seen as disruptive; and
- (b) if so:
 - (i) whether AWAL has been a more significant disruptor than other A&L providers;

¹⁵ The [Merger Assessment Guidelines \(CMA129\)](#) state that the CMA's assessment will reflect the future competitive conditions expected after entry or expansion by the merger firms has taken place (paragraph 5.14). However, it is not necessary for the CMA to conclude on the precise characteristics of the products or services that would be offered. (paragraph 5.12).

- (ii) whether there are other A&L providers which have the ability and incentive to provide a significant dynamic constraint;
 - (iii) the current and prospective impact of AWAL on SME.
41. The CMA will take into account entry or expansion by non-merging rivals over a similar time horizon as the merger firms' entry or expansion.¹⁶ We will consider:
- (a) to what extent third party competitors exert a strong competitive constraint on the Parties;
 - (b) whether other A&L providers have been or are planning developments of their competitive offerings and the potential competitive impact of these providers;
 - (c) what capabilities other current and potential competitors have to expand;
 - (d) how well-developed are third parties' plans for expansion; and
 - (e) whether there are barriers to entry or expansion.
42. We will also consider how competition to distribute music through DSPs occurs, including:
- (a) whether this is expected to change over time (for example if there is an expansion of A&L providers and/or growth in mid-tier artists' shares of music distribution); and
 - (b) whether AWAL would be expected to play a significant competitive role in supplying DSPs going forward.

Market definition

43. The assessment of whether there is an SLC must be made by reference to any market(s) in the UK for goods or services. Within that context, market definition is an analytical tool that forms part of the analysis of the competitive effects of a merger and should not be viewed as a separate exercise.¹⁷
44. However, market definition is not an end in itself. The outcome of any market definition exercise does not determine the outcome of the analysis of the competitive effects of a merger in any mechanistic way. The CMA may take into account constraints on merging parties from outside the relevant market,

¹⁶ [Merger Assessment Guidelines \(CMA129\)](#), paragraph 5.15.

¹⁷ [Merger Assessment Guidelines \(CMA129\)](#), paragraph 9.1.

segmentation within the relevant market, or other ways in which some constraints are more important than others.¹⁸ We will take these factors into account in our competitive assessment. Furthermore, we may not find it necessary to conclude on the precise boundaries of some relevant markets, if they have no impact on the CMA's competitive assessment.

45. Taking the approach followed in phase 1 as our starting point, we propose to take the frame of reference as the wholesale digital distribution of recorded music (**digital music distribution**) in the UK. Given the high and growing importance of streaming, we intend to concentrate our assessment on streaming rather than downloads or radio, and unless we receive evidence to the contrary we propose not to explore physical distribution (such as CDs).
46. We consider that in differentiated markets, it is more appropriate to assess the strength of constraint the Parties place on each other in the competitive assessment rather than to precisely define the boundaries of a market.¹⁹ We will consider with regard to market definition the following points but some may be addressed within our competitive assessment:
 - (a) whether there is segmentation between A&R, A&L and other services;
 - (b) whether it is appropriate to define separate markets for services to artists and labels, and for distribution, or whether these are better considered as aspects of the same market; and
 - (c) the appropriate geographic market.
47. We will also take account of the practicability of defining and measuring participants' activities and shares within different candidate markets.

Neighbouring rights administration services

48. In the Phase 1 Decision, the CMA considered whether the Merger may lead to horizontal unilateral effects in the supply of neighbouring rights administration services in the UK. However, given the presence of other close competitors, and the limited market presence of Sony's neighbouring rights administration services, the CMA found that the Merger did not give rise to a realistic prospect of an SLC on this basis.

¹⁸ [Merger Assessment Guidelines \(CMA129\)](#), paragraph 9.4.

¹⁹ [Merger Assessment Guidelines \(CMA129\)](#), paragraph 9.4.

49. Therefore, we do not propose to investigate neighbouring rights administration services. However, we might consider these services if significant new evidence is presented to us.

Countervailing factors

50. We will consider whether there are countervailing factors which are likely to prevent or mitigate any SLC that we may find. In particular, we will investigate whether entry or expansion will be timely, likely and sufficient to prevent an SLC arising.²⁰
51. The impact of the potential expansion of other suppliers will be assessed within our competitive assessment. We will also consider the potential for entry into digital music distribution in the UK, whether in A&R, A&L or DIY platforms, whether any such entry may be expected to occur as a consequence of the Merger (rather than being part of the counterfactual), and whether such entry might prevent any consequences from the Merger.

Possible remedies and relevant customer benefits

52. Should we conclude that the Merger has resulted, or may be expected to result, in an SLC within one or more markets in the UK, we will consider whether, and if so what, remedies might be appropriate.
53. In any consideration of possible remedies, we may in particular have regard to their effect on any relevant customer benefits that have arisen or may be expected to arise as a result of the Merger and, if so, what these benefits are or are likely to be and which customers would benefit.²¹

Responses to this issues statement

54. Any party wishing to respond to this issues statement should do so in writing, no later than 5pm on Monday 25 October 2021 by emailing sony.awal@cma.gov.uk.

²⁰ [Merger Assessment Guidelines \(CMA129\)](#), paragraph 8.31 and 8.32.

²¹ Section 30 of the Act; see also [Merger Remedies \(CMA87\)](#), paragraphs 3.4 and 3.15 to 3.24.