STATEMENT OF MARTIN MILLS
FOUNDER AND CEO
BEGGARS GROUP
TO
UNITED STATES SENATE ANTITRUST, COMPETITION POLICY AND CONSUMER RIGHTS SUBCOMMITTEE

IN RE: The Universal Music Group/EMI Merger and the Future of Online Music

21 June 2012

A. BACKGROUND

1. Mr. Mills' Role In Independent Music.

Martin Mills established Beggars Banquet in 1974, initially as a series of record shops, and guided its expansion into the Beggars Banquet record label in 1977 and subsequently into other label and joint venture operations. The Beggars Group has established and participated in the 4AD and XL labels, amongst others. In 2002 it completed the purchase of 50% of Matador Records, one of America's largest and most respected independent labels, and in 2007 similarly brought the legendary Rough Trade Records into the group. The Beggars Group is now one of the biggest independent music groups in the UK, and worldwide the largest owner-run group of labels in the alternative sphere, with its USA headquarters in New York, as well as offices in Los Angeles and nine other international capitals, together with joint venture companies in Spain and Australia. The group now comprises four primary active current labels- XL Recordings, in partnership with Richard Russell, 4AD, Rough Trade and Matador. Following a split with his original partner in 1989, Mr. Mills is now the sole owner of the Beggars Group. Beggars was featured in the top forty of the Sunday Times Fast Track International 100 in 2010, and 'Contra' by Vampire Weekend became in the same year the first USA Number One album for a UK independent label for a quarter of a century. Fast Track again recognized Beggars in 2011, this time as one of the top 25 UK companies in terms of five year profit growth. Adele's album "21" became in 2011 the biggest selling album worldwide, by far, and is now one of the ten most successful albums ever.

Mr. Mills has been actively involved in promoting the collective interests of the independent sector, and was instrumental in the original setting up of the Association of Independent Music in 1999, IMPALA in 2000, A2IM in the USA, and most recently the Worldwide Independent Network, each representing the interests of the independent music industry, and Merlin, the rights licensing and rights protection agency for independents. He has been Vice-Chairman of AIM and Chairman of IMPALA and a board member of A2IM, where he is being honored with the organization's first lifetime achievement award, and is actively involved in music industry issues generally, through his participation in the government's Music Industry Forum, the Music Business Forum, at the board of UK Music, and as a director of PPL and VPL, the industry's rights licensing bodies. He was awarded an MBE in the 2008 New Year honors, as well as outstanding contribution awards from Music Week, the Radio Academy, the Featured Artists Coalition, and the Music Producers' Guild.

Artists that he has worked with over the years include White Stripes, Pixies, Interpol, Cat Power, Mercury Rev, The National, The Delgados, Basement Jaxx, The Prodigy, Badly Drawn Boy, The Cult, Bauhaus, Adele, Radiohead, Gary Numan, Dead Can Dance, Vampire Weekend, Bon Iver, The XX, The Horrors, Tuneyards, and TV On The Radio.

2. Why Beggars Group Is Opposed to the Universal Music Group/EMI Transaction

Beggars Group believes that the proposed transaction is the worst outcome in competition terms for the music market and particularly for the development of the online market. It will result in further concentration of an already concentrated oligopolistic market, and remove one of the closest competitors to Universal Music Group ("UMG"). This outcome is avoidable as there were other serious bidders for EMI (who would be likely to remain interested should the transactions be blocked and none of whom would raise the same regulatory concerns).

A UMG/EMI merger would produce a reduction from 4 to 2 Majors, not 4 to 3 Majors. It would transform the market into one where the two market leaders (Universal and Sony) face little competition from the one trailing Major (Warner) (collectively the "Majors") and the independents, fragmented and small competitors who are left even further behind by this transaction. There is no evidence whatsoever that their position is likely to improve in the future.

There is also the danger that there will effectively be a duopoly in the recorded music industry post this transaction. The UMG/EMI transaction would produce a significant reduction in competitive pressure on the two market leaders post-merger, resulting in unilateral anti-competitive effects. According to IFPI data for 2011 UMG/EMI and Sony would control 70.2% of the U.S. recorded music market.

This transaction is quite similar to the duopoly concentration levels which would have been created from the AT&T/T-Mobile merger, which was opposed by the Department of Justice and ultimately withdrawn. The concentration levels in the music market are higher than in the AT&T case, and the duopoly market shares are comparable. In that case, AT&T and Verizon would have been the duopoly with the trailing competitor, Sprint, having approximately the same market share as does Warner in this transaction.

3. Relevant Markets Impacted by the UMG/EMI Transaction

The physical and digital markets need to be looked at both separately and together. Whichever market definition is settled upon, revenues from the physical recorded music market remain important, with digital climbing to 52% in the USA for 2011 according to figures from the IFPI, compared to 31% for the world.

As regards the geographic definition of the market, Beggars Group considers that the market has both national and international characteristics.

B. COMPETITIVE POSITION OF THE MAJORS VERSUS THE INDEPENDENTS

Although "ordinary" market shares are indicative of market power, control of hits and the Top 100 and essential back catalogue ("must-have" repertoire), control of publishing as well as recording, distribution, scale, marketing power, vertical integration and access to media are equally important. When assessing market shares, there are a number of points to bear in mind:

1. Assessing market power through functional market share analysis

It is vital to count the market share of what a company distributes as well as what it owns, as that is what it uses in its commercial negotiations and is therefore what dictates its negotiating power. That is why Universal's arguments about looking at ownership are misplaced in the context of a competition or market power analysis. It is also important to note that increasingly the Majors are insisting that they also obtain online rights as part of a physical distribution deal. Of course charts based on ownership are important when it comes to assessing the independents' sector contribution to innovation and diversity, for example, and should be published, but they are not an adequate measure of market shares or market power.

Market share of hits such as the Top 100 (and indeed the Top 10) are important because they generate the vast majority of sales both online and offline.

When looking at hits such as the Top 100, market shares must be based on actual revenues or some other weighting as ten hits at number 99 clearly do not produce the same market power as ten hits at position no 1.

It is crucially important to consider a company's position in publishing and recording combined because a digital service needs to acquire both the recording rights and the publishing rights to a track in order to distribute it.

When looking at publishing, it is important to remember that many songs have more than one author, who do not necessarily have the same publisher. Each publisher of each part of the song can refuse a license, sometimes called "negative rights." Each Major therefore can have effective control over significantly more music than that Major's market share.

Back in 2000, Universal wrote to the European Commission to oppose the Warner/EMI attempted merger, saying "… in measuring market share, some account must be taken of jointly controlled work in assessing possible market power or dominance arising from the merger. It would be quite wrong simply to look at the works which are wholly controlled by the two parties and say that's all you need to look at to see whether they would have market power or not."

"Must-have" repertoire extends a company's power beyond its market share. For example, Majors also use their lead artists to leverage their whole catalogue (*e.g.*, "you can have Beyoncé if you also use my new alternative artist abc").

(a) The competition risk of excess market power

Competition risks from high market shares and high market power apply across the whole market, not merely online. High market share produces excessive control of the whole market, including pricing and other consumer terms such as the amount of music available in free tiers of subscription services (*e.g.*, Spotify), arising from the increased ability to shape online and other services using music. It also results in reduced innovation generally, fewer artist signings, lower market access for competitors (radio, retail, online, media, publicity), lower consumer choice and diversity. These are all equally detrimental ways of exploiting market power.

For these reasons, Beggars Group considers that there is no choice but to block the UMG/EMI transaction outright.

(b) Market shares of the proposed transaction

As of the IFPI data for recorded music market shares for 2011, all of the markets on a post-transaction UMG/EMI basis (combined shares as follows: physical-- 43.3%, digital-- 40.5% and total-- 41.7%) were "heavily concentrated" as defined in the United States Department of Justice Antitrust Division Federal Trade Commission Horizontal Merger Guidelines. See Horizontal Merger Guidelines ("Guidelines") at 31.

The pre-merger concentration for the overall market is 2312, with a post-merger concentration of 2963 and a change of 651. The pre-merger physical recorded music product market HHI is 2499, with a post-merger concentration of 3269 and a change of 770. The concentration ratio for the digital market falls into the same orders of magnitude (*i.e.*, pre-merger concentration of 2191, with post-merger concentration of 2744 and a change of 553). In all of the markets, the Guidelines dictate that these concentration ratios are "highly concentrated" and "potentially raise significant competitive concerns and often warrant scrutiny." Guidelines at 32.

Moreover, the transaction will create an entrenched duopoly of UMG/EMI, with post merger market shares of 41.7%, and Sony, 28.5%, with a resulting duopoly share of 70.2%.

Universal constantly downplays its 30+% market share of total recorded music, and certainly makes light of the 40+% share resulting from the UMG/EMI transaction. It goes as far as to claim that market share does not equal market power. One should wonder whether Universal downplays its market shares in its commercial negotiations, in its discussions with music services about advances and equity, and in its arguments for splitting anti-piracy settlements. You can be sure that the 30+% figure is front and center, and the 40+% will shine even brighter if the UMG/EMI transaction is permitted to close.

It should also be noted that the real market share of Universal can be much higher depending on the territory, the genre, the week and whether we are looking at the whole market or hits, discussed in more detail below in the context of "must-have" repertoire. Finally, the market power which such market shares produce is also higher than the actual share due to the "multiplier effect" market share and market power give a company at Universal's level. A good example of this phenomenon is Universal's position in terms of publishing and recording. For example, Universal would for last week's Billboard hit singles chart control have 8 of the top 10 singles. This gives enormous power to any company over any service needing a license for that music.

And of course, the real aim of this merger is to drive that market share even higher than the current total by leveraging the new combined strength.

Beyond the top 3, the recorded music market is highly fragmented with no participant in either physical or digital relevant product materials presenting any possibility whatsoever of being able to limit the duopoly's exercise of market power. The independents cannot be viewed as a block and the remaining market share would have to be divided between many disparate players.

Universal has been touting the Indies as a Major, able to exert "very significant constraints on anti-competitive behavior." This contention is as far from reality as it can be. First, the "Independent" or non-Major, category data consists of hundreds and thousands of independent labels, none of which has more than 1-2% of the total recorded music market. While these are fabulous and creative companies they are not corporate behemoths capable of taking on Universal. We at Beggars Group have Adele, one of the biggest selling artists, yet we are a fraction of the size of the nearest major. This also helps to put context around the argument that the success of Adele proves the independents are major competitors. In any event, Adele has such a unique ability to touch so many people all over the world, she is a phenomenon, completely unstoppable, breaking all the rules and as everyone in the business knows, no conclusions from what's happened can be drawn. If UMG wants to demonstrate the market impact of independents, it should look at the second and third biggest selling independent album of the year, or the biggest one from any other year. In many ways her success precisely underlines the barriers facing independent companies as she is actually signed to Sony in the U.S. to make sure she had the access to media required. It should also be remembered that UMG's publishing affiliate publishes Adele.

Merlin, which provides agency services for independent labels in the field of online licenses for certain services such as streaming (not download, which is the dominant part of the digital market), estimates that it is a fraction of UNI/EMI's market share and market power in the digital and overall market.

(c) The impact of removing EMI's competitive pressure

Due to its position as the #4 Major EMI has been able to exert competitive influence upon its fellow Majors. EMI's licensing of its music rights to Pressplay, a digital music service in which it had no equity interest which competed with a service that EMI had an interest in, set a new standard for the Majors. Previously the Majors had been averse to dealing with music sites they had no interest in. Forbes magazine touted this step by EMI as ground breaking, particularly so as it influenced the other Majors to follow its lead. Also EMI was the first Major to abandon the restrictive technology of DRM, a consumer friendly innovation that everyone ultimately adopted for downloads.EMI's exercise of competitive pressure will be lost with this transaction.

For Universal, the increased concentration from the EMI transaction would simply mean adding more market power to Universal's pre-existing strength, enhanced of course by the removal of a significant competitor, effectively a four to two reduction.

(d) Must-have or "incontournable" repertoire – Universal is already too big

Universal's grip of "must-have" repertoire, already huge, will only increase in size post-merger. The heterogeneous nature of music content and the fact that music products are not substitutable for one another, unlike airline tickets or bank accounts – means that a consumer wanting to buy a Lady Gaga album will not settle for Adele instead, which enhances the power attached to owning vast repertoire.

This power is also compounded by the fact that music services cannot succeed unless they have access to all the key repertoire. The repertoire of Universal has already been dubbed "incontournable" or "must-have" by the European Commission in its decisions in the UMG/BMG transaction, paragraph 270:

> "The following analysis demonstrates that the merger clearly reduces the online providers' possibilities to circumvent UniBMG . . . and the combined repertoire . . . even constitutes such a must have repertoire which cannot be replaced by other companies."
>
> It was also noted that the Commission had received replies to its market investigation, which indicated that " . . . Sony BMG and Universal are in any case required content as they make up the vast majority of hit material."

At paragraph 254, the European Commission regulator found that:

> "The market investigation indicates that in some cases major record companies with large record repertoires and high market shares have succeeded in imposing higher licensing rates for recording rights than smaller major record companies. The online and mobile music providers which reported such rate differences referred to the higher bargaining power of those majors with higher market shares as their catalogues are of greater importance for an online and mobile music provider."

This position would be reinforced and the market power of Universal increased following the EMI transaction. What is equally important is not just the issue of licensing rates, but the impact on the licensed service as a whole through advances, minimum guarantees in terms of revenue or output, access to promotional and other shop windows, and the ability of such repertoire owners to use their power to mould the look and feel of music services and restrict the consumer offering.

The question is whether one Major holding as large a basket of repertoire as Universal currently holds causes antitrust concerns. The answer is assuredly in the affirmative. Given this, there is no argument for allowing Universal to grow any bigger through acquisition and thus increase barriers to expansion of competitors and of entry to new online services.

The substantial advances required by music labels and publishers have already been quoted as excessive and have been claimed to be relevant to the demise of recent innovative digital start-up Beyond Oblivion which was closed before launching its first product and whose costs of advances to rights owners were said to be up to $87 million since it opened in 2008. You can be sure UMG was at the forefront of that. Another example was Nokia's music service

"Comes with Music", which was initially licensed by Universal and came to market with huge expectations, but was effectively strangled by excessive financial demands and other controls which resulted in a service that consumers did not want.

Finally, it should also be noted that "must-have" repertoire can impact the physical market as well. In fact, it extends a company's power across the whole market beyond its market share. For example, Majors also use their lead artists to leverage their whole catalogue (*e.g.*, "you can have Beyoncé if you also use my new alternative artist abc") when it comes to radio, television, and promotion.

2. The importance of scale and other factors relating to market power

Market power is reinforced by scale and marketing, as well as size of repertoire and access to media. To understand this better we need to consider what record companies do, how they operate and the barriers to entry and growth.

(a) Barriers to entry and growth

It is sometimes said that barriers to entry in the recorded music industry are low. It is after all relatively easy to make music and to put it on the Internet. That, however, is very far away from the business of being a record company, which does not just make music. Its activities are far broader, extending to seeking out new artists and genres of music, signing artists (and being asked to pay advances), making professional recordings in the studio, manufacturing CDs and other formats such as vinyl, distributing music in multiple territories, promoting artists to music critics, plugging radio and TV shows, multiple media in all territories as well as advertisers, being members of collecting societies in multiple territories, collecting revenues all over the world, negotiating with distributors and retailers all over the world, negotiating with global online services. That is why there are barriers to entry, and of course to growth, in the business. This is also why the Majors' size and breadth reinforces these barriers, imposing barriers in and of themselves.

(b) The Majors' access to the media

Generally, the Majors have a wider relationship with retail and all key media and routes to the consumer such as radio, television appearances, television productions, talent shows, video channels, and compilation in which the Majors leverage, as mentioned above.

Access to TV, radio and other media is key. My own company is pertinent here. We needed to agree to work with Columbia Records part of the Sony group for the U.S, to publicize our biggest artist Adele despite her worldwide acclaim.

Access to advertising opportunities, for example on radio and television, is also crucial. Bulk buying of TV advertising slots by the Majors occurs in almost all territories which limits opportunities for other companies.

Access to media in turn impacts a label's ability to sign artists in the first place.

(c) The Majors' access to online services

In addition, the Majors have better access to online services than the independents. Universal, for example, can obtain better online deals than the independents and in addition has better market penetration, and access to media. This allows it to attract/consolidate major stars on the upstream market for signing artists. If independents cannot get an equivalent online deal for their artists, they may lose them to the Majors.

The Majors' approach to the online market has been interesting in itself. Originally, as the Antitrust Division of the U.S. Department of Justice found in 2005, the Majors had tried to stifle the development of music platforms altogether for the legal on-line distribution of music, as their model was to control distribution as much as possible through their own platforms MusicNet and Pressplay. When the investigation was concluded, the DOJ found that such behavior had terminated.

Once the Majors embraced non-owned services, their strategy to control continued, but in a different way, with negotiations for equity in new services and effective approval over what services can and cannot offer, for example with Myspace Music, another failed venture. The Majors have also attempted to recreate the physical shopping experience or shop window online, with greater prominence given to listings of the Majors, and the Majors dominating advertising in the way they have offline.

The desire and ability to control new markets such as digital continues today. The Majors use the same tools to mould online services and direct consumers in the same way as they did with physical retail, to create barriers for other competitors and stifle innovation. They apply the traditional offline format to a new medium rather than allowing digital services the requisite freedom to develop new and innovative services for consumers. As mentioned above, the Majors have also used their market power to shape the look and feel of online services, as well as moulding the offering itself.

(d) 360 deals enfore the Majors' dominance

Scale also impacts a label's ability to offer 360 deals, a key way in which the Majors are able to attract and retain artists. 360 deals or multiple rights deals mean artists and labels collaborate not just on record sales but also on concerts, merchandising, publishing and other efforts. These deals are a key way that the Majors tie up artists on a long term basis. Although some artists and some independents do not believe that the model works for them, scale and access to key related sectors such as live, merchandising, and publishing are vital, and Universal is in an unparalled position, and the recent Live Nation tie-up further enhances the attractiveness of Universal's offer.

(e) The practical results of the Majors' scale and market power

In the recorded music market, the scale and market power of the Majors gives them advantages over the independents at all of the following levels of the market:

- Access to the financial and corporate muscle required to grow and compete.
- Ability to sign artists and keep artists already signed.
- Ability to offer bigger and better 360 deals.
- Creation and production of recorded music.
- Access to huge back catalogues.
- Access to advertising opportunities.
- Access to radio - a 2009 study conducted by the American Association of Independent Music (based on radio playlist data) evidenced no measurable change in composition over the preceding four years, all of which was dominated by the Majors, despite changes mandated by the Federal Communication Commission to make radio access more open, which rules stemmed from the findings of payola (illegal pay for play) during the New York State investigation which resulted in settlements of millions of dollars paid by the Majors in 2005.
- Access to touring, merchandising and other increasingly important opportunities.
- Control of key facilities such as charts, collecting societies, industry associations and databases, anti-piracy actions.
- Access to distribution.
- Access to retail, and the terms of that access (including access to racking, in-store charts and in-store radio).
- Strength of market share in the charts (current and past) and other "must-have" repertoire.
- Access to media in all its forms – radio, TV, music magazines – as well as to advertising in order to implement an all-round marketing strategy.
- Vertical reach and integration.

Post merger these advantages will only increase for Universal, making it too powerful for effective competition to exist on the market, especially given the power of the competitors left behind, and creating barriers to entry/expansion in all of the digital music industry.

3. Competition from the independents

For the reasons cited above, the gap between the Majors, in particular the market leaders, Universal and Sony, and the independents, has never been bigger. The Majors have greater chart, radio and retail share than ever before. With few exceptions, the independents' ability to break artists internationally and even nationally is severely compromised by the costs of marketing, restrictive licensing from Majors (which affects independent compilations and sample usage), and the targeting of artists, airplay, television exposure and retail placement by the Majors. On the upstream market of signing artists, the power of Majors to sign artists is much greater. Majors can pay more advances, higher royalties, invest more money for marketing and because of vertical integration with TV, movie or mobile networks, as well as live and merchandising, will be more attractive. Further, the Majors can rely on their vast back catalogues, which provide them with unique leverage.

All this means the gap between the Majors and the independents is increasing with only one or two independent labels enjoying more than 1% global market share.

Beggars Group has been a phenomenal independent success story in 2011 – Adele signed with XL Recordings, one of our labels. However, an artist like Adele is exceptional and comes along only every 15 to 20 years. Anyone working in the music business knows that no conclusions can be drawn from her success. In our case, in the U.S., it provides a neat example of why the UMG/EMI merger should not be allowed, as even Adele needed a Major, Sony, to work with her in the U.S., due to the importance of access to media.

What is also interesting is the reaction of the Majors to this success. One commentator, herself a songwriter, noted that a Major label executive had told her "We can accept XL having the biggest selling artist for one year. But next year it better be - it has to be - one of ours." (Source: Guardian music blog 29 December 2011).

Of course, independents do succeed, on their own terms, and on their own home turf, often different from the Majors. We see this porposed acquisition as an attempt to restrict that.

4. Merlin does not provide competitive counter-balance

Merlin is a one-stop shop digital recording rights licensing and rights protection organization, providing certain opt-in services to members. It is only active in the recorded music market and only in relation to digital rights. It does not have agreements with the mainstream music services such as iTunes or Amazon, which are dealt with directly by Merlin's member labels. It is not a label. It does not own or license or distribute or fulfill music. It is not in any way involved in publishing rights, or artist relations or management, A & R or in any promotional or marketing aspects which are vital in both the online and offline worlds. All of these tasks are carried out by music labels themselves.

It has been said that Merlin is the fifth major. Indeed it has called itself the "virtual 5th major," but that does not mean it is a major record company. While Merlin has a significant number of independent labels as members, not all participate in Merlin's licensing activity (because these members have negotiated away their rights to other parties or do not opt in to Merlin services). As a result Merlin's share of the digital market is a fraction of UNI/EMI's market share and market power in the digital and overall market - hardly the strength of a "fifth Major."

C. VERTICAL INTEGRATION

The vertical aspects of concentration in the music market are vital.

Universal is truly a vertically integrated global company, as is Sony.

Universal is a subsidiary of Vivendi, an international media company with interests in media, telecommunications, mobile, video games, film, television as well as music. Universal itself is active worldwide in recorded music and music publishing. It also has activities in music catalogue management, merchandising through its full service merchandising company Bravado, artist management and media metrics (now enhanced by the Universal/Live Nation tie-up) and in music distribution.

VEVO is a good example of a joint venture between the duopolists (Universal and Sony) in the establishment of a music service. It demonstrates vertical integration of a distribution service by the market leaders, who clearly both separately and jointly control vital output for music.

In terms of distribution, although Universal recently sold Fontana, its independent distribution business, it retained a significant stake and continues to distribute through the company. This effectively means Universal continues to control an important part of the physical distribution business for independent labels in the U.S., which will be exacerbated if Universal is allowed to buy EMI and its independent distribution company, also a significant distributor in the USA. Fontana is also active in the digital distribution field via INGrooves who is now the main shareholder. As far as digital distribution is concerned generally, the number of options for independent labels has significantly decreased with Sony just completing a merger with IODA and the Orchard, the two main independent aggregators for independent labels. We expect distribution options for independent labels in both the physical and the digital market to be significantly reduced after the transaction. Again we see the emergence of a de facto UMG/Sony duopoly and an attempt by them to re-establish and increase their control of the market. Most of the Majors now operate label services divisions, offering resources to independent label and artists – but these should not be seen as altruistic support for the market, but rather as a means to lock in repertoire that might turn out to be successful, at no risk.

The Universal/Live Nation tie-up is also key, giving Universal increased market share through Live Nation artists (for example, Madonna's new album is a Universal release), plus a foothold in all key markets linked to music from live to ticketing to artist management to social media metrics, merchandising etc., as well as recording and publishing. Is it in the public interest to allow such huge interests to work together and completely control the music market from A to Z, and then allow

Universal to attach another huge chunk of market share through EMI, neatly creating a new "tipping point" in the whole industry structure so that, no competitor can possibly compete?

The answer is clearly no.

D. DIGITAL MARKET COMPETITIVE DISCIPLINING INFLUENCES

1. Is there countervailing competitive pressure from digital platforms?

Every time this question has been examined by regulators, the answer has been no.

We understand that the European regulator specifically rejected this argument in its recent decision on Sony/EMI (public version not yet available). In its previous UMG/BMG decision the EC found that not even Apple would be able to exert effective constraints on UMG's pricing behaviour (¶¶ 383-385 UMG/BMG).

The reality is that no company, no matter how big, can run a music service without Universal because its repertoire cannot be obtained elsewhere. For the same reason, we do not believe that physical retailers have countervailing power over the market leaders.

Universal touts that the digital and physical markets have developed around a "few players which exercise strong buyer power in their various fields," and that the music business needs "sustainable market players" to thwart the "few players" and control the new innovators in the market. There is no reality to this argument. Universal does and will control a large portion of the music business. Any music service or purchaser that crosses Universal will be left with enormous holes in their repertoire, to devastating effect.

Jean-Bernard Levy of Universal seems acutely aware of this power. He specifically said the EMI transaction is seen as a way to ensure that it increases its muscle in relation to digital services stating, "*In recent years our influence in the music market has declined . . . but the music business itself is rebounding.*" Mr Lévy commented that by gaining muscle with the EMI bid, Universal Music would improve bargaining power in price talks with digital distributors. (See WSJ article "Vivendi defends its turf").

Look at the terms Universal was able to impose on even Google for its new download service!

2. What is the impact of piracy and purported market decline?

Piracy is a problem but there are differing views on its impact. For example, one U.S study shows that, while a large percentage of Americans (around 30%) do pirate music, much of this piracy was casual. Legal streaming services also show signs of displacing some piracy: of the 30% who have pirated, 46% indicated that they now do so less due to the advent of low-cost streaming services (Source: The Copy Culture Survey: Infringement and Enforcement in the US from the American Assembly at Columbia University).

Even if we ignore such evidence, piracy is clearly not a competitor in itself. There is no sign in the market that the Majors reduced their prices or other demands to online services because of privacy. This goes against claims that piracy has exerted a restraining competitive pressure on Universal and Sony. We understand, for example, that the European regulator did not accept that piracy has a countervailing effect in its recent decision on Sony/EMI (public version not yet available).

In any event, even if the threat of illegal downloading were to limit the pricing power of any market player (which we do not accept for the reasons cited above), charging higher prices is not the only way in which market power can be exploited. Reducing investment in artists, limiting choice and reducing quality and reducing value for consumers through restrictions on online services, are other ways in which market power can be exercised in order to increase profits, and the threat of piracy does nothing to limit the extent to which such strategies can be pursued.

In terms of market decline, music is hardly a failing market and neither is EMI a failing firm. All IP-dependent industries have struggled with the challenges of online, and music has arguably dealt with those threates first and best. Data shows the market may be reaching or has reached a tipping point as regards market decline in the USA. According to RIAA 2011 year-end statistics:

- U.S. music shipments in 2011 were up for the first time since 2004 (shipments of $7bn up 0.2% on 2010)

- Digital sales grew 9.2% on 2010, offsetting physical decrease of 7.7%

- Digital became more than half the market for the first time ever at 52%.

A recent study by Barclays Capital published by Music & Copyright on 29 November 2011 also sees a turnaround in sight. It sees annual growth in four of the top five markets by 2015 (Source: Barclays Capital forecast for annual music retail sales change in top five markets by format, 2011-2016).

What Sony boss Nick Gatfield had to say is also interesting. He noted that the digital revolution has not been all bad as 35% of Sony UK's music sales come from online. He was also quoted as saying "*In a weird kind of way this business needed a massive shakeup. It clearly got bloated on the back of the CD boom*." (Sources: Hollywood Reporter December 2011 and Guardian December 2011 "This business needs a massive shakeup").

Universal executives Lucian Grainge and Boyd Muir have stated that the company encourages subscription services as a superior consumer alternative to piracy. Universal has seen a 13.5% increase in digital sales in 2011, this and increased licensing and merchandising income offsetting the decrease in physical sales, although revenues still decreased overall by 1.9% in the first half of the year but with a rebound in the second quarter (Source: Vivendi press release 31 August 2011 and see also FT article "Vivendi signals end of spending spree"). The third quarter 2011 figures also confirmed the rebound observed in the second quarter. In the FT article mentioned above, a UBS analyst is quoted, saying "*the [music] market may be reaching an inflection point after a decade of decline.*"

All of this data stands in sharp contrast to the "sky is falling" arguments made by Universal in the press—significant declines in sales between 2001-2010. The reality is that the marketplace is in transition from the Majors' carefully controlled physical market to the digital market which they intend to be similarly carefully controlled. Universal needs the EMI transaction to increase its stranglehold over the digital market.

In any event, even if market decline continues/returns, it would do so for all players, and does not reduce the power of the individual Majors on the market who would be competing within the same market structure.

On the basis of the above, piracy is not a competitor, the market is not failing, and the merger is specifically designed to give Universal more pricing and other power in the digital marketplace. Jean Bernard Levy, CEO of Vivendi, Universal's parent, sums it up nicely as mentioned above when he said a few months ago – "*The aim is to boost Universal's bargaining power with mass-market stores and a new breed of online distributor, such as Apple and Spotify. By gaining muscle with the EMI bid, Universal Music would also gain bargaining power in price talks with digital distributors.*"

3. Will there be an impact on innovation from the transaction?

Reduced staff and overheads necessarily results from mergers. With that comes a reduced ability to manage artists, which means fewer are signed and more are dropped or "put on ice." Investment in innnovating with new artists and genres will suffer as it has done with every merger in the past (see more below under "What will be the impact on artists?").

So too will innovation in terms of online services suffer. As mentioned above, the Majors put up barriers to licensing of new services at the beginning of the digital market. The Majors have now embraced digital services but their ability to control innovation continues unabated.

The effect the Majors had on iTunes track pricing, getting the prices raised, is just one example. The effect they had on eMusic is another – when that music service decided it couldn't survive on just indie music and brought on board the Majors one by one, it was the arrival of Universal that saw their front line pricing rise – and the consumer, and indie labels, lost their home on the web.

Universal will, post merger, have enormous power to shape deals with new services and crucially, the terms upon which other companies' music is made available. This level of control does not benefit consumers, who, rather than being given options to choose from, are presented with services that the Majors have moulded.

4. Are there legitimate efficiencies flowing from the UMG/EMI Transaction?

In order for efficiencies to counter anti-competitive effects, they have to benefit consumers, be transaction-specific and be verifiable. It is difficult to see how any efficiency produced by this transaction would be of benefit to consumers. How likely is it that the transaction would produce lower prices, better products and service offering to consumers, in the short and long term? Not likely at all.

5. Does EMI need the UMG acquisition?

EMI is a thriving company. It holds very significant back catalogue artists including the Beatles, often seen as the crown jewels of the recorded music market. Coldplay is also in their repertoire. It is also key in classical and jazz with labels such as Blue Note. Its catalogue could make it increasingly successful as the digital market grows.

EMI's main problem was its debt, which has now gone, making it a stronger player. In addition, EMI currently exerts significant competitive pressure on Universal and Sony. There were several bidders for both EMI recording and publishing. We believe that those bidders are still available and interested in EMI if the Universal bid is rejected.

For these reasons, Beggars Group believes that EMI would have a very successful future and does not "need" Universal.

Universal is understood to be making impressive claims about how it will invest in EMI in the future, for example by reinvigorating certain labels. We believe these claims need to be substantiated and compared to the overall picture of what will happen post merger, to the whole EMI company. It has never been the case in any merger that investment into artists has increased. The overall trend is always to decrease staff and investment in labels (and artists, whether existing signings or new potential signings, see below).

6. What will be the impact on artists?

Investment in innnovating with new artists and genres will suffer post-merger. Fewer artists will be signed, artists will be dropped, catalogue will be less actively exploited (except for the "cherries on the cake"), and EMI labels and artists will be morphed into the Universal system. Cost savings are not possible otherwise. The same would happen as has happened following most other acquisitions – *e.g.,* V2 and Sanctuary.

We have been told that artists being signed to EMI are being assured that only small and meaningless acts will be dropped. How will "small and meaningless" be defined?

We understand that Universal is also making certain claims about investment trends in artists by EMI which it claims has been decreasing and will be corrected by Universal. What is Universal's own investment trend over the past few year? Our impression is that this has decreased for all major labels, not just EMI.

Exactly how would Universal increase its overall investment in artists but make the cost savings it needs to ensure the merger is profitable?

Finally, artist careers will also suffer from having even less bargaining power and will have one less door to knock on if they want to sign to a Major label. Career alternatives in terms of independent labels will be less attractive as those labels' market access will be further restricted by the proposed merger. Fewer artists will be able to make it to radio, television or obtain the best touring slots or the best exposure if they are not signed to UMG/EMI or Sony.

Universal have been touting that this acquisition has the support of artists, unions, and those who work in the creative music industry. It is true they have the official support of some unions who represent, amongst others, recorded music artists in the U.S. However, the worldwide federation of musician's unions opposes the deal, and does not understand why there is support in the U.S. The truth is that Universal, in its many guises, is already such a dominant employer that people dare not risk speaking out against them.

7. What will be the impact on consumers?

Based upon the above it should be clear that consumers will be adversely affected by the UMG/EMI transaction. Price increases, stifled innovation, excessively controlled online market, limitations on music choice for consumers, marginalization of independent artists and labels, and squelching of independent music development are among the ills that the transaction will exact upon consumers.

D. CONCLUSION

We appreciate the opportunity to bring the views of Beggars Group, and the independent recorded music world generally, on the anticompetitive consequences of the proposed UMG/EMI transaction to the attention of the Subcommittee. The transaction will lead to a loss of consumer choice, injury to competition, increased barriers to entry, impairment of innovation, further entrenchment of the Majors to the disadvantage of independent recorded music, increased molding of the online market and ultimately increased prices/reduced terms for consumers. This transaction should not be permitted to go forward.

Thank you.