
Digital radio access undertaking Submission in response to the ACCC's draft decision dated 18 December 2008

Commercial Radio Australia – Public Version

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1 Introduction and Statement of Interest

Commercial Radio Australia Limited (**CRA**) is the peak industry body representing commercial radio broadcasting stations in Australia. CRA has 260 members and represents approximately 99% of the commercial radio broadcasting industry in Australia.

CRA has been heavily involved in the development of the access regime for digital radio services in Australia.

CRA appreciates the opportunity to comment on the ACCC's draft decision dated 18 December 2008 (**Draft Decision**).

This submission responds to the Draft Decision and has been prepared by CRA on behalf of the Eligible Joint Venture Companies (**EJVCs**) that have lodged digital radio access undertakings with the ACCC.

2 Executive summary

CRA agrees with the ACCC statement that the extent of the changes required to the digital radio access undertakings to ensure approval are not major.¹

However, while CRA does not have any objection to most of the changes to the access undertakings that have been identified in the Draft Decision, it does not agree with some of the ACCC's analysis that has underpinned aspects of the Draft Decision and the conclusions that flow from such analysis.

CRA's concerns in this regard are primarily focused on the ACCC's analysis of the pricing principles. In particular, CRA does not agree with the ACCC's view that there are insufficient incentives on EJVCs to ensure that its costs are efficiently incurred.

CRA submits that:

- 'gold-plating' is not a serious risk with respect to investment in digital radio multiplexing facilities – the ACCC appears to have overlooked this fact in its Draft Decision; and
- the various incentives identified by the ACCC that exist outside, and independently of, the access undertaking, are in themselves sufficient to ensure that the costs incurred by EJVCs are efficient – this includes:
 - the common shareholding that exists (or, in the case of digital community broadcasters, which will shortly exist) between EJVCs and access seekers; and
 - the limited financial benefits that are likely to accrue to broadcasters during the start up phase for digital radio services.

CRA has attached a revised version of the access undertaking for consideration by the ACCC.

¹ ACCC, Draft Decision, page 6.

In the event that the ACCC intends to provide EJVCs with a notice under section 118NF of the *Radiocommunications Act 1992* (**Radiocommunications Act**), as part of its final decision, CRA submits that the changes required by the ACCC in that notice should reflect the changes that have been specified by CRA in the revised version of the digital radio access undertakings previously submitted by the EJVCs.

3 Pricing principles

3.1 The ACCC's concerns about 'gold plating' are misplaced and do not arise in the context of digital radio multiplexing services

CRA strongly disagrees with the ACCC's concern that EJVCs may not have sufficient incentives to ensure that costs are efficiently incurred and that there is an associated risk of 'gold-plating'.²

The ACCC's analysis is overly simplistic.

'Gold-plating' is not a serious risk with respect of digital radio multiplexing facilities – this fact has been overlooked by the ACCC.

CRA is concerned that the ACCC's comments on 'gold plating' in the Draft Decision:

- reflect a misunderstanding of the nature of investment in digital radio multiplexing facilities; and
- appear to import regulatory thinking from other networked industries into its analysis of the digital radio industry, even though these concepts are not directly applicable to the digital radio industry.

While CRA appreciates that there are elements that are common to all regulated industries and that the ACCC's views in respect of the digital radio industry are influenced by its approach in other industries, it is also important for the ACCC:

- to recognise the fundamental differences that exist between the digital radio industry and other industries;
- to ensure that the scope of access regulation applicable to digital radio multiplexing services takes sufficient regard of the technical limitations of such services.

For example, there is no real risk of over-investment in digital radio multiplexing infrastructure. This contrasts with other regulated industries where 'gold-plating' may represent a valid regulatory concern.

It is highly unlikely that EJVCs will 'gold-plate' or invest in digital multiplexing facilities in excess of what is required for the effective delivery of high quality, robust services.

This is due to two interrelated factors:

- the stability of demand for digital radio multiplexing services; and

² ACCC, *Draft Decision*, page 32.

- technical constraints, together with the 6 year moratorium on new digital only entrants, that limit the number of additional services that can be accommodated over digital radio multiplexing infrastructure.

The amount of multiplex capacity that may be supplied by each EJVC is finite due to limited spectrum availability and the fixed statutory entitlements of incumbent commercial broadcasters and digital community broadcasters. EJVCs must plan, design, construct and invest in digital radio multiplexing facilities subject to these limitations.

The constraints associated with the supply of digital radio multiplexing technology have been recognised in the Radiocommunications Act, which limits demand for digital radio multiplexing services in respect of each foundation category 1 digital radio multiplex transmitter to the standard access entitlements of incumbent commercial broadcasters and the digital community representative company (which represents community broadcasters) and any excess-capacity access entitlements that may be available.

Therefore, there is no serious risk, due to spectrum and technological limitations, that an EJVC would invest in digital radio multiplexing facilities in a manner that exceeds what is required to meet its standard access obligations and excess-capacity access obligations.

That is not to say that EJVCs do not have any control or discretion in the manner in which they plan, design and construct their digital radio multiplexing infrastructure.

EJVCs have significant levels of control over the planning, design and construction of their infrastructure and the investment decisions that are made by EJVCs in respect of this infrastructure will clearly drive the cost of supplying digital radio multiplexing services.

However, the fact that EJVCs have significant levels of control over their investment in digital radio multiplexing infrastructure does not mean that there will be a serious risk of 'gold-plating'.

For example, EJVCs have procured high quality digital radio transmitters as part of their design of the digital radio multiplexing infrastructure. The fact that these transmitters may not necessarily be the cheapest transmitters available in the marketplace does not mean that costs associated with this investment have been inefficiently incurred, or that such an investment decision has resulted in 'gold-plating'.

Similarly, even though it is standard engineering practice in the broadcasting sector to have backup infrastructure in place (i.e. a hot-spare) to ensure that there are no interruptions to services, EJVCs have not yet undertaken all possible investment in such infrastructure as a means of minimising the upfront costs associated with the commencement of digital radio services.

However, over the medium term, it is quite likely that EJVCs will invest in such backup infrastructure in accordance with standard engineering practice in the broadcasting sector. The investment by an EJVC in such backup infrastructure would not constitute an inefficient investment in infrastructure, nor would it constitute 'gold plating'.

Accordingly, CRA strongly disagrees with the ACCC's premise that there is a potential for 'gold plating' of digital radio multiplexing facilities.

3.2 The common shareholding between EJVCs and access seekers provides sufficient incentives to ensure that costs are efficient

The ACCC's draft decision correctly seeks to identify influences on the incentives of EJVCs to minimise costs independently of the pricing principles.³ However, CRA does not agree with the ACCC's draft position that these incentives are, in the absence of specific prices in the access undertaking, insufficient to negate any risk that the costs incurred by the EJVC are inefficient.

In its draft decision, the ACCC stated:⁴

"The ACCC's draft position is that it considers that the degree of vertical integration between a multiplex licensee and access seekers, and to a lesser extent the fact that the facilities are new and that alternative media might provide some constraints on the extent to which costs could be passed through, provide the multiplex licensee with some incentive to operate efficiently. However, the ACCC would have reservations about relying completely on these factors for driving efficiency in the context of the proposed pricing principles and a lack of specific indicative prices within the undertaking".

CRA strongly considers that the various incentives identified by the ACCC that exist outside, and independently of, the access undertaking, are in themselves sufficient to ensure that the costs incurred by EJVCs are efficient.

The common shareholding that exists between EJVCs and access seekers provides a significant incentive to ensure that the EJVCs costs are efficient. In CRA's view, this incentive is, in itself, sufficient to ensure that the costs incurred by EJVCs are efficient.

In the event that an independent third party owned or operated the multiplexer and provided digital radio multiplexing services, CRA considers that there would be a strong risk that the costs which were incurred by the access provider would exceed the efficient costs.

However, CRA strongly considers that this is not the case in Australia where there is a common shareholding arrangement between the EJVC and access seekers.

As the ACCC is aware, incumbent commercial broadcasters have taken up shares in EJVCs and will also be access seekers pursuant to the access undertaking. Similarly, while digital community broadcasters have not taken up an offer to become shareholders as yet, it is expected that digital community broadcasters will also become shareholders in the EJVC in due course.

The ownership structure of the EJVCs means that there is a strong alignment between the interests of shareholders and access seekers, thereby removing any theoretical risks that the costs incurred by the EJVCs are inefficient or that the EJVCs may not seek to minimise their costs.

The fact that digital community broadcasters have yet to take up a shareholding in EJVCs does not reduce these incentives. This is because all access seekers will pay the same access charge for an equivalent amount of capacity. Therefore, the incentive to ensure that costs are efficiently incurred (which arises from the fact that incumbent commercial

³ ACCC, Draft Decision, page 32.

⁴ ACCC, Draft Decision, page 33.

broadcasters have taken an ownership stake in the EJVC) also benefits other access seekers that do not currently have an ownership interest.

There is also:

- no real risk that the EJVC will incur costs on an inefficient basis or seek to artificially inflate the level of access charges payable by access seekers that do not have an ownership stake in the EJVC, as this will result in the inefficiencies being borne by all access seekers pursuant to the pricing principles; and
- there is no risk that the EJVC will use access pricing in an anti-competitive manner, for example, by making the level of access charges unaffordable for certain access seekers – this is because:
 - the removal of certain access seekers would most likely result in an increase in the level of access charges payable by all other access seekers; and
 - two-ninths of the multiplex capacity is reserved for digital community broadcasters (through the representative company) and is not available for use by incumbent commercial broadcasters.

[Redacted]

[Confidential]

[Redacted]

[Confidential]

Accordingly, CRA submits that the common shareholding between EJVCs and access seekers provides a significant incentive to ensure that the EJVCs costs are efficient and that this incentive is, in itself, sufficient to ensure that the costs incurred by EJVCs are efficient.

3.3 The pass through of access charges to advertisers in downstream markets

Even though the ACCC has expressed a conclusive view in its Draft Decision, it has stated that if it is possible for broadcasters to pass higher access charges through to advertisers in the form of higher advertising charges, then there is less incentive for the EJVC to operate efficiently.⁵

CRA submits that this line of analysis is overly simplistic.

First, the ACCC's statements are predicated on the assumption that the level of access charges are likely to be set inefficiently. CRA disagrees with this assumption on the basis that the common shareholding between EJVCs and access seekers will, in itself, provide sufficient incentives to ensure that any costs incurred by the EJVC are efficient.

⁵ ACCC, Draft Decision, page 33.

Second, the ACCC's comments about the ability of broadcasters to pass through higher access charges in the form of higher advertising fees is not supported by any market analysis or proper assessment of whether it would, in fact, be possible for such pricing behaviour to occur.

CRA considers that it is not open to the ACCC to draw inferences about the alleged ability of broadcasters to pass higher access charges through to advertisers without any proper assessment of the state of competition in affected advertising markets.

When deciding whether a broadcaster could pass on higher access charges to advertisers, it is necessary to first undertake the task of analysing:

- specific markets within which the relevant advertising services are offered; and
- the state of competition in those markets, including the extent to which an increase in advertising would result in advertisers switching to other radio broadcasters or other advertising mediums (e.g. television).

The assessment of competition in advertising markets is a complex exercise. This has been acknowledged by the ACCC⁶ and is supported by the fact that the ACCC itself avoids adopting a "one-size-fits-all"⁷ approach to market definition and the analysis of competition in media markets.

In light of the complexities of advertising markets, CRA does not consider that it is appropriate for the ACCC to assume that higher access charges can be passed through by broadcasters in the form of higher advertising charges without any proper examination of the state of competition in the affected advertising markets.

3.4 Safeguards to ensure that costs are efficiently incurred

CRA strongly submits that it is unnecessary for the ACCC to insist on changes to the pricing principles to limit the recovery of costs by the EJVCs to those that are considered to be efficiently incurred.

However, in the event that the ACCC maintains its position that EJVCs face insufficient incentives to ensure that their costs are efficiently incurred, CRA would not necessarily object to a requirement for EJVCs to adopt the definition of efficient costs set out in the attached access undertaking.

The revised access undertaking submitted by CRA provides:

- that an EJVC may recover no more than its efficient costs; and

⁶ ACCC, *Media Mergers*, August 2006. See also, ACCC, Public Competition Assessment, *Macquarie Media Group – proposed acquisition of Southern Cross Broadcasting (Australia) Ltd and nine regional radio stations owned by Fairfax Media Limited*, 27 November 2007

⁷ ACCC, Public Competition Assessment, *Macquarie Media Group – proposed acquisition of Southern Cross Broadcasting (Australia) Ltd and nine regional radio stations owned by Fairfax Media Limited*, 27 November 2007, at paragraph 67.

- a definition of efficient costs, which is to be considered by the EJVC in setting its access charges and in any review of the access charges (or dispute arising from such a review).⁸

The practical effect of these proposed amendments is that EJVCs will face a 'price ceiling' and will ensure that access charges do not include cost elements that cannot be characterised as efficient costs.

3.5 Rights of access seekers to request reviews of the access charges

The ACCC has expressed concerns that there are no provisions in the access undertaking that allow access seekers to trigger price reviews independently of an EJVC initiated review.⁹

Given that the EJVC is responsible for the supply of digital radio multiplexing services, CRA considers that:

- the EJVC is best placed to determine the frequency and scope of any review of its access charges to take account of changes in its cost structure; and
- it will be the EJVC that will most probably initiate reviews of the access charges to ensure that they continue to reflect efficient costs.

CRA also considers that there is no tangible benefit in extending the right to initiate a review of the access charges to access seekers. In particular, CRA has significant concerns about the potential for certain access seekers to engage in 'regulatory gaming' as a means of reducing the level of access charges that are payable, notwithstanding the fact that such charges are likely to be consistent with the pricing principles.

Accordingly, CRA strongly submits that it is unnecessary for the ACCC to require a process that gives access seekers a separate right to request a review of the access charges.

However, in the event that the ACCC maintains its position that access seekers should be given a right to request a review of the access charges, CRA would not necessarily object to a requirement for EJVCs to adopt the comprehensive price review mechanism set out in the revised access undertaking provided by CRA.

CRA considers that the proposed price review mechanism in the revised access undertaking is reasonable and provides access seekers with an efficient process for requesting and participating in a review of the access charges, while simultaneously minimising the potential for 'regulatory gaming' and the administrative costs faced by EJVCs.

The key features of the price review mechanism proposed in the revised access undertaking are as follows:

- the access charges are fixed for a period of 2 years following the completion of a price review (and cannot be reviewed by other access seekers in this period);

⁸ The definition of "Efficient Costs" in clause 3.3 of schedule 2 of the revised access agreement is modelled on several examples that exist in other networked industries in Australia and overseas, and has been simplified for application to the digital radio industry.

⁹ ACCC, Draft Decision, section 8.7.

- there are two main avenues for initiating price reviews:
 - an access seeker may request a review of the initial access charges set by the EJVC and may request a further review 2 years after the completion of a review of the initial access charges or the completion of an EJVC initiated review; and
 - the EJVC may undertake a review of the access charges at any time;
- in all price reviews, the EJVC must consult with access seekers and provide sufficient information to permit access seekers to verify that the access charges are consistent with the pricing principles; and
- an access seeker may bring a dispute against the EJVC if it considers, in good faith and upon the completion of a price review, that the access charges are not consistent with the pricing principles (however, as means of limiting ‘regulatory gaming’ and the possibility of a multitude of disputes arising in respect of each price review, only a single access seeker can bring a dispute in respect of each price review undertaken – this is the first access seeker that lodges a dispute);

The key elements of the process for EJVC initiated price reviews and access seeker initiated price reviews are summarised in diagrammatic form in **Attachment A** and **Attachment B** respectively.

CRA submits that the proposed price review mechanism described above is reasonable and provides access seekers with sufficient rights to initiate a review of access charges, while providing EJVCs with a sufficient level of protection from the risk of facing multiple price review requests from one or more access seekers simultaneously.

CRA also submits that it is appropriate for access charges to be fixed for a period of 2 years following the completion of a price review. The period of 12 months proposed by the ACCC in its Draft Decision does not represent an appropriate timeframe for access seeker initiated price reviews.

3.6 Access to information to enable the independent verification of charges

The ACCC has stated in its Draft Decision that:¹⁰

- there should be a mechanism by which access seekers can verify whether the access charges are consistent with the pricing principles in the access undertaking; and
- information necessary for the access seeker to be able to verify the access charges should be made available at the same time that the EJVC introduces, changes or reviews its charges.

CRA has previously expressed the view that it would provide indicative prices once its downstream supply arrangements were finalised and all the costs associated with the supply of digital radio multiplexing services are known.

Given that there are already sufficient incentives on EJVCs to ensure that their costs are efficiently incurred, CRA considers that the provision of indicative prices would, in itself, be sufficient for access seekers.

¹⁰ ACCC, Draft Decision, page 38.

However, as the revised access undertaking has a process that allows an access seeker to request a review of the access charges and a more formalised process for disputing whether the access charges (or revisions to them) are consistent with the pricing principles, there is a reasonable argument to suggest that access seekers should, as part of these processes, be entitled to request data from EJVCs that will permit them to independently verify whether the access charges are consistent with the pricing principles.

The revised access undertaking provides a mechanism that permits an access seeker to request information from the EJVC to independently verify that the access charges are consistent with the pricing principles.

4 Other comments on the ACCC's draft decision

4.1 Variation provisions

The ACCC has identified various concerns in its Draft Decision in relation to the variation provisions of the access undertaking and access agreement.

While CRA does not agree with the ACCC's concerns for the reasons set out in CRA's previous submission, CRA would not necessarily object to the inclusion of the ACCC's requested amendments in the final version of the access undertaking and has sought to include these amendments in the revised access undertaking provided with this submission.

4.2 Consultation concerning excess multiplex capacity

CRA does not entirely agree with the ACCC's proposed amendment to clause 7.4(a) of the main body of the access agreement.

For the purpose of allocating excess-capacity access entitlements, section 118NT of the Radiocommunications Act provides for an EJVC to ascertain:

- within 90 days of the digital radio start up date for the designated BSA area, the initial level of demand for access to excess multiplex capacity¹¹; and
- at any time after the 12 month period beginning on the digital start up day for the designated BSA area, the subsequent level of demand for access to excess multiplex capacity.¹²

While the Radiocommunications Act makes it mandatory for the EJVC to ascertain the initial level of demand for excess multiplex capacity¹³, it is not mandatory for the EJVC to ascertain the subsequent level of demand for excess multiplex capacity.¹⁴ It is only when the EJVC proposes to ascertain the subsequent level of demand for excess multiplex

¹¹ Radiocommunications Act, section 118NT(2).

¹² Radiocommunications Act, section 118NT(3).

¹³ Radiocommunications Act, section 118NT(2)(a) ("*Initial level of demand for access to excess multiplex capacity must be ascertained*").

¹⁴ Radiocommunications Act, section 118NT(3)(a) ("*Subsequent level of demand for access to excess multiplex capacity may be ascertained*").

capacity (notwithstanding the fact that it is optional) that it becomes necessary for the EJVC to undertake consultation with qualifying content service providers.¹⁵

CRA submits that neither the current drafting of clause 7.4(a) of the main body of the access agreement, nor the ACCC's proposed amendments, are entirely consistent with the requirements of sections 118NT(2) and (3) of the Radiocommunications Act.

CRA has proposed amendments in the revised version of the access undertaking to ensure consistency with these provisions of the Radiocommunications Act.

4.3 Allocation of multiplex capacity to incumbent commercial broadcasters

In its Draft Decision, the ACCC has expressed concerns that the provisions governing the allocation of multiplex capacity to incumbent commercial broadcasters in the proposed access undertaking is inconsistent with the terms of the Radiocommunications Act.

In particular, the ACCC has stated:¹⁶

"The legislative framework enables individual commercial broadcasters to claim standard access entitlements of one-ninth of the multiplex capacity, but two-ninths is reserved for community broadcasters. This is not the same as the individual incumbent commercial broadcasters claiming entitlements to one-ninth of the multiplex capacity allocated to incumbent commercial broadcasters. This means that clause 6.3(b) of the Access Agreement would need to change with the removal of the words 'made available by the Multiplex Licensee to Incumbent Commercial Broadcasters'..."

CRA does not consider that clause 6.3(b) of the main body of the access agreement is inconsistent with the Radiocommunications Act.

When the access agreement is viewed in its totality, it is clear that:

- incumbent commercial broadcasters can only claim a total of seven-ninths of multiplex capacity on a multiplexer, with individual incumbent commercial broadcasters claiming one-ninth of the allocated multiplex capacity as a standard access entitlement; and
- the remaining two-ninths of multiplex capacity is reserved for digital community broadcasters (which are claimed through, and based on the allocations specified by, the Digital Community Radio Broadcasting Representative Company).

Notwithstanding the fact that CRA does not share the ACCC's concerns with respect to this clause, CRA would not object to the inclusion of the amendments to clause 6.3(b) of the main body of the access agreement requested by the ACCC in its Draft Decision.

4.4 Ability of the Representative Company to outsource

CRA agrees with the ACCC's comments in respect of clause 6.4(e) and 6.4(f) of the main body of the access agreement¹⁷ and has proposed amendments to these clauses in the revised access undertaking to address these issues.

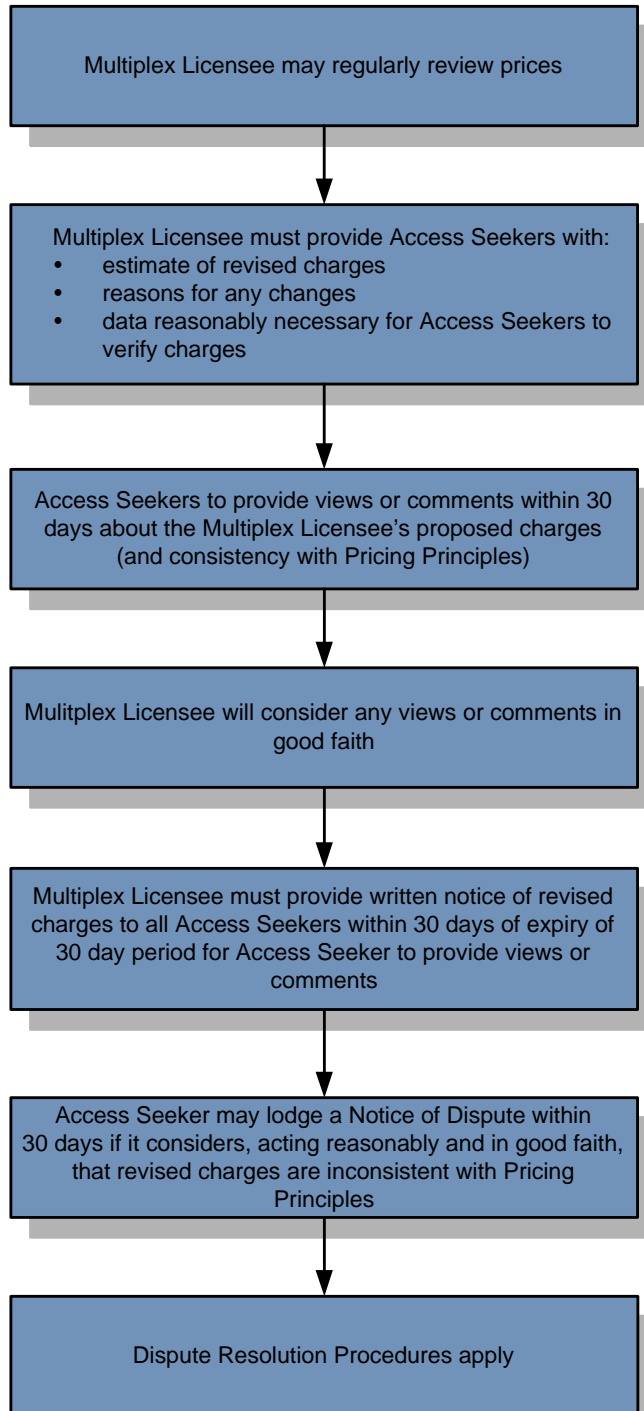
¹⁵ Radiocommunications Act, section 118NT(3)(b).

¹⁶ ACCC, Draft Decision, page 19.

¹⁷ ACCC, Draft Decision, section 7.5.

Attachment A Key elements of EJVC initiated price review process

Multiplex Licensee Initiated Reviews



Attachment B Key elements of access seeker initiated price review process

Access Seeker Initiated Reviews

