



FOXTEL MANAGEMENT PTY LIMITED

Supplementary Submission to Australian Competition
& Consumer Commission
FOXTEL Special Access Undertaking

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1. Introduction

FOXTEL Management Pty Ltd and FOXTEL Cable Television Pty Ltd (**FOXTEL**) refer to the previous submission made in support of their special access undertaking (**FOXTEL Submission**).

This is a submission in reply to the following submissions which have been made in relation to the special access undertaking (**SAU**) given by FOXTEL:

- Submission by Seven Network Limited (**Seven Submission**);
- Submission by Two Way TV Australia Limited (**TWTV Submission**); and
- Submission by Ten Network Holdings Limited (**Ten Submission**).

This submission is supported by:

- a supplementary report of Mr Henry Ergas of Charles River Associates (**CRA**) in reply to the report of Mr Houston (made on behalf of Seven);
- a supplementary report by Professor Stephen Gray in reply to the report of Professor Officer (made on behalf of Seven); and
- a FOXTEL technical report responding to the various technical issues raised in the Seven Submission and the TWTV Submission.

FOXTEL also notes that its request for access to the confidential version of the submission by Ten was refused (even if limited to legal advisers). FOXTEL submits that this should be taken into account by the Australian Competition & Consumer Commission (the **Commission**) in assessing what weight to put on that submission.

2. Market power

In section 6.5(a) of the FOXTEL Submission, FOXTEL addressed issues of market power and submitted that it did not possess market power. This submission was based in part on the report of Dr Williams and is supplemented by the witness statements of current and former subscription television executives, all of which FOXTEL has now tendered in the C7 proceedings.

2.1 Allegation of market power with no analysis of market

Both Seven and Mr Houston submit that FOXTEL has market power. For example:

- Seven submits that FOXTEL has a "*monopoly over basic pay TV packages*";¹ and
- Mr Houston opines that FOXTEL currently possesses market power in the supply of digital subscription television services.²

The fundamental problem with the allegations made by Seven and Mr Houston about FOXTEL's market power is that they have made no attempt to define the market in which FOXTEL is said to possess that power. In fact, Seven has gone further and explicitly said

¹ Seven Submission, para 4.1

² Houston Report, section 6.2.1

that the Commission should not, and does not need to, define the relevant market.³ However, without defining the market, it is not possible to consider whether a firm has market power. As the High Court has observed, "[d]efining the market and evaluating the degree of power in that market are part of the same process...".⁴

In previous submissions to the Commission, FOXTEL has also expressed the view that it is not essential for the Commission to define the market in which FOXTEL competes for the purposes of considering applications under Part XIC of the *Trade Practices Act 1974* (Cth) (the **Act**). In the present application, though, FOXTEL submits that it is necessary for the Commission to make an assessment concerning the nature and degree of competition faced by FOXTEL, and thereby effectively define the market in which FOXTEL competes (although ultimately FOXTEL submits that the undertaking is in the long-term interests of end users (**LTIE**) no matter how narrowly the market is defined).⁵

The primary reasons for this are explained in sections 8.2(a) and 8.3(a) of FOXTEL's Submission. In particular, in considering the LTIE test, the Commission must compare the likely state of the market with the undertaking compared to that without the undertaking. The counterfactual market without the undertaking is a market in which, in order to supply subscription television services, potential new subscription television providers must either:

- (a) develop their own delivery mechanism for their subscription television service; or
- (b) seek access to an existing delivery mechanism, and in the case of the FOXTEL delivery mechanism:
 - (i) rely on FOXTEL's s 87B undertaking (which expires in December 2007); or
 - (ii) seek declaration of the FOXTEL delivery mechanism and the arbitration of terms and conditions of access.

Having regard to the competitive pressures faced by FOXTEL and advancements in various technologies that enable the delivery of subscription television services, FOXTEL has submitted that there is considerable doubt whether:

- (a) entry by potential new subscription television providers is likely in any event; and
- (b) the Commission would declare any part of FOXTEL's delivery mechanism.

Those submissions are supported by lay industry evidence and expert industry and economic reports. FOXTEL has provided the Commission with a great deal of evidence about the market in which FOXTEL operates and the competitive constraints that FOXTEL faces.

There is a second reason why it is necessary for the Commission to make a proper assessment of the nature and degree of competition faced by FOXTEL. Seven's submission is underpinned by the (frequently made) assertions that FOXTEL has a "monopoly over basic pay TV packages"⁶, "faces no competition"⁷, and has a "monopoly in the supply of premium or tiered channels"⁸, and other similar assertions to the effect that

³ Seven Submission, page 3

⁴ *Queensland Wire Industries Pty Ltd v Broken Hill Pty Co Ltd* (1989) 167 CLR 177 at 187 per Mason CJ and Wilson J

⁵ FOXTEL Submission, page 60

⁶ Seven Submission, page 10

⁷ Seven Submission, page p11

⁸ Seven Submission, page 11

FOXTEL is in a monopoly position. None of these assertions are supported by any evidence, whether lay or expert.

FOXTEL rejects these assertions. FOXTEL has provided the Commission with:

- a folder of lay evidence concerning the competitive constraints it faces;
- industry expert reports from John Paul concerning media distribution mechanisms and models in Australia and from Mark Ettridge concerning subscriber management and conditional access systems; and
- an expert report of Dr Phillip Williams in relation to market definition.

FOXTEL submits that on the basis of this evidence, the Commission should conclude that FOXTEL faces substantial competitive constraint in the supply of subscription television services, and that the assertion by Seven that FOXTEL is a monopoly is unfounded.

2.2 Mr Houston's criticisms of Dr Williams' views

Further, except for vague references to market power and unsubstantiated criticisms by Mr Houston, the conclusions that Dr Williams draws about the relevant market definition do not appear to be challenged by Seven or Mr Houston.

In section 6.2.1 of his report, Mr Houston discusses FOXTEL's market power and seeks to rebut the conclusions of Dr Williams in regard to FOXTEL's lack of market power. Mr Houston states that he considers FOXTEL's audience share and its historic and expected future cash flows provide a relatively poor indication of the existence of market power.

(a) Audience share

In relation to audience share, Mr Houston asserts that many FOXTEL customers are prepared to subscribe to FOXTEL even though they watch FOXTEL infrequently. He refers to no evidence in support of his assertion. In fact, the evidence available demonstrates that Mr Houston's assertion is incorrect.

Attachment 1 is a table showing the percentage of time subscription television homes throughout Australia spent each week viewing subscription television between 6am and midnight for the period 2002 to 2006. **Attachment 2** presents this data as a graph. The data in Attachment 1 clearly shows that, since 2003, households that subscribe to subscription television spend just over half of their television viewing time watching subscription television. Contrary to Mr Houston's assertions, these households do not watch subscription television infrequently and subscription television does not "*represent only a small percentage of their total weekly television viewing*".⁹ Clearly, from the point-of-view of its subscribers, FOXTEL provides attractive and relevant programming, which they consume a significant amount of compared to their consumption of the products of the terrestrial broadcasters.

Maintaining high levels of viewing amongst subscribers is important to FOXTEL to retain subscribers. Mr Williams, FOXTEL's current Chief Executive, states in paragraph 72 of his witness statement¹⁰ that he pays close attention to the percentage of time subscription television households spend watching subscription and terrestrial television each week and that, when this figure drops below 50% (which it did in 2002), he considers strategies, such

⁹ Houston Report, para 99

¹⁰ Attachment 19, tab 11

as changes to programming and advertising, in order to combat the decline. This demonstrates the importance FOXTEL places on remaining attractive and relevant to its subscribers.

But this is only half the battle: to be successful FOXTEL needs to grow. This is where FOXTEL's audience share is important. It is a quantitative measure which approximates FOXTEL's market share. In paragraph 181 of his report and following, Dr Williams has analysed ratings data for the period 30 May 2004 to 15 January 2005. His analysis shows that during this period subscription television received 14% of total viewing time.¹¹ As Dr Williams points out, FOXTEL's share of viewing would have been less than this.¹² A comparison of the amount of time spent by subscription television households watching subscription television (around 50%) and the amount of time spent by television viewers generally (around 14% in the period 30 May 2004 to 15 January 2005) illustrates the relatively low penetration rate achieved by subscription television. The level of viewing in subscription television homes makes clear that subscription television providers are offering a product that subscribers find very attractive. However, for most Australians, it appears that subscription television is not sufficiently attractive to justify subscribing. FOXTEL submits that this is because non-subscribers consider that the television they are able to obtain from terrestrial broadcasters, videos and DVDs is sufficient to meet their demand and that the quality and price of terrestrial television, videos and DVDs is a significant constraint on FOXTEL and other subscription television providers. FOXTEL has provided the Commission with Dr Williams' report to support this position, which is based on extensive assumptions drawn from statements of current and former subscription television executives.

(b) Cash flows

On any view, FOXTEL has incurred significant negative cash flow in its ten years of operation. Dr Williams points to these losses as evidence of the competition that FOXTEL faces from its rivals in the television broadcasting market.¹³ Mr Houston responds by asserting that an analysis of cash flows does not provide any real indication of FOXTEL's market power. He then proceeds to describe market power as the ability of a firm to "*give less and charge more*".¹⁴ However, having defined market power in that way, he makes no effort to explain why, if FOXTEL has the ability to do this (as he asserts), it has suffered such large losses during its life. The obvious conclusion is that FOXTEL does not possess this ability and does not possess market power.

Mr Houston states that he views Dr Williams' analysis as going to whether FOXTEL, with the benefit of hindsight, would elect to make the same investments again, having faced the losses it has. While Dr Williams' analysis can be used for that purpose, that is not the only use of the analysis and the conclusions that Dr Williams draws from his analysis are valid ones. FOXTEL's cash flows are indicative of its inability to price as it chooses and its absence of market power. Mr Houston's reference in paragraph 37 of his report to FOXTEL posting an operating profit after interest and tax in the first week of January 2006 is not to the point.

¹¹ Para 186

¹² Para 187

¹³ Para 207

¹⁴ Houston Report, para 101

Mr Houston criticises Dr Williams for only considering FOXTEL's cash flows to 2012 and opines that this is "*an inadequate time-horizon*" to consider FOXTEL's return on its investments.¹⁵ However, Mr Houston does not explain what an adequate time period would be to assess FOXTEL's cash flows and his criticisms do not affect the assistance provided by Dr Williams' analysis in determining whether FOXTEL has the ability to "*give less and charge more*".

(c) Price reductions and quality increases

Mr Houston opines that the best way of considering whether FOXTEL has market power is to consider whether it would be reasonable to expect FOXTEL to reduce its price or seek to improve the quality of its product in response to new entry. In his supplementary submission, Mr Ergas explains why the test for market power proposed by Mr Houston is defective.

Despite the defects in the test proposed by Mr Houston, the evidence FOXTEL has provided to the Commission in the form of Dr Williams' report and the statements of current and former subscription television executives, demonstrates that FOXTEL is constantly seeking to adjust the price/service quality package it offers the public, to make its service as affordable as possible and to increase the quality of its service. This is because FOXTEL is seeking to grow its subscriber base and increase its share of viewing, in circumstances where it faces significant competition from, amongst others, the incumbent and profitable terrestrial broadcasters. For example:

- FOXTEL is constantly seeking to produce or acquire programming which will increase the attractiveness of its service. The creation and launch of the *Crime & Investigation Network* channel in 2005, the acquisition of the *Playhouse Disney* channel in 2005 and the production of *Love My Way* are all examples of how FOXTEL is continually seeking to offer subscribers greater choice and acquire or create the best content it can.
- FOXTEL developed and launched its digital product, FOXTEL Digital, for a number of reasons including to respond to the introduction of digital television by the terrestrial broadcasters and to improve significantly its product by providing greater value, choice and convenience to subscribers in order to drive interest amongst consumers and attract subscriptions and revenue.¹⁶
- In making pricing decisions, FOXTEL's current Chief Executive, Mr Williams, states that he has regard to the fact that the terrestrial broadcasters provide a "free" service and to the prices charged for video and DVD rental and purchase.¹⁷ This is consistent with the approach of one of FOXTEL's former Chief Executives, Mr Mockridge, who was also conscious of what consumers were prepared to pay for FOXTEL, given they could access the terrestrial broadcasters for free.¹⁸ Mr Mockridge considered that the main constraint on FOXTEL's pricing was that, if its

¹⁵ Houston Report, para 100

¹⁶ Statement of Mr Williams, paragraphs 171 to 178; statement of Mr Delany, paragraphs 146 to 150

¹⁷ Statement of Mr Williams, paragraph 182

¹⁸ Statement of Mr Mockridge, paragraphs 34 and 36

prices increased, subscribers would simply revert to the terrestrial broadcasters as their primary source of television entertainment.¹⁹

- FOXTEL also refers to **Confidential Attachment 3**.

None of this evidence is referred to by Mr Houston. Indeed, Mr Houston refers to no evidence at all (nor any factual assumptions that he has been given) when he asserts that, in his opinion, "*there is sufficient reason to believe that, if entry were to occur as a result of CA/SI unbundling, FOXTEL would reduce its prices and may be forced to alter its fundamental programming subscription choices*".²⁰ FOXTEL submits that the Commission should reject assertions of that kind which are unsupported by evidence.

3. Appropriate counterfactual

In considering the reasonableness of the terms and conditions of the undertaking, the Commission must compare those undertakings with an appropriate counterfactual.

Seven asserts that the counterfactuals against which FOXTEL purports to assess the LTIE assume that FOXTEL "*submits alternative SAUs*".²¹ Contrary to Seven's suggestion, FOXTEL does not suggest that it would lodge alternative SAUs; rather, that the SAU it has lodged is 'reasonable' (the statutory test) compared to any possible counterfactual.

Seven asserts that the appropriate counterfactual involves access seekers relying on FOXTEL's s 87B undertaking or seeking declaration of FOXTEL's service "*determined by the access seeker*".²² FOXTEL adopted this general statement of the counterfactual in its submission.²³ However, the general statement is not a complete statement of the counterfactual for three reasons. First, the counterfactual must also contemplate the prospect that potential new subscription television providers may develop their own delivery mechanism for their subscription television service or may seek access to an existing delivery mechanism other than FOXTEL's. Secondly, the counterfactual must contemplate the prospect that the Commission would decide not to declare the FOXTEL service, for the reasons explained by FOXTEL in its first submission.²⁴ Seven's submission that the appropriate counterfactual should be declaration presupposes that declaration of this service would be in the LTIE. FOXTEL submits that this assumption cannot be made with any degree of certainty, particularly given the increasing avenues for the delivery of subscription television content²⁵ and the potential impact of declaration on investment. Thirdly, assuming that the potential new subscription television provider seeks access to part or all of FOXTEL's delivery mechanism, and assuming declaration, the general statement fails to articulate with any precision the terms and conditions on which access to

¹⁹ Statement of Mr Mockridge, paragraphs 34 and 36

²⁰ Houston Report, para 103

²¹ Seven Submission, page 1

²² Seven Submission, pages 1, 7

²³ FOXTEL Submission, page 56

²⁴ FOXTEL Submission, pages 56 – 57

²⁵ See Attachment 18 to FOXTEL's Submission, "*Identification of Media Distribution Mechanisms and Models in Australia*", John Paul, ACPG Pty Ltd. In addition, since that report was prepared, BigPond Movies has launched; Reeltime has published a prospectus and announced a video on demand (**VOD**) service expected to commence in July 2006; and Anytime has announced a VOD service in partnership with Regional Internet Australia.

FOXTEL's services would be given in the counterfactual world, and therefore makes any comparison of the reasonableness of the SAU with the counterfactual impossible.

Seven also asserts that there are four relevant differences between the factual (access pursuant to the SAU) and the counterfactual.²⁶ Apart from the alleged "tie", the differences referred to by Seven are matters of semantics only. They are minor differences resulting from the slightly different legislative scheme involving an undertaking as opposed to declaration and arbitration. If the concerns identified by Seven were material, it would lead to the conclusion that the Commission should never accept an access undertaking, as declaration and arbitration would always be preferable. Plainly, Parliament empowered the Commission to consider access undertakings in accordance with the provisions of Division 5 of Part XIC, and the fact that there may be minor differences in the considerations applicable to declaration and arbitration is either irrelevant or immaterial to the Commission's task under Division 5.

Of more significance are Seven's dual assertions that:

- (a) in the event of declaration of the FOXTEL service, it is highly unlikely that it would include a "tie" to FOXTEL's subscribers; and
- (b) FOXTEL must abide by the SAOs under s 152AR of the Act in relation to the FOXTEL digital pay TV service that is declared.²⁷

Each of those assertions is considered in the next section. Even if the service was declared, FOXTEL submits that this declaration would not be 'determined by the access seeker' as asserted by Seven,²⁸ but determined by the Commission having regard to the statutory criteria. FOXTEL submits that for the reasons set out in section 5 below, this declaration could not include provision of an unbundled CA/SI service or provision by FOXTEL of STUs in non-FOXTEL homes. Further, for the reasons set out in the FOXTEL Submission and also discussed in section 5 below, FOXTEL submits that the Commission would not determine terms and conditions of access that included a requirement to supply an unbundled CA/SI service or provision by FOXTEL of STUs in non-FOXTEL homes because such terms would not be reasonable.

Finally, Seven contends that FOXTEL has wrongly placed reliance on the potential counterfactuals referred to as options D and E in the Ergas Report.²⁹ For the reasons explained in the next section, FOXTEL submits that even if the FOXTEL STU services were declared under Part XIC, FOXTEL would not be required to supply any or all of those services in non-FOXTEL subscriber homes. Nevertheless, FOXTEL has examined options D and E on the hypothesis that FOXTEL could be required to supply the services in non-FOXTEL subscriber homes and on the basis contemplated by those options, in order to demonstrate that it would not be reasonable to require FOXTEL to supply services on those terms. If one ignores the limits of Part XIC (which are described in detail in the next section), then options D and E constitute legitimate counterfactuals to consider, assuming declaration of the FOXTEL STU service. Following declaration and assuming a dispute about access to the FOXTEL STU service, the Commission must arbitrate the dispute applying the criteria in s 152CR. Whether the Commission would determine that FOXTEL

²⁶ Seven Submission, pages 7,8

²⁷ Seven Submission pages 7

²⁸ Seven Submission, page 1

²⁹ Seven Submission page 5

should be required to supply any part or all of its STU services in non-FOXTEL subscriber homes would need to be assessed by the Commission in that counterfactual world.

Seven's contention that FOXTEL has wrongly placed reliance on the potential counterfactuals referred to as options D and E in the Ergas Report is noteworthy. Although Seven's submission that the SAU is not reasonable is necessarily underpinned by a view that preferable alternative terms and conditions of access would be available under Part XIC (the counterfactual), nowhere does Seven articulate what those alternative terms and conditions would be. It appears that Seven has chosen to be deliberately silent on specifying its preferred counterfactual. Although Seven has submitted a report by Mr Houston that examines a counterfactual based on Option D³⁰, in its submission Seven appears to want to distance itself from that counterfactual option. The failure to state a precise counterfactual, or even alternative counterfactuals, undermines Seven's submission, as the criticisms made by Seven are unable to be tested by reference to available alternatives and therefore lack foundation.

4. Regulatory framework

4.1 SAU to be "consistent" with SAOs

Seven submits that in assessing whether FOXTEL's undertaking is "consistent with" the SAOs this is not necessarily synonymous with "not inconsistent with".³¹ FOXTEL submits that this interpretation of section 152CBD is incorrect.

Section 152CBD stipulates that that Commission must be satisfied that the terms and conditions of the SAU are "consistent with" the SAOs. However, the Act does not provide any detail regarding what this entails. In its Final Decision on Optus' undertaking with respect to the supply of its Domestic GSM Terminating Access Service released in February 2006 (the **Optus Decision**), the Commission stated that it adopts the following approach to determining whether an undertaking is consistent with the SAOs (emphasis added):³²

- identify those SAOs that are applicable to a particular access provider; and
- assess whether the proposed undertaking is consistent with the applicable SAOs. This assessment may involve consideration of whether the terms and conditions raise any inconsistencies with the applicable SAOs. *If the terms and conditions are not found to be inconsistent with the SAOs, the Commission is likely to regard the undertaking as being consistent with the applicable SAOs.*

The Commission then went on to elaborate that its view is that the meaning of "consistent with" is that there is *"some uniformity and adherence... but... there is no requirement for exact or complete correspondence."* In outlining how it would apply this view of the meaning of consistency to the question of whether an undertaking met the requirements of the Act, the Commission stated that it does not require that the terms of an undertaking *"be precisely in accordance with the applicable SAOs"*.³³

³⁰ For the reasons explained in section 6.1 below and in the supplementary report of Mr Ergas, Mr Houston has also failed to properly articulate the counterfactual he is proposing based on Option D.

³¹ Seven Submission, page 2

³² Optus Decision, page 182.

³³ Optus Decision, page 182.

This approach to the meaning of "consistent with" is not new to the Commission. As already outlined by FOXTEL in its Submission,³⁴ it is the view that has been taken by the Commission in its analysis of the consistency of the terms and conditions of undertaking with the SAOs on many previous occasions.³⁵ FOXTEL submits that the Commission should not change its view on the meaning of "consistent with" and should thus consider whether the terms of the SAU are either expressly or impliedly *inconsistent* with the SAOs. FOXTEL submits that for the reasons set out below, its SAU is consistent with the SAOs.

4.2 Promotion of competition

In its submission, Seven draws on the decision of the Australian Competition Tribunal (the *Tribunal*) in *Sydney Airports*³⁶ to assert that the requirement in the access regime contained in Part IIIA that there be a promotion of competition as a result of a declaration does not mean there must be an increase in the level of competition.³⁷ FOXTEL submits that this is incorrect and that it does not reflect the intention of the legislature or of the Tribunal.

Indeed, in the proposed amendments to Part IIIA of the Act contained in the Trade Practices Amendment (National Access Regime) Bill 2005, it is proposed that when considering the declaration of a service, the criteria be changed so that the promotion of a **material increase** in competition is necessary.³⁸ According to the Explanatory Memorandum accompanying this Bill, the addition of the phrase 'material increase' is designed to ensure that declarations are only sought where increases in competition are not trivial.³⁹

The Commission has recently stated that "[t]he issue is whether access would improve the opportunities and environment for competition such that competitive outcomes are more likely" (emphasis added) and that "there must be some *"practical effect"* on the level of competition that is brought about by a declaration before it can be considered to promote competition."⁴⁰ Similarly, the Tribunal has confirmed that the likelihood of promotion of competition must not be trivial and that "there must be some real prospect of entry into the dependent market within a reasonable time for competition to be promoted".⁴¹

³⁴ FOXTEL Management Pty Limited, Submission to the Australian Competition and Consumer Commission: FOXTEL Special Access Undertaking, pages 10 to 11.

³⁵ A Report on the Assessment of Telstra's Undertaking for the Domestic PSTN Originating and Terminating Access Services, July 2000 pages 15-16; Assessment of Telstra's Core Services Undertakings – Preliminary View, 12 December 2003 page 16; A Final Report on the Assessment of Telstra's Undertaking for the Line Sharing Service, August 2004 page 21; Assessment of Telstra's Undertakings for PSTN, ULLS and LCS Final Decision, December 2004 page 23; A report on the assessment of the Analogue Pay TV Access Undertaking proffered by FOXTEL Management Pty Ltd December 2003, Confidential Version page 11.

³⁶ *Re Sydney Airports Corporation Ltd* (2000) FLR 10.

³⁷ Seven Submission, pages 3-4; Houston Report pages 10-11

³⁸ Paragraph 44G(2)(a).

³⁹ Explanatory Memorandum, page 21.

⁴⁰ Final Recommendation, Lakes R Us application for declaration of water storage and transport services, 10 November 2005, paras 6.1, 6.45

⁴¹ *Re Application by Services Sydney Pty Limited* [2005] ACompT 7 (21 December 2005), paras 132-136

In any case, Mr Houston has misrepresented the position of Dr Williams:⁴² Dr Williams adopts the correct test, the "with or without test". This test is not inconsistent with *Sydney Airports*; rather, it simply sets out the way in which a 'promotion of competition' must be assessed. Indeed, it has recently been affirmed by the Tribunal.⁴³

Further, one of the other stated purposes of the telecommunications access regime in Part XIC of the Act is 'encouraging the economically efficient use of, ... and investment in ... infrastructure'⁴⁴. Section 152AB has now been amended to provide that in assessing the LTIE criteria relating to investment matters, "regard must be had to the risks involved in making the investment": s 152AB(7A). In addition, the Environment, Communications, Information Technology and the Arts Reference Committee released a report on 10 August 2005 entitled 'The Performance of the Australian Telecommunications Regulatory Regime' in which it recommended, amongst other things, that 'the ... objective of ... encouraging the economically efficient use of, ... and investment in infrastructure – *be given primacy*.'

FOXTEL therefore submits that the Commission must pay careful attention to the risks (including financial, operational and technical) inherent in FOXTEL's investment in the digital service. Potential investors will monitor closely the terms and conditions of access to FOXTEL's infrastructure prior to deciding whether to make a similar outlay. Furthermore, although FOXTEL has already invested in the infrastructure needed to provide the relevant service, it still requires certainty about the terms and conditions of access to that service, to enable it to assess further investment and the impact on its own internal operations.

4.3 Arbitration v Undertaking

In the description of the benefits that would accrue as a result of rejecting the SAU, Seven includes the ability for access seekers to refer a dispute to arbitration by the Commission.⁴⁵

This assertion misunderstands the underlying structure of Part XIC, which provides several options for determining conditions of access. Indeed, the Explanatory Memorandum to the Trade Practices Amendment (Telecommunications) Bill 1996 which inserted Part XIC into the Act states:

The Part enables the terms and conditions of access to be determined by any one, or a combination of, three methods - commercial negotiation, an undertaking submitted by individual carriers or carriage service providers who are under an access obligation and which has been accepted by the ACCC, or under arbitration by the ACCC.

This is reflected in s 152AY which sets out the various methods of complying with the standard access obligations. In that section, arbitration of disputes about access is listed as an option in the case that 'there is no ... undertaking'.⁴⁶

Arbitration is therefore but one avenue through which competition may be promoted (indeed, it is seen as a last resort). As the Act recognises, the submission of an undertaking is another. If potential arbitration by the Commission was considered to be a benefit in the sense described by Seven, then no undertakings would ever be accepted.

⁴² Houston Report, paras 18-19

⁴³ *Re Application by Services Sydney Pty Limited* [2005] ACompT 7, para 139

⁴⁴ s 152AB(2)(c),(e).

⁴⁵ Seven Submission, page 7

⁴⁶ s 152AY(b)(iii)

In fact, the process of allowing access providers to submit access undertakings is preferable to the alternative of undergoing arbitration to resolve access disputes. There are a number of serious disadvantages with the process of arbitration under Part XIC of the Act. It is an adversarial and lengthy process which can be extremely harmful to business relationships. Its high cost is a further burden on the parties and these financial pressures may mean that the most desirable outcome is not achieved.

In the light of the limitations of the process of arbitration, the advantages of the possibility of submitting an undertaking become more significant. One of the benefits of an undertaking is the fact that it deals with the terms of access for all potential access seekers, rather than just one as is the case in an arbitration.

As noted in the Explanatory Memorandum to the Telecommunications Competition Bill 2002 (Cth), 's152CLA... recognise[s] that the Commission should generally give priority to the consideration of undertakings in preference to arbitrations.' This is achieved by allowing the Commission to temporarily cease consideration of an access dispute if it receives an access undertaking which relates in any part to the matter in contention. Thus, it can be said that submitting an access undertaking will ensure greater certainty for both the access seeker and access provider, relative to the process of engaging in an access dispute and related arbitration.

5. Consistency with SAOs

Under the undertaking, FOXTEL undertakes to provide Digital Set Top Unit Services to an access seeker where the particular STU is being used by a FOXTEL subscriber. This limitation is described in section 6 of the FOXTEL Submission.

Seven describes this limitation as a "tie" and submits that the tie is not consistent with the SAOs.⁴⁷ Seven's submission fails to state the requirements of s 152CBA accurately, and fails to appreciate the particular application of ss 152AL and 152AR to the services supplied by FOXTEL. In particular, Seven's submission fails to appreciate the differences in the nature and characteristics of the services supplied by FOXTEL compared with other carriers or carriage service providers (such as Telstra).

FOXTEL submits that the restriction is a proper delimitation of the extent of the Digital Set Top Unit Service supplied by FOXTEL and is consistent with the obligations referred to in paragraph 152CBA(3)(a).

Under s 152CBD, the Commission must not accept the undertaking unless it is satisfied that the terms and conditions specified in the undertaking "*would be consistent with the obligations referred to in paragraph 152CBA(3)(a)*". The obligations referred to in paragraph 152CBA(3)(a) are not merely "*the SAOs*" as assumed by Seven. Instead, those obligations have two important and related conditions or limitations:

- (a) first, the obligations apply only if the carriage service provider supplies the service to itself or to other persons; and
- (b) secondly, in that event, the carriage service provider must comply with the SAOs (the obligations referred to in s 152AR) to the extent that those obligations would apply to the person in relation to the service if the service were treated as an active declared service.

⁴⁷ Seven Submission, page 8

The reason for these limitations is clear. The purpose of the provision is to require the carriage service provider to comply with the SAOs in relation to the service the subject of the undertaking:

- (a) as if the service was declared under s 152AL; and
- (b) only if the declared service is actually being supplied by the carriage service provider.

This reflects the same limitations contained in s 152AR: the SAOs only apply if the carriage service provider supplies a declared service to itself or to other persons (the supplied services being called active declared services), and only in respect of the active declared services.

FOXTEL submits that it is clear from the terms of ss 152AL and 152AR that the listed carriage services and facilitating services that it supplies as a carriage service provider are locationally confined to FOXTEL subscriber homes. To contend that FOXTEL's services can be defined without reference to any locational limitation is to ignore the requirements of Part XIC and the provisions of the *Telecommunications Act 1997 (Cth)* (the ***Telecommunications Act***) which are incorporated into Part XIC.

Under s 152AL, the Commission may declare that a specified eligible service is a "declared service". An "eligible service" is defined as:

- (a) a listed carriage service (within the meaning of the Telecommunications Act); or
- (b) a service that facilitates the supply of a listed carriage service (within the meaning of that Act),

where the service is supplied, or is capable of being supplied, by a carrier or a carriage service provider (whether to itself or to other persons). The expression "carriage service provider" also has the meaning given in the Telecommunications Act. The relevant definitions in the Telecommunications Act are significant:

- A carriage service provider is a person who supplies, or proposes to supply, a listed carriage service to the public using a network unit (s88 of the Telecommunications Act).
- A carriage service is a service for carrying communications by means of guided and or unguided electromagnetic energy (s7 of the Telecommunications Act).
- A listed carriage service is a carriage service between a point in Australia and one or more other points in Australia (s16 of the Telecommunications Act).
- A network unit is a line link that connects two distinct places in Australia, or a radiocommunications facility (whether using satellite or otherwise) used to supply a carriage service between different points in Australia (Division 2 of Part 2 of the Telecommunications Act).
- A carriage service is supplied to the public if it is supplied an end user (not being the supplier) (s88 of the Telecommunications Act).

The identification of the geographic points to which or between which the carriage service is supplied is therefore essential to the definition of a "listed carriage service" and "carriage service provider". This is for an obvious reason. It would be nonsensical to suggest that a listed carriage service existed, and that a carriage service provider supplied or proposed to

supply a listed carriage service, to points or between points where there was no relevant facilities in place to enable that carriage.

The limitations inherent in the definitions of “listed carriage service” and “carriage service provider” have a special significance in relation to FOXTEL’s business. This is apparent from the reasoning of the Full Federal Court in *FOXTEL v Seven Cable Television* (2000) 102 FCR 555. In that case, the Court concluded that FOXTEL was a carriage service provider. Although FOXTEL was not the owner of network units for the delivery of its signals to subscribers, it was nevertheless a carriage service provider, and supplied listed carriage services, because it entered into contracts with subscribers to deliver programs to the subscribers, and pursuant to those contracts it:

- (a) installed and maintained equipment within the subscriber’s home (cable and STU); and
- (b) made arrangements with carriers such as Telstra to enable the relevant signal to be transmitted to the subscriber’s home.

Having regard to the foregoing, the Full Federal Court concluded that (at pages 575-6):

*“In our opinion, it follows that service in the relevant sense includes the commercial arrangements by which the service provider can use the network unit **and the commercial arrangements by which the service is provided to and received by the customer.** The access, which is the end point of the legislative chain, needs to be to a “service” which **reaches the customer.**”* (emphasis added)

The Court also observed that (at page 576):

*“...[the] carriage service is best seen in this case as the **bundled commercial service which carries the communication to the receiver.**”* (emphasis added)

As found by the Full Federal Court, FOXTEL is only a carriage service provider, and only supplies a listed carriage service, by reason of entering into commercial arrangements with its customers and installing the relevant cabling and STU in a customer’s premises. Any location which has not entered into a commercial arrangement with FOXTEL for receipt of FOXTEL’s programs and which does not have relevant cabling and an STU installed, is not a “point” to which FOXTEL supplies a listed carriage service. For that reason, FOXTEL’s business is distinct from most other carriers and carriage service providers. The listed carriage services supplied or able to be supplied by carriers and most carriage service providers is defined by the scope of the network units they own or use through commercial arrangements, and the points reached by those network units. In the case of FOXTEL’s business, it is also defined by the existence of contractual arrangements with subscribers and the installation of cabling and STUs.

Section 152AL empowers the Commission to declare an eligible service that is being supplied or is capable of being supplied. Accordingly, the declaration process is not confined to eligible services that are actually being supplied at the time of declaration. Nevertheless, the meaning of the expression “capable of being supplied” in the context of FOXTEL’s service raises a particular difficulty. It is highly likely that the service is not capable of being supplied to locations that do not have cabling and an STU installed.

Furthermore, s 152AR is confined to declared services that are actually being supplied. It can be seen that s 154AR(2) defines “active declared services” as the declared services

actually being supplied by the carriage service provider, whether to itself or to other persons.

For the reasons explained by the Full Federal Court, the listed carriage service supplied by FOXTEL (as a carriage service provider) is *“the bundled commercial service which carries the communication to the receiver”* (ie the STU and the television in the subscriber’s home). FOXTEL is not a supplier of listed carriage services, and there can be no “active declared service”, in respect of locations (or points) where it has not entered into commercial arrangements with a subscriber and has not installed cabling and an STU at the subscriber’s premises.

FOXTEL submits that under Part XIC, an access seeker is not entitled to require FOXTEL to extend the geographic reach of the service actually supplied by it from time to time. This is plain from s 152AR, which proceeds upon the clear assumption that the service to which access is given exists and is capable of being supplied by the access provider immediately to itself or to access seekers (see in particular s 152AR(2), (3) and (8)). Seven advances the proposition *“... if FOXTEL supplied the declared Digital Set Top Unit Service only to an access seeker, the Digital Set Top Unit Service still would be an active declared service.”*⁴⁸ While the proposition is strictly correct, it is simply an exercise in circularity. If FOXTEL commenced the supply of the declared Digital Set Top Unit Service to an access seeker in non-FOXTEL subscriber homes, undoubtedly FOXTEL would be supplying an active declared service to those homes. However, the relevant question is: if FOXTEL is not supplying the declared Digital Set Top Unit Service in a particular location, is the supply of the service to that location an “active declared service” for the purposes of s 152AR(2), and is FOXTEL required to supply such a service to an access seeker? For the reasons explained above, FOXTEL submits that the answer is plainly no.

Seven also contends that s 152AR(8) contemplates the need to provide CA and SI services to other persons, even where FOXTEL no longer supplies the end user itself.⁴⁹ This is plainly incorrect. Section 152AR(8) is premised on the access provider supplying an active declared service. In respect of non-FOXTEL homes, this premise is not satisfied. Further, the obligation imposed on the access provider under s 152AR(8) is to provide necessary services to enable the service provider to supply carriage services and/or content services *“by means of the active declared service”*. If the active declared service is not being supplied by FOXTEL, the obligation cannot arise.

For the above reasons, FOXTEL submits that the limitation contained in the terms and conditions of the undertaking to the effect that FOXTEL undertakes to provide Digital Set Top Unit Services to an access seeker only where the particular STU is being used by a FOXTEL subscriber is consistent with the obligations referred to in paragraph 152CBA(3)(a).

⁴⁸ Seven Submission, page 9

⁴⁹ Seven Submission, page 9

6. The tie is not in the LTIE

6.1 Introduction

Seven and Ten assert that the "tie" of the service with FOXTEL's basic package is not reasonable as it is not in the LTIE.⁵⁰

That assertion is necessarily underpinned by various assumptions about the counterfactual to the SAU. The difficulty in responding to the submissions of Seven and Ten lies in the fact that neither of them fully and clearly state the counterfactual with which they are comparing the reasonableness of the SAU. The criticisms of the SAU that are made in their submissions assume the existence of a preferable counterfactual world (preferable in the sense of better promoting competition and efficiency), but the assumptions they make about the counterfactual world are impossible to test or critique because they remain unstated.

For the purposes of examining the reasonableness of the SAU, FOXTEL identified and articulated various possible counterfactuals, and provided substantive evidence to enable the Commission to assess the reasonableness of the SAU in light of the counterfactuals. The two primary counterfactuals were articulated in the report of Mr Ergas and referred to as Options D and E. Neither Seven nor Ten have proposed other potential counterfactuals.

While the Seven Submission fails to specify its assumed preferable counterfactual, it has lodged a report by Mr Houston which purports to assess the reasonableness of the SAU in comparison to Option D. When comparing the SAU to a counterfactual based on Option D, it is important to note that that counterfactual assumes the following:

- (a) the FOXTEL service is declared;
- (b) there is the reasonable prospect of new entry from a person who is able to offer a subscription television service which is viable on a stand-alone basis (ie that would be attractive to customers as a substitute to the FOXTEL service, and not as a complement to the FOXTEL service); and
- (c) FOXTEL could be and would be required under Part XIC to provide CA/SI services unbundled from STUs.

In relation to assumption (a), for the reasons already stated in section 3 above, declaration is uncertain.

In relation to assumption (b), for the reasons explored in section 6.2 below, FOXTEL submits that it is highly unlikely that there will be a new subscription television entrant in the medium term that is viable on a stand-alone basis. Even if such a new entrant emerged, FOXTEL submits that competition and efficiency are better promoted by the SAU than the Option D counterfactual.

In relation to assumption (c), for the reasons explored in section 5 above, FOXTEL submits that even if the service were declared, the Commission could not require the CA/SI service to be unbundled from FOXTEL's STUs and supplied to access seekers. Further, for the reasons explored in section 6.4(c) below, FOXTEL submits that if the service were declared, it would not be reasonable or in the LTIE for the Commission to require that the CA/SI service be unbundled from FOXTEL's STUs and supplied to access seekers.

⁵⁰ Seven Submission, section 4; Ten Submission, para 7

As noted earlier and explained in more detail in the supplementary report of Mr Ergas, the precise counterfactual being assumed by Mr Houston is ambiguous in many respects. The supplementary report of Mr Ergas identifies and examines those ambiguities to demonstrate that the conclusions reached by Mr Houston are flawed. This section of FOXTEL's submission also replies to various factual issues that are raised by Mr Houston's report (and to some extent the submissions of Seven and Ten). FOXTEL submits that in many important respects Mr Houston ignores (or was not provided with) the available evidence concerning the Australian subscription television industry and that the conclusions that Mr Houston reaches are not only unsupported but contradicted by this evidence.

FOXTEL submits that the critical question for the Commission in considering whether the SAU is reasonable is whether there is a counterfactual that is real, achievable and to be preferred in the LTIE. FOXTEL submits that on the evidence before it, the Commission should be satisfied that there is no such counterfactual.

In section 6 of its first submission, FOXTEL described the significant costs and inefficiencies that would be imposed on FOXTEL if access was to be provided to FOXTEL's services on the basis of the counterfactual Options D or E. Those submissions are not repeated in this submission, but FOXTEL reiterates that those costs and inefficiencies should be weighed heavily by the Commission in its consideration of the reasonableness of the conditions of the SAU.

6.2 Likelihood of new entry

Neither Seven nor Mr Houston have provided any analysis or evidence about the type of service a potential new subscription television provider would be able to supply on a stand-alone basis in Australia.⁵¹ As discussed above, it is necessary under the "promotion of competition test" for there at least to be some possibility of new entry or increased competition.

FOXTEL submits that there are two broad types of potential new subscription television providers:

- (a) a provider of a small range of niche programs; and
- (b) a provider of a diverse range of programs which would be considered as a substitute to FOXTEL's product.

The commercial factors concerning the provision of each type of service in Australia are entirely different.

In FOXTEL's view it is extremely unlikely that a potential new subscription television provider will be able to supply a service that is considered by consumers to be both a substitute for FOXTEL's basic service as well as a service that appeals to FOXTEL subscribers.

If an access seeker is able to offer a service to compete with the FOXTEL basic package, it is therefore likely to have similar content and it is unlikely that a consumer would have any

⁵¹ Mr Houston relies on the anti-siphoning legislation in Australia to suggest that there may be greater scope in Australia for entry by broadcasters seeking to compete with FOXTEL. However, FOXTEL does not see how this assists Mr Houston's argument as the anti-siphoning legislation prevents any subscription television operators, including new entrants, from procuring access to certain sports rights unless a terrestrial broadcaster has acquired the rights. This legislation therefore does not appear to assist access seekers any more than FOXTEL.

interest in subscribing to both services. In that case, there is no reason why the access seeker could not provide its own delivery mechanism for its service. It would be in a position to acquire a conditional access system and STUs which best met its business needs. There is no reason to suppose that the costs of its doing so would be greater than the costs of acquiring those services from FOXTEL. Each of Optus, Austar, TransACT and Neighbourhood Cable provide their own CA/SI and STU services. It is clear that the cost of those services is not a barrier to entry. Mr Houston's argument that using incompatible STU constitutes a barrier to entry is considered in the following section.

On the other hand, if the access seeker simply chose to offer one or a small group of niche channels, it is unlikely that that service would be viable as a stand alone service or that many subscribers would take it even if it were. The service is unlikely to be viable because the total costs associated with acquiring a customer and installing, servicing and disconnecting an STU (including the capital cost of the STU itself) would have to be recovered from the sale of one or a small number of channels. The acquisition of a customer and associated churn is one of very large costs any subscription television operator must bear. It is unlikely that those costs could be recovered from the sale of one or a limited number of channels. The acquisition costs for each new cable and satellite subscriber is set out in **Confidential Attachment 4**.

Moreover, FOXTEL believes that the service is unlikely to be attractive to a significant number of consumers. In FOXTEL's experience, what is necessary to attract significant numbers of consumers to a subscription television service and to ensure that they remain subscribers is to offer an extensive range of programming. Programming of a particular type may have appeal to a limited number of consumers and that appeal may be sufficiently great in some cases for the consumer to be willing to take that service and that service alone. However, in most cases, what attracts a significant number of consumers to a pay television service is the amount of choice that service offers.

Accordingly, a potential provider of niche programs is likely to want to access FOXTEL's customer base, as its programs will be complementary to the FOXTEL service. This is facilitated by the SAU and competition and efficiency are not improved by any plausible counterfactual.

6.3 Barriers to entry

Mr Houston asserts that the critical entry barrier for a person who wishes to provide a subscription television service that is substitutable to the FOXTEL service is the reluctance of consumers to purchase an incompatible technology.⁵² He states that customers subscribing to a potential alternative subscription television service (the access seeker's service) will "most likely want the option of also receiving FOXTEL programming at some point in the future" and not having that option represents an entry barrier because:

- if a new customer subsequently wants FOXTEL, the customer will be reluctant to switch or buy a second STU for reasons of cost and convenience; and
- it reduces switching costs for existing FOXTEL customers.

FOXTEL disagrees with these assertions. They are based on various assumptions about practices in the Australian subscription television industry that are contrary to known facts. The source for Mr Houston's false assumptions is unstated.

⁵² Houston Report, para 104.

The supplementary report of Mr Ergas also examines this aspect of Mr Houston's report and concludes that Mr Houston has failed to justify the conclusions he has reached.

(a) FOXTEL's business model not a barrier

FOXTEL submits that its business model, under which consumers do not have to purchase an STU, removes any potential barrier to entry associated with incompatible STU and is pro-competitive. Switching to FOXTEL involves only a negligible cost to the subscriber as they do not have to purchase an STU but pay a minimal amount (if any) for installation. FOXTEL now routinely offers discount installation on most start-up packs (on fixed-term contracts with direct debit payment). FOXTEL submits that this potential cost is unlikely to be a significant deterrent for subscribers wishing to avail themselves of a new entrant's service.

If the new entrant adopted the same business model as FOXTEL, then switching between the two providers would impose no significant cost at all.

However, Mr Houston appears to assume that a new entrant would adopt a different business model to FOXTEL, and would sell and not subsidise the cost of STUs. Even if such a model were to be adopted by a new entrant, it is not apparent that there would be a barrier to entry. A person who subscribes to the new entrant's product would be able to switch to the FOXTEL service at very little cost (because FOXTEL subsidises its STUs). To the extent that a person is deterred from subscribing to the new entrant's service by reason of purchasing an incompatible STU, that is a result of the new entrant's chosen business model, not FOXTEL's business model. It would be perverse to require FOXTEL to offer unbundled CA/SI services to an access seeker, with all the associated costs and inefficiencies, to address a perceived barrier to entry created by the new entrant's chosen business model.

Mr Houston does not explain why he has assumed that a new entrant would wish to sell STUs, imposing an upfront cost on subscribers. As Mr Houston points out himself, all subscription TV providers in Australia (Optus, Austar, TransACT and Neighborhood Cable) adopt the ownership model used by FOXTEL. This ownership model is also the model that is still adopted for delivery of subscription television in the majority of jurisdictions around the world.⁵³ Industry expert Mr John Paul of Trident Media Partners⁵⁴ is not aware of any jurisdictions where CA/SI services are unbundled and STUs are owned by providers. Mr Paul estimates⁵⁵ that only approximately 16% of systems around the world provide CA/SI services unbundled with STUs and all of these systems adopt a retail model where the manufacturers of STUs are tightly controlled⁵⁶ (such as BSKyB in the UK).⁵⁷

⁵³ Indeed, DirecTV which has always used retailed STUs has recently announced that it will be giving subscribers the option of leasing them in order to drive take up of interactive TV: Linda Moss, "DirecTV opts for a leasing model", 23 January 2006, www.multichannel.com

⁵⁴ Mr Paul provided a previous expert report: Attachment 18 to the FOXTEL Submission

⁵⁵ Based on working knowledge of the industry and previous unverified research from 2004 of 43 leading pay TV systems, excluding Latin America.

⁵⁶ Departures from this model have proven disastrous – such as MultiChoice South Africa where more than 13 types of retail boxes have hamstrung the networks abilities to evolve the platform – and penetration from launch was painfully slow: John Paul, Trident Media Partners.

⁵⁷ Mr Paul is also not aware of any jurisdictions where pay TV companies install STUs on behalf of competitive pay TV companies (Options E of Ergas' Report).

In addition, there is a direct relationship between STU ownership and piracy costs. There is more public access to STUs and smartcards in a retail model where these items are stored and distributed by numerous retailers. One of the biggest risks for a retail STU model is therefore the increase in security exposure which is why immature markets avoid this approach. The UK, US and South Africa battled substantial piracy and hacking during the first five years of satellite operation and continue to stay only one step ahead of the hackers. BSkyB has so far been reasonably successful in implementing a retail model by strictly approving each new vendor and managing the various types of STUs, new and legacy, that are present in the marketplace.⁵⁸ However, this is a huge operational undertaking for BSkyB which, given FOXTEL's comparative size and the immaturity of the Australian industry, FOXTEL is simply not equipped to undertake. Subscription television in Australia currently only has approximately 24% penetration whereas in the UK penetration is at around 44%⁵⁹ and in the US it is now approximately 86%.⁶⁰

On the basis of the available evidence and current industry practice in Australia, it can only be concluded that Mr Houston's assumption is entirely unreasonable.

(b) Assumption of reciprocity

Mr Houston's conclusion (that incompatible STU constitutes a barrier to entry) must also assume that FOXTEL would be willing to or could be compelled to use a foreign STU to provide its service in the event that a new entrant's subscriber switched to FOXTEL. If this assumption is incorrect, requiring FOXTEL to supply unbundled CA/SI services would not remove the perceived barrier to entry, as the subscriber would still require a FOXTEL STU to receive the FOXTEL service.

It is clear that Part XIC does not allow the Commission to force FOXTEL to use a retailed STU or an STU owned by another operator. FOXTEL submits that it is highly unlikely that it would be prepared to use such an STU. For the reason explained in the FOXTEL Submission, there are compelling commercial reasons why FOXTEL, like most subscription television providers around the world, wishes to retain control of its STU. Those reasons are not only the commercial benefit of subsidising the cost of STU for subscribers to enhance take up of the service, but also technology and piracy reasons. FOXTEL would have grave concerns about its ability to innovate and upgrade its service and to control piracy issues if it were to supply its service through foreign STU. Furthermore, if the access seeker owned the STU (as opposed to the STU being sold to the subscriber), the terms upon which FOXTEL would obtain access would also be another significant issue.

Mr Houston simply assumes that reciprocal access is feasible, albeit contingent upon overcoming a number of hurdles.⁶¹ However, he makes no attempt to address these hurdles or assess the likelihood of reciprocal access being able to be granted. The assumption is again contradicted by all available evidence. FOXTEL submits that for the reasons expressed, it is highly unlikely that it would supply its service through foreign STU, and. Accordingly, if incompatible STU constituted a barrier to entry (which FOXTEL rejects

⁵⁸ Similarly, DirecTV in the US used a method to combat hacking in 2001 which sent simultaneous messages to the smart and STU. This worked only because the systems were linked and the STUs and vendors were strictly controlled by DirecTV: John Paul, Trident Media Partners.

⁵⁹ British Sky Broadcasting Group plc, *Annual Report and Accounts 2005*, page 3.

⁶⁰ Federal Communications Commission, *12th Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, 10 Feb 2006 at page 4, para 8.

for the reasons given above), the same alleged barrier to entry exists under the SAU as under the Option D counterfactual.

(c) Consumer aversion to 'stacking'

In support of his assertion that STU incompatibility is a barrier to entry, Mr Houston also states his opinion that consumers would be averse to stacking STUs.

FOXTEL disagrees and submits that consumers understand that if they change service providers they need new equipment (either leased or bought). As discussed above, most markets around the world prove this to be the case: in almost all jurisdictions there are multiple operators with independent proprietary CA systems which require a different STU. The Commission itself has expressed scepticism about the argument that customers are reluctant to "stack" STUs and stated that "consumers seem willing to stack many other electronic entertainment equipment, such as amplifiers, videos and DVDs."⁶²

In any case, stacking STUs would not be necessary in the assumed counterfactual being considered by Mr Houston. The counterfactual assumes that a new subscription television provider is able to offer a substitute service to that of FOXTEL. For the reasons explained above, it is very unlikely that the subscriber will want both services at the same time. Through its business model, FOXTEL is able to redeploy STU when subscribers cease to be customers. If the new entrant adopts the same business model (which is the most likely assumption, it can do likewise. Accordingly, switching costs for subscribers will be minimal under either the SAU or the counterfactual, and there will be no need for stacking.

If the counterfactual assumes a niche provider, then the service is highly unlikely to be a stand alone service and the provider will wish to supply the service to FOXTEL's subscriber base. This will be done through the SAU again without the need for stacking..

6.4 Reasonableness of the SAU

Mr Houston states that in his opinion the Commission cannot be satisfied that the SAU is reasonable when it is compared to the Option D counterfactual.⁶³ This opinion is based largely on Mr Houston's conclusions concerning the barrier to entry represented by STU incompatibility, which conclusions are fundamentally flawed as discussed above. This section of the report also addresses other opinions or conclusions expressed by Seven or Mr Houston which are erroneous.

(a) Standardisation in infrastructure

Mr Houston places a lot of weight on the benefits he says will arise from "standardisation" of STUs in Australia. Mr Houston's arguments are purely theoretical and are contradicted by real world experience: in practice they have not and cannot work.⁶⁴ An industry standard for a CA/SI system or an STU is not desirable or practical because it limits the development of application, content and STU functionality.⁶⁵ The theoretical efficiencies of

⁶¹ Houston Report, para 92

⁶² The Commission "Report to Senator Alston on Emerging Market Structures in the Communications Sector", June 2003, page 141.

⁶³ Houston Report, para 163

⁶⁴ There are multiple examples of failed open CA/multiple STU models eg the Optus Aurora platform and terrestrial digital STUs: see Engineering Report, attachment 5 to FOXTEL's submission, page 26.

⁶⁵ In fact, in 2002 the EC repealed 'standards' that were in place for digital television and has stated that it does not believe it is appropriate to impose standards for digital interactive television: Directive 2002/21/EC of the European Parliament and of

lower development costs with respect to standardised architectures are vastly outweighed by the need to evolve functionality via the CA and STU code. In fact, there is no real standard in the subscription television industry at any level (STU, CA or applications) because as soon as software is implemented and changed it ceases to be a standard and becomes proprietary and incompatible with other implementations of that standard.⁶⁶ The various overseas examples Mr Houston uses to support standardisation are either taken out of context or are irrelevant. A table discussing these examples is **Attachment 5**.

(b) Ability and incentive to alter the content of its basic package.

Seven and Mr Houston have suggested that FOXTEL would have a greater incentive and ability to add channels to its basic package to make the access seeker's service less desirable or necessary to a subscriber in the unbundling counterfactual than in the factual.⁶⁷ There are two main assumptions inherent in this assertion:

- FOXTEL has the incentive to alter the content of its basic package; and
- unbundling the CA/SI reduces this incentive or ability.

In terms of the first point, FOXTEL denies that it has the incentive to alter the content of its basic package in the way alleged by Seven and Houston. FOXTEL refers to its previous submissions on this point (section 6.5(b) of the FOXTEL Submission). FOXTEL also refers to Confidential Attachment 3 to demonstrate that it is unlikely that FOXTEL would add new channels to its basic service in the way contemplated by Seven and Houston.

In relation to the second point, FOXTEL refers to the supplementary report of CRA at **Attachment 6**.

(c) The costs of unbundling CA/SI services

Seven has asserted that FOXTEL's operational or technical requirements are not compromised under the counterfactuals of unbundling CA/SI or providing the full STU service.⁶⁸ Seven has not sought to provide any evidence in support of this assertion. Instead, Seven makes the unsubstantiated allegation that previous statements made by FOXTEL to the Commission on technical and other difficulties with providing access have been shown not to accurately reflect the position when tested.⁶⁹

Mr Houston assumes that CA/SI unbundling is technically feasible, albeit potentially at a cost to FOXTEL.⁷⁰ However, he does not take these costs into account at all in his

the Council of 7 March 2002 on a Common Regulatory Framework for Electronic Communications Networks and Services; Commission Staff Working Paper, *Communication from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of Regions on reviewing the interoperability of digital interactive television services, Extended Impact Statement*, 30 July 2004, Com(2004)541; Commission of the European Communities, *Communication from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of Regions on reviewing the interoperability of digital interactive television services pursuant to Communication COM (2004) 541 of 30 July 2004*, Com(2006) 37, 2 February 2006

⁶⁶ For example, the Sun Microsystems Multimedia Home platform (*MHP*) has been adopted by many standard bodies as the defacto standard for interactive API layer and applications, even in Australia. But MHP is a standard not an actual implemented software package - once it is implemented it is customised by the implementer (Sun, for example) and becomes incompatible with other implementations of MHP.

⁶⁷ Houston Report, section 6.2.2.3.2

⁶⁸ Seven Submission, section 4.6, pp 19-21

⁶⁹ Seven Submission, page 19

⁷⁰ Houston Report, para 92

analysis, nor does he weigh up those costs with the likelihood of a promotion of competition as a result of unbundling (see Houston 6.3.1).⁷¹

FOXTEL has provided clear technical and industry evidence about the real risks and costs that would result if FOXTEL were forced to supply CA/SI on an unbundled basis or supply the full STU service.⁷² This evidence is unchallenged. In addition, it is apparent that there are serious risks of dispute between FOXTEL and access seekers about upgrades and changes to the technology.⁷³ FOXTEL submits that these factors are highly relevant to the Commission's assessment of the SAU and any potential counterfactual.

6.5 The effect of the s 87B undertaking

Finally, Seven argues that FOXTEL's submissions concerning the impact on its business if access in the form of Options D and E were to be granted are contrary to its assurances that it would build its digital pay TV platform in a manner which facilitated access. In particular, Seven argues that FOXTEL's need to separate its SMS or modify its system seems to be contrary to clause 4.9 of FOXTEL's s 87B undertaking and the need to obtain sub-licences in respect of third party IP seems to be contrary to clause 4.11 of FOXTEL's s 87B undertaking.

FOXTEL submits that these arguments are incorrect. FOXTEL's s 87B undertaking was clearly provided on the basis that access was to be granted only to STUs in FOXTEL homes. There is nothing in FOXTEL's s 87B undertaking or commentary in relation to it by FOXTEL or the Commission that suggests that FOXTEL's obligation was to ensure access to its STUs when not in use by FOXTEL. This is clear by the terms of the s 87B undertaking itself, in particular that:

"The design and equipment of that part of the digital network used to provide any Commercial Retail Digital Cable Subscription Television Service and any Commercial Retail Digital Satellites Subscription Television Service (the STS Network) will facilitate access to the STS Network by access seekers wishing to provide a Subscription Television Service by accommodating multiple access seekers."

The "STS Network" only encompasses STUs used by FOXTEL to provide its commercial retail digital cable and satellite subscription television service. Clauses 4.10 (in relation to the active customer smartcard database) and 4.11 (in relation to third party rights) all rely on the concept of access to the "STS Network", not access to STUs that are not deployed by FOXTEL as part of that Network. Further, it is clear that the s 87B undertaking was given on this assumption as both the analogue and digital undertakings attached to that Undertaking only contemplated access to STUs in FOXTEL homes.

Finally, it is disingenuous for Seven to refer to the Commission's view expressed in its reasons accompanying its Interim Determination in the analogue pay TV access arbitrations in relation to access to STUs in non-FOXTEL homes. The Commission (as Seven well knows) subsequently accepted FOXTEL's analogue undertaking on the basis

⁷¹ Houston Report, para 146

⁷² FOXTEL Submission, section 6.3; Engineering Report, Attachment 5 to FOXTEL Submission

⁷³ The joint venture between Optus, FOXTEL and Austar is an example of how a single CA hampers development. During this relationship all changes had to be approved by three operators who rarely agreed. Inevitably FOXTEL broke free and the joint venture fell apart.

that access is only granted to STUs in FOXTEL homes⁷⁴ (which Seven did not seek to challenge) and also accepted the FOXTEL exemption in relation to the digital undertaking on that basis.⁷⁵

7. Access Pricing

7.1 Cost of capital

FOXTEL refers to the response by Professor Stephen Gray at **Attachment 7** to the report of Professor Officer on the appropriate gamma.

FOXTEL will be responding separately in relation to the inclusion of marketing costs in response to the Commission's information request of 23 March 2006.

7.2 Verification of costs

Ten asserts that the pricing methodology proposed by FOXTEL is "*unnecessarily complicated and lacking in transparency*". Ten has provided no evidence to support that assertion and paragraph 22 which is masked for confidentiality is unavailable for FOXTEL or its legal advisers to comment on.

However, FOXTEL submits that its pricing methodology is set out clearly in Schedule 3 to its Digital Access Agreement and is very transparent, including the annual publication of FOXTEL of a rate card based on that methodology.⁷⁶

7.3 Allocation of costs

Seven also criticises the revenue/ratings methodology for allocating costs. The Tribunal previously accepted this methodology.⁷⁷

Seven's primary complaint appears to be that FOXTEL's revenue is not subject to an 'imputation'.⁷⁸ This is because FOXTEL bears all of the costs of the STU business that are not allocated to access seekers. Accordingly, it is FOXTEL's average revenue per rating point which is the relevant base against which to allocate costs, by imputing a minimum revenue per rating point to access seekers. This has a further desirable consequence: FOXTEL should not have to devote capacity to access seekers whose revenues and contribution to its cost recovery are below the average it could obtain itself. In a context where FOXTEL's prices are in any event constrained by effective competition from other forms of entertainment, this will serve the desirable purpose of ensuring that resources are not devoted to channels on which users place a low value. It also implies that given that access seekers are under no requirement to bear any of the "down side" associated with FOXTEL's investment, when they use that investment they should do so in a way that does not require FOXTEL to bear the risk that they might contribute less than FOXTEL itself would.

⁷⁴ The Commission, "A report on the assessment of the Analogue Pay TV Access Undertaking proffered by FOXTEL Management Pty Ltd on 22 December 2003", March 2004

⁷⁵ The Commission, "Section 152ATA Digital Pay TV Anticipatory Individual Exemption Application lodged by FOXTEL - Final Decision", December 2003

⁷⁶ Schedule 3, clause 1 of the DAA

⁷⁷ *Re Seven Network Limited (No 4)* [2004] ACompT 11 at 326

⁷⁸ Seven Submission, section 8.2, pages 34-35

Seven asserts that the imputed revenue method is unfair because FOXTEL receives higher revenue from the basic package compared with access seekers, and that this inflates an access seeker's imputed revenue.⁷⁹ This is incorrect. FOXTEL's gross revenue in isolation is not relevant to the imputed revenue; it is FOXTEL's revenue per ratings point that is relevant. There is no evidence to suggest that FOXTEL's revenue per rating point for its basic package is higher than for premium packages.

Seven also criticises the use of a minimum ratings figure per channel, because if and when 400 channels are offered, the minimum will equal the average.⁸⁰ The minimum figure is the current minimum measure of ratings currently offered by Australian television ratings agencies. If and when a greater number of channels is offered, it can be assumed that the ratings agencies will use a lower minimum measure.

8. Interactive Services

FOXTEL refers generally to the Technical Report at **Attachment 8** in relation to issues raised by the Seven Submission and TWTV Submission on interactive services. However, FOXTEL also wishes to make a few additional comments below.

8.1 Return Path

FOXTEL refers to section 7.5 of the Seven Submission and refers to section 1 of the Technical Report at Attachment 8 in response.

FOXTEL does not provide itself or other persons with carriage or related services in relation to a return path connection. This is the case for both PSTN and cable return path connections: in the case of point of presence (**POP**) services on the PSTN, FOXTEL obtains these services from a third party – Telstra; in the case of PSTN return path connections, FOXTEL customers obtain these from their usual telephony services provider; in the case of cable return path, FOXTEL currently does not offer this to its subscribers. Therefore FOXTEL is not an access provider in respect of such services for the purposes of s 152AR of the Act; accordingly these services have been excluded from the DAA.

To the extent that a modem is installed in a FOXTEL STU to enable a return path connection, whether this be a PSTN or cable modem, FOXTEL will grant access to this installed modem (see clause 6 of the DAA). Requiring FOXTEL to upgrade the modem connections in its STUs or install these where they are not installed is beyond the scope of FOXTEL's obligations under Part XIC of the Act: FOXTEL has agreed to provide access seekers with STU services to an *equivalent quality* as it provides to itself. If there is no modem, this affects FOXTEL to the same extent it affect the access seeker.

If an access seeker wishes to use the available connection then, as FOXTEL has done, it will need to negotiate a commercial arrangement with a relevant third party service provider of POP services. Whether this is *too expensive or impractical for access seekers to arrange* is not an issue for the DAA and FOXTEL: it is a separate issue for the access seeker to determine when it decides to enter into the DAA.

As FOXTEL has previously submitted to the Commission (see section 5 of the FOXTEL Submission), in FOXTEL's view:

⁷⁹ Seven Submission, section 8.2, pages 34-35

⁸⁰ Seven Submission, section 8.2, pages 34-35

- the ability to supply 'interactive' services using telephones and SMS is already available today and is as competitive as using the remote control linked to the STU; and
- POP services on the PSTN network are widely available and can be self-supplied or obtained from a variety of sources.

For the reasons above, FOXTEL submits that there is no possibility of there being "multiple access regimes" in respect of access to FOXTEL's services.

8.2 Second or subsequent tuner

In paragraph 25 of the Ten Submission, Ten states that FOXTEL has changed the DAA to remove an exclusion relating to dedicated access to any second or subsequent tuner or hard drive installed in a FOXTEL STU and should clarify whether this amendment means that access to second or subsequent tuners, to the extent they are introduced into FOXTEL's STU, will form part of the Digital Set Top Unit Service. FOXTEL notes that this change to the DAA resulted from the decision of the Commission in relation to FOXTEL's application for an anticipatory individual exemption order in relation to its (then) proposed digital subscription television service. In deciding to make the order, the Commission requested that FOXTEL delete the relevant exclusion.⁸¹

The balance of Ten's comments on this issue, in which it comments about the "benefits" of dual tuners,⁸² have nothing to do with retail access to FOXTEL's infrastructure and FOXTEL submits that this issue is not relevant to the Commission's assessment of FOXTEL's SAU. FOXTEL has written to the Federal Government about the problems associated with dual tuners and notes that the Federal Government has accepted these problems and indicated that it will not be mandating dual tuners.⁸³

8.3 Definition of Related Services and Modem Services

FOXTEL refers to paragraph 15 of the Ten Submission. FOXTEL does not believe that the definition of 'Related Services' in the DAA needs to be amended to include an express reference to "interactive services".

The definition is already widely drafted, to the benefit of access seekers. To the extent that "interactive services" (by which FOXTEL understands Ten to mean services that provide content such as multiple player angles, different news options, player statistics and near video on demand etc) are related to the digital subscription television services being provided by an access seeker and have the sole purpose of *enhancing* television programs, then they are clearly covered by the existing provisions.

In addition, the use of the word 'interactive services' may create confusion as to the nature of Related Services, and unnecessarily limit them. As FOXTEL has previously submitted to the Commission (see section 5 of October 2005 Submission), the delivery of services such as multiple player angles, different news options, player statistics and near video on demand, all of which use the forward path and do not require the use of the modem or the return path to send signals back to the subscription television provider, are not interactive

⁸¹ The Commission, "Section 152ATA Digital Pay TV Anticipatory Individual Exemption Application lodged by FOXTEL - Final Decision", December 2003 at pages 70 to 74, 85 and 88

⁸² Ten Submission, para 25 and 26

⁸³ Kitney "Pay TV wins in the battle of the boxes" The Financial Review, page 1, 28 Jan 2003

as no signal is transmitted from the subscriber's STU to the subscription television provider (or any one else) when the subscriber makes a selection of what to view from the alternatives provided. Rather, the subscriber is simply making a selection between information which is already being delivered to the subscriber's STU, in much the same way as a subscriber selects a particular channel. For example, Sky News Active offers 8 information screens, each of which uses the forward path.

FOXTEL does not agree with the statement in the Ten Submission that it will be "*extremely difficult for access seekers to launch interactive offerings based on the Modem Services offered under the current DAA*"⁸⁴ and there is no basis for this statement. FOXTEL currently offers a range of return path services using the PSTN return path – for example: Sky News Active voting; MTV awards voting in 2005; Super Simpsons voting; Australian Antiques Roadshow voting; and Pick & Play games. In addition, in FOXTEL's view, the ability to supply 'interactive' services using telephones and SMS is already available today and is as competitive as using the remote control linked to the STU.

FOXTEL also refers to Section C of the TWTV Submission. FOXTEL submits that the DAA adequately reflects the fact that FOXTEL is now undertaking to provide Modem Services. The definition of Digital Set Top Unit Services as described in schedule 1 clearly sets out Modem Services as part of such services.

FOXTEL does not agree that the DAA needs to be amended to include references to Access Seeker Modem Content, as suggested. The primary purpose of the DAA is to enable access seekers to provide digital subscription television services and related services to subscribers. FOXTEL has widely defined "Related Services" for the reasons noted above.

8.4 Acceptance Testing

FOXTEL will set out the required specifications and other technical and operational requirements of access seeker equipment and content, in the Operational Procedures, Modem Services Protocol and Interface Specifications. FOXTEL has agreed to undertake (see clause 4.3(a)(ii) of the DAA) technical testing in relation to an access seeker's broadcast signal. FOXTEL anticipates that, as part of the Modem Services Protocol, FOXTEL will also conduct necessary testing at rates set out in the rate card and, as a practical matter, at the same time as testing of the access seeker's broadcast signal.

8.5 Ability for access seekers to supply only interactive overlay

One of the reasons TWTV opposes the SAU is that TWTV submits that the SAU does not allow a third party to use it in order to provide interactive features which enhance channels already broadcast as part of the FOXTEL service.

FOXTEL submits that this criticism is not a valid one. First, there are real technical difficulties in allowing an access seeker to provide an interactive overlap onto an existing channel. FOXTEL refers to section 4 of the Technical Report at Attachment 8 in this regard.

First, although the TWTV submission is put in the context of an access seeker wishing to add return-path interactivity to a channel already forming part of the FOXTEL service, essentially what TWTV is arguing for is a right for all channels which form part of the

⁸⁴ Ten Submission, para 15(b)

FOXTEL service to be able to enhance their channels with interactive features as they wish, regardless of the interests of FOXTEL as the retail provider with the direct customer relationship. This involves an interference in the wholesale arrangements between FOXTEL and its channel suppliers. It is akin to allowing a channel supplier to supply additional channels as it wishes *as part of the FOXTEL service*.

Second, it is vital for FOXTEL to be able to control the content available on its service in order to maintain the quality and integrity of the service. An access seeker may want to add return-path interactivity to an existing channel in a way that FOXTEL considers would be inappropriate, or unattractive, upsetting or annoying to its subscribers. For example, an access seeker may attempt to advertise or sell products through an interactive application to subscribers who may just want to enjoy the television programme without interruption or provide content through an interactive application over a children's channel that would be inappropriate for children. Such actions may cause damage to FOXTEL's brand and cause subscribers to disconnect from FOXTEL.

Third, whether a channel on the FOXTEL service can add return-path interactivity to its channel, or channels, depends on negotiations between FOXTEL and the channel supplier, which are in turn dependent on a number of factors including the availability of sufficient transmission capacity and whether FOXTEL considers the interactive application will add to the overall appeal of the channel and the FOXTEL service. The retail access regime created by the Act does not, and is not intended to, impact on the wholesale arrangements between FOXTEL and its channel suppliers. TWTV is, on its own submission, a sophisticated supplier of return-path interactive applications. TWTV here in Australia and in other countries has deployed applications and technology. If TWTV believes that it does not have the experience to provide the necessary technology and application then TWTV can source these services from OpenTV as FOXTEL does today. If TWTV wishes to add interactivity to channels that form part of the FOXTEL service, it can and should do so by agreement with the relevant channel supplier and FOXTEL. In the alternative, it would be possible for any access seeker to develop or license a channel, augment it with whatever return-path interactive applications it is able to provide and supply it on a retail basis using the SAU.

8.6 Provision of own modem

In section 7.5(c) of the Seven Submission, Seven submits that access seekers may want to use a better modem than the one installed in FOXTEL's STUs. Seven asserts that the SAU is not consistent with s 152AR(5) because it does not provide for access seekers to interconnect their own modem.

The DAA does not prohibit the interconnection of an access seeker's modem; it is simply not addressed in the DAA. It is not possible in the DAA to address every conceivable contingency or requirement of access seekers. It is questionable whether the contingency identified by Seven will in fact eventuate.

In any event, in the SAU FOXTEL undertakes to comply with the obligations in s 152AR (see clause 2.1 of the SAU). Accordingly, it is incorrect to assert that the SAU or any part of the DAA is inconsistent with the SAOs. If the contingency identified by Seven materialises, it will be addressed under the SAU and in accordance with the requirements of s 152AR.

9. EPG

9.1 EPG services

FOXTEL refers to paragraph 17 of the Ten Submission. FOXTEL submits that the definition of EPG services need not be expanded as supply of series link and real time functionality is already contemplated by the DAA. Clause 5.1(d)(iv) requires an access seeker to provide to FOXTEL series link and real time data, if it wishes to offer series link and real time functionality to subscribers.

FOXTEL does not agree with the concerns raised in paragraphs 18-19 of the Ten Submission. As set out in FOXTEL's original submission, FOXTEL is offering EPG services to access seekers in the interests of providing greater certainty to them. However the EPG remains a FOXTEL-branded EPG, and FOXTEL bears the bulk of the costs of supplying it to users. Consequently, it is reasonable that access seekers are not awarded identical rights to FOXTEL in respect of reserving and displaying channel numbers on the EPG.

As explained in the FOXTEL Submission, access seeker channels in any category will not necessarily be 'forced' onto a particular page of the EPG as suggested by Ten. Only active channels will be listed on the EPG. Therefore, even if FOXTEL reserved a significant number of channel numbers in between an active channel number and a channel allocated to an access seeker, the access seeker's channel would be listed directly after the last active channel, which could be on the first or a subsequent page of an EPG genre listing.

Notwithstanding the above, FOXTEL disagrees with the Ten Submission that access seeker's channels appearing on the second page of a category make the access seeker's channels harder to select:

- in FOXTEL's experience, placement of channels on the first or subsequent pages of an EPG genre is not as relevant as what listings a channel is placed next to. FOXTEL has many popular channels on the second page of EPG genres – for example, The History Channel appears on the second page within the News and Documentary category. FOXTEL must be fair and reasonable in its allocation of channel numbers to access seekers (see clause 10(d) of the DAA);
- subscribers to access seeker channels are likely to find and select channels they have actively subscribed to and paid for. Providing information and instructions to subscribers in respect of channel numbers is the responsibility of an access seeker.

9.2 Access to the EPG

FOXTEL refers to paragraph 20 of the Ten Submission, and paragraph C.1 of the TWTV Submission.

Use of the EPG will benefit an access seeker's subscribers as it will provide them with a simple mechanism to locate and activate the channels they have subscribed to. However, as FOXTEL bears the bulk of the cost of supplying the EPG, it is reasonable, having regard to the cost of providing the EPG and FOXTEL's level of investment in the EPG, for FOXTEL not to make listings visible to all viewers but only to those viewers who subscribe to the access seeker's channels. That an access seeker's channels listed on the FOXTEL EPG are viewed only by that access seeker subscribers does not of itself restrict access to content offered by those access seekers: access seekers are free to undertake their own

marketing activities in relation to their channels using their own resources. The FOXTEL EPG should not be used as a marketing tool for access seekers, when there are numerous other avenues open to the access seeker to do this, for example, advertising in magazines or on television or on radio.

In relation to the TWTV Submission that the FOXTEL EPG should display and advertise the fact that red button interactive features are available on various channels, FOXTEL currently offers an "Active" button feature on its EPG. This "Active" button identifies all channels that have 'interactive' features. Access to this button will be available to all access seekers, in the same manner in which it is to available to all FOXTEL channels (FOXTEL has agreed to provide access seekers with an equivalent quality of service as it provides to itself: see clause 4.1(b) of the DAA).

10. Other Issues

10.1 Changes to Operational Procedures etc

FOXTEL refers to Section C of the TWTV Submission on this point.

As FOXTEL has previously submitted to the Commission, these documents will not be open to negotiation with access seekers as they relate to the technical and operational requirements and capabilities of FOXTEL's system. They are fundamental to the successful operation of FOXTEL's pay TV platform: which primarily supports FOXTEL's business, in addition to the businesses of a number of access seekers.

However, in the spirit of equivalent quality of service and non-discriminatory access, these documents will apply equally to FOXTEL and to access seekers. Further, FOXTEL has agreed not to engage in conduct with the purpose of hindering or preventing access (see clause 4.7(c) of the DAA).

FOXTEL has provided the Commission with a copy of the latest version of the Operational Procedures. This will be made available to access seekers if the conditions in clause 2.4 of the SAU have been met.

In relation to any changes to these documents, as they relate to technical and operational requirements and capabilities of FOXTEL's system, changes will not be open to negotiation with access seekers. However, any revised procedures will apply equally to FOXTEL and to access seekers. Further, in clause 11.2(b) of the DAA, FOXTEL has agreed to give an access seeker reasonable prior notice of a proposed modification where it will have a material adverse impact on the functionality or performance of the services supplied to the access seeker or result in additional costs to that access seeker under the DAA. FOXTEL will use reasonable endeavours to take into account any reasonable material technical concerns notified by the access seeker when it considers how it will implement the proposed modification.

If FOXTEL cannot enhance, modify or upgrade its platform as it requires then it will not be able to improve services for its customers. It is in the LTIE that FOXTEL be able to enhance and upgrade the performance of the FOXTEL pay TV platform.

10.2 Bank Guarantee

FOXTEL disagrees with the TWTV Submission on this point. FOXTEL submits that the provisions are reasonable: they are a typical request in commercial relationships of this nature.

The extent of the bank guarantee is limited: the amount must be reasonably determined by FOXTEL to be sufficient to enable the performance of the access seekers obligations under the DAA. As previously submitted by FOXTEL, it is not possible for FOXTEL to predetermine the exact amount of liability and cost in respect of which it will require a bank guarantee as this will depend on the nature of each access seeker (their size, financial viability etc), and the number and type of services that each access seeker will require from FOXTEL during the term of the DAA. Accordingly, the amount of the bank guarantee must be determined by FOXTEL, acting reasonably.

The fact that an access seeker may terminate by giving one month's notice is not relevant to determining the amount of a bank guarantee and the extent of FOXTEL's need to obtain a form of security from access seekers. It *might* be relevant if FOXTEL itself could terminate by giving one month's notice: but it cannot do this.

10.3 The DAA can be changed at any time and for any reason

FOXTEL does not agree with TWTV's view that the *'DAA ... provides no certainty whatsoever of the terms in which an access seeker can deploy its service'* (see section C.3 of the TWTV Submission).

While FOXTEL does have the right to change certain of the terms and conditions of the DAA, these are limited to the situations set out in clauses 4.4 and 11.2 only (see clause 30.2 of the DAA). Significantly, FOXTEL may not alter the provisions of schedule 3, which deals with access charges and pricing methodology (see clause 4.4(b)).

Further, FOXTEL has agreed with the Commission that it will not vary the DAA other than in accordance with section 2.5 of the SAU. Notably, this includes a requirement that the Digital Set-Top Unit Services supplied to an access seeker remain supplied to the equivalent quality as FOXTEL supplies to itself.

FOXTEL contends that these provisions are reasonable as:

- they are necessary to enable FOXTEL to improve, enhance and adapt its pay TV platform to take advantage of new technologies, market practices etc, and give consumers a better viewing experience;
- FOXTEL remains committed to providing an equivalent quality of service to access seekers as it provides to itself and;
- access seekers can terminate the DAA if they receive notice of change under clause 4.4(b) or 11.2(b) (see clause 24.3(i) and (j) of the DAA)

Without these limited "unilateral rights" to vary the DAA, FOXTEL contends that it would be likely to be impossible to obtain the unanimous approval of all access seekers to undertake any changes to its pay TV platform: this is not in the LTIE and clearly against the legitimate business interests of FOXTEL who wishes to provide a world class pay TV service.

10.4 Charges for faults

FOXTEL refers to Section C.4 of the TWTV Submission. FOXTEL contends that these provisions are reasonable as:

- FOXTEL is constantly monitoring its pay TV platform and connected equipment, remedying faults (and it is in FOXTEL's best interests to do this), thereby limiting the likely need for an access seeker to contact FOXTEL about a fault.

- Only where an access seeker **notifies** FOXTEL of a fault with FOXTEL's equipment, and FOXTEL is not the cause of the fault due to its negligence or breach, will the access seeker be charged: this charge reflects FOXTEL's reasonable costs and expenses in investigating a fault. In most cases FOXTEL expects that such notified faults will be caused by an access seeker's equipment or service.
- Access seekers must be fully responsible for their equipment and services and must maintain these to the required technical and operational standards. As they are seeking access to FOXTEL's pay TV platform, unless FOXTEL is in breach of its obligations under the DAA, it is reasonable that access seekers take such full responsibility for their equipment and their services.

However, FOXTEL agrees to amend the DAA to provide that in Schedule 2, clause 6, where a Fault is notified by the access seeker and it is not caused nor contributed to by FOXTEL or the access seeker, then the costs in paragraph (b) will be shared equally between FOXTEL and the access seeker.

FOXTEL contends that it is not reasonable for the definitions of *Access Seeker Fault* and *FOXTEL Fault* to be consistent, for the reasons noted above.

10.5 Ownership of enhancements to the network

FOXTEL refers to Section C.5 of the TWTV Submission. Enhancements will be made solely to accommodate, and for the benefit of, access seekers. They merely enable FOXTEL to provide services under the DAA and offer no additional benefits to FOXTEL. Most enhancements will be shared among access seekers. FOXTEL has agreed that it will pro-rate the costs of any shared enhancements to a maximum of 20% of the actual costs of them.

As FOXTEL has previously submitted to the Commission, given that the enhancements are shared, it is not clear that they could be removed and "returned" to access seekers. But even if they could, the cost of doing so would be significant. In FOXTEL's view, it would not be worth the effort nor would it provide any benefit to access seekers to remove enhancements at the termination of the DAA and provide these to access seekers.

10.6 Warranties, indemnities and assignment rights

FOXTEL refers to Section C.7 of the TWTV Submission. FOXTEL contends that the warranties, indemnities and assignment rights in the DAA are commercial and reasonable, given the arrangements that FOXTEL has in place with other third parties in relation to its platform and the technical and operational risks to FOXTEL of an access seeker's presence on its pay TV platform.

In relation to the assignment provisions, FOXTEL must have the flexibility to reorganise its business and affairs, especially given the term of the DAA. As owner of the FOXTEL platform, FOXTEL is responsible for numerous subscribers including those of other access seekers. Given that, FOXTEL must be able to verify and approve those access seekers who have access to its system. FOXTEL therefore disputes the statement that these provisions are grossly unbalanced. It is likely that potential damage or loss in relation to FOXTEL would be greater than an access seeker on FOXTEL's pay TV platform. It is reasonable that FOXTEL have the ability to reduce those potential losses or damage. At any rate, access seekers will only be liable to the extent that they have caused or contributed to the damage or loss.