



**Neighborhood
C A B L E**

PUBLIC SUBMISSION

TO THE

Australian Competition and Consumer Commission

Third Line Forcing Notifications lodged by Telstra Corporation Limited and Telstra Pay TV
Pty Limited

Notification Numbers N31277 and N31278

February 2004

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1 INTRODUCTION

The Australian Competition and Consumer Commission (ACCC) has received notification of third line forcing conduct from Telstra Pay TV Pty Limited and Telstra Corporation Limited in relation to the bundling of Foxtel's digital subscription television services and Austar's "new" subscription television services sold as a Telstra Pay TV service with telecommunications services offered by Telstra Corporation Limited.

The Commission has asked for interested parties to assist in its consideration of the notifications by submitting papers commenting on the notifications.

Neighborhood Cable, a regional Pay TV and telecommunications service provider which has invested heavily in telecommunications and Pay TV infrastructure and services in regional Victoria is an interested party to the notifications and, as such, tenders this submission to the ACCC.

The structure of this submission is to clearly put forward Neighborhood Cable's view on the legal and competitive implications of the notifications both from the perspective of regional Australia generally and Neighborhood Cable, as a unique regional telecommunications company, specifically.

The submission will then set about justifying Neighborhood Cable's position by discussing:

- The public benefit;
- The public detriment and
- The markets

which will be impacted by the notifications should the ACCC fail to remove the immunity for the notified conduct.

2 NEIGHBORHOOD CABLE'S POSITION ON THE NOTIFICATIONS

The key objective of the *Trade Practices Act 1974* is to foster and develop economic advancement through competition and efficiency by principally preventing anti-competitive conduct.

Third line forcing is one of the most detrimental forms of anti-competitive conduct being a specific form of exclusive dealing and, as such, is expressly prohibited in terms of the Act.

Such conduct in a robust, truly competitive environment, like, for example, building supplies or retailing would not be tolerated due to its clearly anti competitive nature. Yet here is one of Australia's largest companies, itself a near monopoly, justifying to the ACCC through this notification that a customer can take up its (re-branded) Pay TV service (at up to a 5% discount) on the condition that a customer also takes one or more telecommunications services from a separate entity (at up to a 10% discount) is not anti-competitive and is in the public interest. The Pay TV service, quite incidentally, is the Pay TV service of a third party, itself a monopoly in regional New South Wales, Victoria, Queensland, South Australia, Tasmania and the Northern Territory.

Neighborhood Cable, regional Australia's only facilities based telecommunications carrier and Australia's only truly independent Pay TV provider strongly objects to the notification made by Telstra Pay TV Pty Limited and Telstra Corporation Limited and urges the ACCC to actively consider removing immunity from this anti-competitive market conduct.

It is the view of Neighborhood Cable that while the ACCC saw their way clear to allow such conduct in some Australian capital cities, given the market dynamics and competitive nature of those markets, that the conditions and competitiveness of the telecommunications and Pay TV markets in regional Australia is significantly weaker or absent in many markets and allowing such conduct in those markets would banish, forever, any prospect of the development of competitive forces in those markets.

Consider Telstra Pay TV, a subsidiary of Telstra Corporation, a 50% stakeholder in Foxtel which is a 50% stakeholder itself in XYZ entertainment, together with Austar, the producer or exclusive rights holder of a raft of Pay TV channels including TV1, Arena, Lifestyle and Discovery.

How many competitors of any size in any market gained access to these vital channels? Transact, Neighborhood Cable, Northgate? Despite repeated and passionate pleas - none, not one.

It is the view of Neighborhood Cable that in order for the ACCC to allow such conduct to continue to enjoy immunity from the third-line forcing provisions of the *Trade Practices Act 1974*, significant changes to the supply arrangements of Pay TV content allowing complete access to all competitors for all content would need to be agreed by the parties to this notification. This undertaking alone would be the only way of ensuring that a competitive playing field is maintained for all competitors in regional Australia specifically in the Pay TV industry and more generally, given the telecommunications services link in this notification, telecommunications services as well. It is, however, also the view of Neighborhood Cable that these changes to supply arrangements will not occur, particularly after the decision of the ACCC in November 2002 to aggregate the supply and distribution of Pay TV content.

3 THE NEIGHBORHOOD CABLE EXPERIENCE

The supporting documentation inviting submissions to discuss this third line forcing notification mentions a test applied by the ACCC to determine whether immunity should be continued. That test is referred to as the “with-and-without analysis”.

Neighborhood Cable can provide a unique insight, from a real world perspective, of dealing in regional markets where the third line forcing referred to in the notification is currently permitted by the ACCC’s November 2002 decision and regional markets where approval for this market conduct is now being sought.

Neighborhood Cable owns and operates, facilities based, hybrid fiber optic/coaxial (HFC) cable broadband telecommunications networks in the Victorian regional cities of Mildura and Ballarat where third line forcing approval by Telstra Corporation and Telstra Pay TV is currently being sought as well as the City of Greater Geelong, where Telstra Corporation and Telstra Pay TV currently enjoy immunity from the third line forcing provisions of the *Trade Practices Act 1974* in terms of the November 2002 decision.

Over all of these HFC networks, Neighborhood Cable delivers Pay TV, broadband internet and some telephony services.

In the markets of Mildura and Ballarat, pre launch subscriber interest was similar on a percentage basis.

In both of these markets Austar directly targeted potential Pay TV subscribers pre-launch and continued to do so post launch.

Despite restricted marketing due to budgetary constraints, in both of these markets Pay TV subscriber uptake was strong and similar in number as a function of time.

In both of these markets, subscriber uptake of broadband internet services was very strong, significantly exceeding budget and auguring well for a successful, competitive broadband internet marketplace in those cities.

In Geelong by contrast, pre-launch subscriber interest well exceeded either Mildura or Ballarat on a percentage basis up until January 2003.

Due to the importance of the market for the future of Neighborhood Cable, little expense was spared in the pre-launch and launch marketing campaigns.

Yet despite very positive indications pre third-line forcing immunity in Geelong, Neighborhood Cable believes that the concerted efforts of Telstra armed with the third-line forcing immunity to bundle Foxtel's Pay TV with Telstra's telecommunications services has had a significant and detrimental effect upon the uptake of Neighborhood Cable's competitive broadband and Pay TV products in the Geelong market.

This experience has serious consequences not only for Neighborhood Cable's rollout considerations in new regional centres in Victoria and beyond should the third-line forcing in the notification continue to attract immunity from the *Trade Practices Act 1974*, but, we believe, will have a devastating effect on the potential for any new competition in either Pay TV or telecommunications anywhere in regional Australia which is so desperately needed.

To date, Neighborhood Cable has invested over \$50 million in deploying facilities based infrastructure in regional Victoria to enable the creation of a healthy and vibrant, competitive Pay TV and telecommunications environment in those markets where none previously existed. The ACCC would be aware, Neighborhood Cable has long campaigned for open access to Pay TV programming as is the case internationally where healthy and competitive Pay TV and telecommunications markets thrive. Neighborhood Cable has long held the view that a profitable Pay TV business is the key to the real regional holy grail – competitive broadband telecommunications services.

Unfortunately, as a nation, we seem to have gone the other way, actually providing immunity from one of the core anti-competitive elements of the *Trade Practices Act 1974* – third-line forcing.

Telstra Pay TV and Telstra Corporation now seek to create a nationwide Pay TV and telecommunications monopoly by expecting a similar immunity Australia-wide.

This would be a devastating blow to telecommunications competition in regional Australia and the ACCC must very carefully consider the long term effects of endorsing immunity from a central element the anti-competitive legislation contained in the *Trade Practices Act 1974*.

4 THE PUBLIC BENEFIT OF THE NOTIFICATION

Neighborhood Cable cannot identify any benefit which would accrue to regional or metropolitan Australia, competitive Pay TV or telecommunications services should immunity from the third-line forcing provisions of the *Trade Practices Act 1974* be afforded Telstra Pay TV and Telstra Corporation.

As Telstra Pay TV would be simply “reselling” the standard Foxtel and Austar offering and tiers, the public would not benefit from any of the classic results of true competition. This, again, is in contrast with the public benefit in the capital cities when Optus TV and Foxtel “pooled” programming allowing subscribers to benefit from improved choice and new channels.

Business Efficiency

There are no grounds for justifying any improvement in business efficiency. Telstra Pay TV will simply be billing “its” customers instead of Foxtel or Austar, where conceivably, Foxtel or Austar were previously billing the same customer.

Increased Competitiveness

There are no grounds for justifying increased competitiveness as the act of giving the same product, effectively, two (or now three) brands, creates no more competition. What regional and metropolitan Australia needs more than anything else is *tangible* and sustainable competition. This notification, seeks to go the other way.

Rationalization

There are no grounds for arguing public benefit through the more efficient allocation of resources or in lower or contained production costs through rationalization. It is difficult to rationalise when you are starting out with only one provider. It can be argued, in fact, that the reverse is true in this case. There is likely to be a duplication of resources where none previously existed as one service provider divides to become two with no change to the product.

It is Neighborhood Cable’s experience that the vast majority of “new” customers to a Pay TV service are simply churn from an alternate provider. This being the case, it is likely that most of Telstra Pay TV’s new customers will simply be “churn” from Foxtel or Austar. This is an inefficient allocation of resources.

Employment Opportunities

It is unlikely that any new significant employment opportunities will be created as a result of this notification standing. Both Foxtel and Austar currently subcontract installation and sales resources

and it is conceivable that Telstra Pay TV will simply utilise this same resource. Given that the vast majority of new Telstra Pay TV customers would be ex Foxtel or ex Austar and not require any new hardware or installation resource, the prospects for new employment opportunities would be minimal.

Cost Savings

It is unlikely that any significant industry cost savings will be realised by this notification. Supply chains between and through all of the parties associated with this notification are well established and are not likely to change in any way that could promote cost savings or lower prices.

More Competitive Marketplace

To conceive of this notification as the creation of a more competitive marketplace is to strike at the very core of the anti-competitive provisions of the *Trade Practices Act 1974*. As previously detailed, all of the parties to this notification are deeply intertwined to the point where, for example, a Telstra Pay TV customer receives a signal from a satellite transponder which Foxtel (50% owned by Telstra) shares the cost of with Austar to offer a channel which Foxtel and Austar jointly produce and own exclusive rights to. Telstra simply re-branding a service which it already sells to that very same market hardly constitutes the promotion of competition in the industry. More correctly this should be viewed as a concentration in the industry into the hands of one supplier.

Equitable Dealings

The conduct of Telstra and Foxtel in the past towards potential competitors leads to the unavoidable conclusion that the parties to this notification have no intention of promoting equitable dealings in the market. Furthermore, there are no provisions or undertakings in their notification or supporting documentation to suggest otherwise.

Export Growth or Import Replacement

There are no grounds in this notification to support a view that either any growth in export markets or the development of import replacements would accrue.

Economic Development

The anti-competitive nature of this notification will have the effect of suppressing and stifling competition and development of regional Pay TV and, more importantly, telecommunications services. Neighborhood Cable has already experienced this in its Geelong market where third-line forcing of the type the subject of the notification, is currently immune from those provisions of the *Trade Practices Act 1974*.

This effect, in turn, will have a negative effect on capital investment in these industries in regional Australia, therefore no argument supporting immunity from third-line forcing being sustained on the basis of stimulating economic development or capital investment can possibly be sustained.

Improvement in Services or Choice

As the service proposed to be offered by Telstra Pay TV in regional Australia is identical to the product already offered by Austar (as it is the Austar product), there is no argument supporting continued immunity from third-line forcing on the basis of improvement to or expansion of services or consumer choice. Rather the opposite is true. The consolidation that will result in the pay TV industry will impede the development or implementation of competitive services or products in both the pay TV industry as well as for telecommunications services.

Better Informed Public

Apart from the ability or opportunity for Telstra to engage in a marketing campaign to bundle customers in terms of the immunity they seek, and the potential for that campaign to raise awareness of or alert the public to the availability of the services they already have access to under a different brand name at a slight discount, it is unlikely that the public could be better informed about anything substantial related to their Pay TV or telecommunications providers in terms of the details of this notification.

5 THE PUBLIC DETRIMENT OF THIS NOTIFICATION

Should the parties to this notification continue to receive immunity from the third-line forcing provisions of the *Trade Practices Act 1974*, it will be to the detriment of regional Australia and the prospects for enhancing or in many cases initiating or stimulating any competition in Pay TV and more specifically telecommunications services well into the future.

As mentioned previously, the market dynamics of regional Australia insofar as the competitive marketplace is concerned is quite different to the Australian capitals and the ACCC should not make the mistake of allowing Telstra use the arguments it made in its submissions in 2002 to support its position in regional Australia.

In Pay TV, there is not and has never been any level of competition in the regional markets serviced by Austar. In instances where competitors have attempted to create competition (Neighborhood Cable and Northgate Communications) access to programming has been limited, drip fed over a considerable period or denied altogether. As a result of this anti-competitive conduct, Northgate was forced to rely on revenue from a limited telephony service but eventually failed and Neighborhood Cable derives the majority of its revenue from telecommunications services.

Were the parties to this notification to enjoy immunity to third-line forcing prohibitions, the public interest rather than being served, would, in fact, be undermined. Telecommunications competition is already at near monopoly status in even larger regional centres and Neighborhood Cable holds grave fears that the limited competitive forces that are at play in regional Australia will be further reduced or driven out altogether as a result of the effects of this notification should it be allowed to stand.

Not only does Neighborhood Cable, from its grass roots perspective of regional Australia, believe that the immunity from the conduct, the subject of the notification, will substantially reduce or eliminate competition especially in telecommunications services in regional Australia, it also believes that the conduct will have a detrimental flow-on effect with regard to research and development, innovation and technology development which so much work, time and money has been recently invested in, primarily by progressive local governments, across regional Australia. Technology centres, business incubators and regionally based investment are all at significant risk should the availability and supply of competitive telecommunications services be further concentrated forcing these initiatives, the skilled jobs and employment flowing from them, so desperately needed in regional Australia, to migrate to the capital cities.

Telstra's ability to cross-subsidise combined with its overwhelming power at all levels in the market makes the prospect of attracting, much less commercialising, any regionally based innovation significantly more difficult than if the immunity were to be revoked and Telstra were to be forced to behave in a more pro-competitive manner.

While recent Commonwealth Government enquiries into telecommunications services in regional Australia have reported that services have improved, Neighborhood Cable holds the view that should the ACCC grant this application for exemption there would be little to no incentive for any new investment in regional Australia for competition Pay TV or more importantly telecommunications services.

The real risk of doing irreparable damage to the fragile regional telecommunications market and the hard work of dedicated and committed organisations to attract investment in technology, infrastructure and employment which would most likely flow from the maintenance of this immunity is far too great a burden on regional Australia and the likely detriment far too real.

As the closing argument to this section, Neighborhood Cable would like the Commission to consider the unfair market position which Telstra will succeed in putting itself in, should this immunity fail to be revoked.

Until the last quarter of 2003 the Foxtel/Austar Pay TV service is transmitted via the Optus B3 satellite. The coverage of this satellite was known as the "banana beam" covering an area from Adelaide to Melbourne then up the eastern seaboard, following the coast to near Cairns, Qld. The satellite footprint services up to 700km inland in the south (South Australia, Victoria and southern New South Wales, tapering off to cover 500km inland from Sydney, 400km inland from Brisbane and 300km to 100km inland from Rockhampton north.

This "banana beam" left some 75% of Australia's landmass un-serviced.

However, the commissioning of Singtel Optus' new satellite, Optus C1 with a multiplicity of satellite transponders, 100% of the Australian landmass became a market for the delivery of Pay TV services.

How much better for Telstra could it be than to be in a position to bundle a Pay TV service, never before available, with telecommunications services over which in the vast majority of markets, Telstra also holds a monopoly or near monopoly.

The barrier to entry for any new competitor would be so great in these regions, which have arguably the greatest need for competitive services.

6 MARKET DEFINITION

In contrast to the 2002 notifications which dealt with markets and services which were of a similar size and range, this notification deals with an entirely different set of circumstances altogether. Markets, which this notification affects range in size from isolated communities of a few hundred (if that) residents to small cities up to 150,000 residents in size spread over a geographic area of 6,000,000 km².

This is an “all or nothing” notification – that is, the immunity is valid either for all of Australia or it is revoked for all of Australia. There is no market-by-market or State-by-State option. Even in Neighborhood Cable’s limited experience in 3 regional Victorian cities, each market (Mildura, Ballarat and Geelong) demonstrate entirely different dynamics and are without question distinct and separate markets with regard to uptake, usage, competitive environment, product mix and approach.

This notification affects all of the following markets across regional Australia:

- Group A less than 500 residents
- Group B 500 to 5,000 residents
- Group C 5,000 to 20,000 residents
- Group D 20,000 to 50,000 residents
- Group E 50,000 to 100,000 residents
- Group F more than 100,000 residents

Neighborhood Cable defines the above groupings as it has experience in the widely differing market dynamics itself of Group B, Group C, Group D and Group F type regional cities.

Within some or all of these markets (which populate 98% of Australia’s landmass and is the subject of this notification) exist a service provider or providers of the following services:

- Pay TV: Currently an Austar monopoly save 8,000 homes in Mildura and 32,000 homes in Ballarat;
- Local telephony: It is Neighborhood Cable’s experience that in its Victorian markets, no carrier other than Telstra can switch local calls in regional cities;
- Long Distance Telephony: If competitive forces exist, all long distance is carried over the Telstra network to the end user;
- Fixed-to-mobile: Available to all of regional Australia, end users are connected to Telstra infrastructure in terms of which Telstra earns revenue for all fixed to mobile calls regardless of terminating network;

- Mobile services: Available to the majority of Communities Group B and above. However, a large number of these communities, if they have mobile services at all, only have CDMA in which case, Telstra is the monopoly service provider (even if billed by Optus). Legislated competition in mobile services is proof that healthy, dynamic competitive telecommunications services can reach the vast majority of Australians should the will exist to ensure a competitive marketplace.
- Broadband services: Despite a growing number of “competitive” broadband service providers (spawned by a competitive backhaul market – in particular Comindico) relatively few of these have raised their gaze beyond Australia’s capital cities. Even those who have looked beyond capital cities only get as far as a point-of-presence (POP) in a Telstra defined Call Collection Area (CCA). Broadband connectivity, in the limited areas around the POP, to the end user is 100% the domain of the Telstra last mile. Broadband connectivity, as a direct result of the lack of competitive infrastructure investment, reaches a small percentage of regional Australia’s population. Should the immunity the subject of this notification stand, such investment in competitive last mile infrastructure, limited as it is under the current conditions will be eliminated in the future.
- Dial-up Internet: As a simple data over analogue phone connection, much of Australia is serviced by an arguably adequate service in a relatively competitive marketplace.

In the opinion of Neighborhood Cable the most likely market to be affected, and seriously affected adversely, will be telecommunications services. There is no change to the range or choice in Pay TV, so that market is unlikely to be affected.

Telecommunications services, on the other hand, which have the real potential to develop into a commercially viable, competitive, marketplace especially, and most importantly, in broadband services will be the hardest hit should the immunity not be revoked.

Customers will, in industry parlance, become much more “sticky” to Telstra and at this infant stage in the development of broadband services where, in many instances, Telstra is the only available provider, this has grave consequences for the future of competitive regional telecommunications.

7 CONCLUSION

It is the view of Neighborhood Cable, one of regional Australia's only competitive Pay TV and facilities based telecommunications carriers, that the Commission should withdraw the immunity from the third-line forcing provisions of the *Trade Practices Act 1974* as contained in the notifications N31277 and N31278 – Telstra Pay TV Pty Limited and Telstra Corporation Limited.

The competitive dynamics of even the largest markets in regional Australia to which this notification refers are not robust enough to support such market conduct at this infant stage of the development of either Pay TV or more importantly competitive telecommunications services.

Many of the hundreds of smaller markets which this notification impacts upon have little or no competitive activity which, when forced to take a Pay TV service which is already an entrenched monopoly, puts Telstra in a dominant, monopolistic position striking at the very core of the anti-competitive constitution which the Australia public rely upon through the provisions of the *Trade Practices Act 1974*. Further, such action would seriously adversely affect any decision by a competitive telecommunications service provider to invest either in regional markets or in the infrastructure required in regional markets to deliver competitive services.

As a nation, we have the expectation that robust marketplaces will be created through capitalistic market forces to deliver a range of efficient, safe and affordable goods and services in a dynamic, highly competitive marketplace. We see and enjoy the benefits of this expectation all around us – supermarkets, hardware, office supplies, hairdressers, builders, landscapers. Why should our communities expectations and service performance be lowered just because we are talking about Pay TV and telecommunications. The latter, being a critical part of our national fabric and international competitiveness should, in fact, be required to satisfy the very highest standards of competitive scrutiny. The application, if granted, would merely service to entrench the position of Telstra as the dominant, and possibly only, provider of telecommunications services to regional Australia and would make it extremely difficulty, if not commercially unsound, for any competitor to venture into the regional Australian telecommunications and Pay TV market.