Allens Arthur Robinson

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ABN 47 702 595 758

Level 28
Deutsche Bank Place
Corner Hunter and Phillip Streets
Sydney NSW 2000
Australia
T +61 2 9230 4000
F +61 2 9230 5333

Correspondence
GPO Box 50
Sydney NSW 2001
Australia
DX 105 Sydney

www.aar.com.au

David Hatfield
Director, Adjudication Branch
Australian Competition and Consumer Commission
GPO Box 3131
Canberra ACT 2601

Dear Mr Hatfield

Exclusive dealing notification N94674, lodged by FOXTEL Management Pty Limited - response to interested party submissions

I refer to your letter dated 23 June 2010.

FOXTEL Management Pty Limited (***FOXTEL***) provides the following responses to the submissions from interested parties. FOXTEL does not propose to respond to all matters raised in the submissions with which it disagrees but has focussed on issues where FOXTEL believes some confusion exists. This response will also respond to specific queries raised by the ACCC.

1. Public benefits

Availability of the Proposed Service on an unmetered basis

Some interested parties submitted that the claimed public benefit of BigPond subscribers receiving the Proposed Service on an unmetered basis would be available without the notified conduct as other ISPs would be prepared to also provide the service on an unmetered basis[1]. Accordingly, certain submissions claim that the exclusivity that forms part of the Proposed Service is not needed.

This argument does not, however, properly address the public benefits claimed in FOXTEL's submission. It is not Telstra's charges to end customers that are relevant. FOXTEL has confirmed that Telstra has agreed to unmeter the service even absent exclusivity. Rather the issue is Telstra's charges to FOXTEL. FOXTEL explained in section 4.3 of the submission accompanying its notification that Telstra has agreed only to waive certain charges to FOXTEL if the agreement is an exclusive one. Consequently, depending on the volume of content/data downloaded, FOXTEL plans to initially make the Proposed Service available at no or minimal additional data download cost to its subscribers as it plans to pass on to customers the benefit FOXTEL receives by Telstra waiving certain of its charges to FOXTEL.

[1] See for example Herbert Geer letter to ACCC, 18 June 2010, page 7

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Bangkok
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Further, certain submissions also argue that FOXTEL's claimed public benefit of unmetered access is not dependent on its exclusivity with Telstra as alternate ISPs already have plans that offer customers unlimited or very substantial data download allowances[2]. This argument is misleading as it compares existing plans offered by other ISPs and Telstra's agreement to offer the Proposed Service on an unmetered basis, to all BigPond subscribers with a plan of 1.5Mbs (with a data cap of 10Gb or more).

In order for a consumer to receive the benefit of unmetered access or a very substantial download allowance on a third party ISP plan, the customer must necessarily pay more than for plans with metered access or smaller download allowances. For example, an unmetered plan from Optus currently starts at $99 month when combined with a $59 a month mobile[3] and iiNet's 100GB plan starts at $129 per month[4] whereas Telstra's current 12GB plans start at $59.95 per month[5].

The submission from Quickflix argues that for any other supplier, or potential supplier, of audiovisual content over the internet, its competing services would be "metered" for Telstra BigPond customers unless Telstra elects otherwise[6]. This argument does not take into account that other suppliers or potential suppliers of services such as Quickflix are free to enter into similar "unmetered" arrangements with other ISPs, in competition with the Proposed Service.

The submission from Vodafone Hutchison Australia argues:

> No public benefits arise from BigPond customers not being charged an additional amount for the service. FOXTEL's submission does not consider the total cost of the BigPond connection and service delivery. FOXTEL has not demonstrated that the total cost of the broadband connection, including anticipated data downloads for FOXTEL's proposed service, will be lower by virtue of its proposed exclusive dealing arrangement with Telstra.

It is not necessary in order for FOXTEL to establish public benefit that it must prove that broadband costs will be **lower** as a result of the Proposed Service. The Proposed Service will result in BigPond customers receiving content on an unmetered basis and FOXTEL subscribers receiving content at no or minimal charge. The Proposed Service will, therefore, provide increased value for the customer, which will clearly be a public benefit.

Finally, it is not relevant whether there may be additional or other public benefits from alternate arrangements. The test in s93(3A)(b) of the *Trade Practices Act 1974* (Cth)(***TPA***) by which the ACCC is bound to consider FOXTEL's notification is whether:

> the likely benefit to the public from the conduct or the proposed conduct will not outweigh the likely detriment to the public from the conduct or proposed conduct.

[2] See for example Submission of AAPT to ACCC, 4 May 2010, page 6; Submission of Optus to ACCC, 18 June 2010, page 6

[3] http://personal.optus.com.au/web/ocaportal.portal?_nfpb=true&_pageLabel=Template_woRHS&FP=/personal/bundles/broadbandmobile&site=personal

[4] http://www.iinet.net.au/broadband/plans.html

[5] http://www.bigpond.com/internet/plans/adsl/plans-and-offers/

[6] Letter from QuickFlix to the ACCC, 18 June 2010, page 2

For the reasons given in the submission accompanying its notification, FOXTEL's letter to the ACCC dated 26 May and this letter, FOXTEL believes that the public benefits that arise from the third line forcing conduct involved in FOXTEL providing the Proposed Service outweigh any public detriment.

Increased choice for consumers

The submission from Herbert Geer argues that the Proposed Service will not result in an increase in consumer choice for content. FOXTEL did not make such a submission. FOXTEL submitted in the submission accompanying its notification that:

> The Proposed Service will be a new **service** to be offered by FOXTEL to subscribers. Accordingly, it will provide subscribers with increased choice **for the acquisition of content.**[7]

Accordingly, the Herbert Geer submission confuses FOXTEL's claim about an increased choice of service by which content is delivered, with an increased choice of content. The Proposed Service will also include additional content (which FOXTEL acquires on a non-exclusive basis) such as library content which is not currently available under the FOXTEL service. The fact that the content to be made available via the Proposed Service is content that FOXTEL purchases on a non-exclusive basis (and is therefore available to others), is one of the main arguments made by FOXTEL as to why the Proposed Service will not result in public detriment in the market for the retail supply of audiovisual content. In addition, the Proposed Service will offer a new, on-demand, way of accessing content.

2. Claimed public detriments

Customer churn towards Telstra's bundled plans

The Herbert Geer submission claims:

> Telstra's prime motivator is to entice Foxtel subscribers to switch from other ISPs to Telstra BigPond for their broadband. Once customers are lured across to Telstra BigPond, they will be locked in to lengthy bundled contracts for pay TV, broadband and often also telephony. Increasing the cost of disengagement will reduce customer willingness to churn to an alternative supplier, regardless of how uncompetitive the Telstra access service is.[8]

As FOXTEL has noted above and in its previous submissions, the Proposed Service will not be the exclusive source of the content made available and other ISPs will be free to obtain this content through other suppliers. Therefore customers will be able to choose between the different sources of content and will not be forced to obtain content through the Proposed Service if it does not suit their needs.

[7] Submission in support of notification by FOXTEL Management Pty Limited in relation to proposed third line forcing conduct, 4 May 2010, page 5

[8] Letter from Herbert Geer to ACCC, 18 June 2010, page 8

A number of submissions question why access to additional content cannot also be provided over the existing FOXTEL network.[9] FOXTEL is unable to offer the Proposed Service itself due to capacity restraints.

The Proposed Service will foreclose Telstra's ISP competitors from accessing FOXTEL's content

As FOXTEL has noted above and in its previous submissions and contrary to TransACT's submission[10], the Proposed Service will not be the exclusive source of the content made available. Accordingly, it is impossible for FOXTEL to foreclose Telstra's ISP competitors from having access to this content as ISPs will be able to either access this or similar content themselves or reach agreement with other content aggregators in order to do so.

The Proposed Service will substantially lessen competition

Optus in its submission argues that the consequences of the Proposed Service will be:

(a) a reduction in customer choice;

(b) increased prices for customers accessing broadband and voice services; and

(c) a reduction in innovation[11].

FOXTEL considers that each of these arguments is incorrect as the Proposed Service:

(d) will be a new service that will provide subscribers with increased choice for the acquisition of content;

(e) will be offered by Telstra on an unmetered basis and therefore cannot result in increased prices for customers; and

(f) will not reduce innovation as the Proposed Service is the result of innovation and can only encourage other ISPs to offer similarly innovative products, as iiNet and Internode are with Fetch TV.

Level of service differentiation

Macquarie Telecom in its submission claims that the Proposed Service will result in an increase in the level of Telstra's service differentiation and that this is a concern as competitive markets are characterised by a low level of product and service differentiation. Macquarie Telecom claims that Telstra is able to differentiate itself because of the content offering and unmetered data download offered as part of the Proposed Service.[12]

This argument is misleading for two reasons:

(a) as Macquarie Telecom itself recognises in its submission,[13] the content to be offered by FOXTEL as part of the Proposed Service is non-exclusive, accordingly,

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[9] Letter from Herbert Geer to ACCC, 18 June 2010, page 6; Submission from AAPT to ACCC, 4 May 2010, page 2; Submission from Optus to ACCC, 18 June 2010, page 2

[10] Letter from TransACT to ACCC, 18 June 2010, page 6

[11] Herbert Geer also makes this argument in its submission, Letter from Herbert Geer to ACCC, 18 June 2010, page 3

[12] Letter from Macquarie Telecom to ACCC, 18 June 2010, page 4

[13] Ibid.

Telstra will be unable to differentiate itself from its competitors on this point if they choose to innovate and also offer content or form associations with content aggregators which will enable the content aggregator to offer content on an un-metered basis; and

(b) submissions from other ISPs make clear that they also provide unlimited or very substantial data download allowances. Accordingly, dependent on the pricing offered by these ISPs, Telstra may in the future be unable to differentiate itself from its competitors on this point as well.

Barriers to entry

Certain interested party submissions claim that the Proposed Service will result in an increase in barriers to entry for IPTV providers. This is incorrect. As FOXTEL pointed out in the submission accompanying its notification, there are minimal barriers to entry as the majority of online content is acquired by FOXTEL on a non-exclusive basis. The fact that new entry is occurring clearly supports FOXTEL's submission.

FOXTEL's submission in this regard is supported by the June 2010 report of the Australian Communications and Media Authority, *IPTV and internet video delivery models, Video content services over IP in Australia* (***ACMA Report***). The report states:

> In addition, the number of participants in content distribution has increased as other industries have entered the market. For example, online retailers such as Amazon.com are now providing video on-demand services.

Herbert Geer submit that the Proposed Service will weaken the ability of prospective pay TV market entrants to gain a foothold in the pay TV market and that this would be cured by FOXTEL offering the service to all subscribers with internet access, regardless of their ISP provider[14]. However if FOXTEL were to offer the Proposed Service to customers of all ISP providers, this may discourage other ISP providers from seeking partnerships with FOXTEL's competitors or potential new entrants in the relevant content market, thereby actually reducing competition in these markets. As FOXTEL has submitted, FOXTEL does not consider the Proposed Service to be a subscription TV service, rather an ancilliary service which gives subscribers the ability to access content on an on-demand basis.

3. Appropriate market definition

Certain interested party submissions claimed that FOXTEL's definition of the relevant markets is incorrect. FOXTEL submits that ultimately it does not matter how the ACCC defines the market.

If the market is defined as a subscription television market (which is incorrect in FOXTEL's view), there is no effect on that market as the service is not subscription television, but an ancilliary service allowing content to be delivered on a point-to-point basis via the internet which could be provided by a number of providers. At the very least, as the Proposed Service is delivered over the internet, any service which delivers content to a TV or to a

[14] Letter from Herbert Geer to ACCC, 18 June 2010, page 8

computer (which can be connected to and viewed on a TV) must be included in the market. Such a conclusion is supported by the ACMA Report.[15]

If the market is broader then there are a number of players in the market as FOXTEL has outlined in its submission.

4. Relevance of potential entrants

The submission from Herbert Geer states:

> Our Clients submit that future entrants, whether likely or not and whether launching in the market for the retail supply of subscription television services or the broader market of the retail supply of audiovisual content, should be discounted by the ACCC in its consideration of Foxtel's notification... [16]

This argument is contrary to principles underlying the TPA and should be disregarded. For example, s46(3)(a) of states:

> In determining for the purposes of this section the degree of power that a body corporate or bodies corporate has or have in a market, the court shall have regard to the extent to which the conduct of the body corporate or any of the bodies corporate in that market is constrained by:
>
> (a) competitors, **or potential competitors**, of the body corporate or any of those bodies corporate in that market... (our emphasis)

Similarly, s50(3) of the TPA lists as three factors that the Court must take into account in determining whether an acquisition would have the effect of substantially lessening in a market:

(a) the actual **and potential** level of import competition in the market; and

(b) the height of barriers to entry (to assess the ease with which a potential competitor could enter the relevant market and constrain the merged firm);

(c) the extent to which substitutes are available in the market **or are likely to be available in the market**.

Paragraph 3.14 of the ACCC Merger Guidelines also states that:

> Section 50 [of the TPA] requires a **forward-looking analysis** into the effects or likely effects of a merger, since analysis is generally conducted before the impact of a merger on competition can be observed. The ACCC therefore focuses on **the foreseeable future (generally within one to two years)** when considering market definition and each of the merger factors to determine whether a substantial lessening of competition is likely to occur.

FOXTEL submits this is also the relevant time in which to assess the effects of the Proposed Service.

[15] ACMA Report, pages 11 and 33-35

[16] Herbert Geer letter to ACCC, 18 June 2010, page 3

5. NBN

Certain submissions argued that the Proposed Service will allow Telstra to increase its market share in the market for the provision of broadband telecommunications services and that this will allow Telstra to obtain more advantageous terms from NBN Co than its competitors. Consequently, this will create a dominant position on the NBN for Telstra.

These arguments are misleading. They suggest that Telstra is the only ISP that is able to offer a service in connection with the Proposed Service in the period leading up to negotiations between NBN Co and ISPs and that Telstra will, therefore, have an unfair competitive advantage in its negotiations with NBN Co. FOXTEL submits Telstra does not have an unfair competitive advantage.

As stated in FOXTEL's submission accompanying its notification, the content to be supplied via the Proposed Service is non-exclusive. Accordingly, ISPs other than Telstra can easily acquire rights to the same content or enter into an arrangement with another content aggregator and offer a similar product to compete with the Proposed Service. Two recent examples are iiNet's and Internode's agreements to supply Fetch TV in Australia.

Accordingly, the Proposed Service, the Fetch TV service to be offered by iiNet and Internode and the offering of similar IPTV services, will provide each ISP with the same opportunity to increase their market share before they enter into agreement with NBN Co.

FOXTEL's submission in this regard is supported by Telstra's submission that:

> Optus has of its own election failed to innovate and differentiate its broadband services from its competitors in the Australian market, but instead competes predominantly on the basis of price. It is therefore unsurprising that, when faced with a competitor such as BigPond which is differentiating its services by offering additional features to subscribers such as unmetering of the Proposed Service, the reaction from Optus is to call on the Commission to prohibit the proposed innovation. Telstra's view is that, to the contrary, by allowing the Proposed Service to be supplied the Commission will be incentivising the development of competitive new broadband service features by other ISPs. The Proposed Service will be characterised predominantly by nonexclusive content which Optus and others are free to obtain for supply to their customers.[17]

6. ACCC queries

In your letter of 23 June 2010, the ACCC requested that FOXTEL respond to the following queries:

Confidential information

Several interested parties have requested access to the excluded information in the submission which accompanies FOXTEL's notification to the ACCC. The information relates to FOXTEL's proposed pricing and packaging for the Proposed Service. As FOXTEL is yet to finalise this information, FOXTEL continues to claim confidentiality over it and requests that the ACCC refrain from disclosing it to any interested party. FOXTEL

[17] Telstra Corporation Limited letter to the Australian Competition and Consumer Commission dated 18 June 2010

considers that this information is clearly commercially sensitive in nature. There is also a risk that the release of the information may have a price signalling effect.

In any event, FOXTEL does not believe that disclosure of the confidential information is necessary in order for third parties to provide submissions to the ACCC on the effect of the conduct.

Further information regarding the underlying "IP connectivity services" provided by Telstra to FOXTEL

The ACCC has sought a description of the underlying "IP connectivity services" provided by Telstra to FOXTEL in exchange for the "excess carriage charge". The services supplied by Telstra to FOXTEL in exchange for the excess carriage charge include carriage (either over ADSL, ADSL2, cable, fibre or other substitutable IP access technology depending on the customer).

The ACCC has also enquired as to whether FOXTEL intends to pass on the "excess carriage charge" to subscribers and if so in what proportion. There are no plans to pass on the excess data carriage costs at this stage.

Yours sincerely

Jacqueline Downes
Partner
Jacqueline.Downes@aar.com.au
T +61 2 9230 4850