A Submission by

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BROADCASTING INQUIRY SUBMISSION

Dear Professor Snape,

Thank you for the opportunity to comment on the Productivity Commission's Broadcasting Inquiry.

Telstra appreciates the significant challenge that reform of broadcasting regulation poses to government in an era of converging services across the information technology, media and communications industries.

Telstra recognises the key characteristics of convergence (evident at this stage) as being *enhanced competition*, but with heightened *uncertainty*.

Convergence is bringing about the broadening of markets, as traditional industry and market boundaries erode and firms from hitherto separate industries compete in new markets.

Uncertainty is evident in respect of consumer demand, commercial viability, including appropriate business models, technological developments and regulation.

In this context, the need for technology neutral, competitively neutral regulation is clear. Asymmetric regulation is less necessary and more harmful, serving only to tilt the playing field in a distortionary manner. Regulation of converging industries in a neutral manner will facilitate the enhancement of competition that convergence brings, leading to greater

efficiency, innovation and investment, and ultimately consumer benefit, than can be provided by asymmetric regulation.

Telstra sees four regulatory principles as essential in creating a regulatory environment for convergent services which support these desirable market characteristics. These principles are the following:

1. Regulation should be technology neutral;

2. Regulation of a service should be neutral as to who is providing the service;

3. Regulation should address only the providers of services which, because of their characteristics, it is necessary to regulate to achieve the desired policy goal; and

4. Regulation should, to the extent possible. be light-handed in nature to ensure that firms in the emerging convergent services market have sufficient commercial flexibility and regulatory certainty to invest and to innovate.

Implementing these principles clearly requires a forward-thinking regulatory approach which can provide the sufficient flexibility and freedom required for convergent services to develop, acknowledging the current uncertainty in relation to business models, technologies and markets. There is a need for policy-makers and regulators to recognise and take account of the market-broadening effects of convergence in their policy and decision-making.

Subsequent to this submission Telstra will provide a paper dealing with the economic issues associated with the regulation of broadcasting, in response to the paper by Associate Professor Joshua Gans, submitted to this Inquiry by John Fairfax Holdings.

Telstra looks forward to providing further input into this important policy process in the future. If you have any queries on the submission please call Jane Fowler on 02 9298 4858.

Yours sincerely

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Productivity Commission

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BROADCASTING INQUIRY

A Submission by Telstra Corporation Limited

EXECUTIVE SUMMARY

Telstra is pleased to provide its submission to the Productivity Commission's Broadcasting Inquiry. This submission focuses on two areas raised in the Discussion Paper which are of principal interest to Telstra. These are:

- the need for technology neutral, competitively neutral regulation of converging markets, and the corresponding inappropriateness of asymmetric regulation; and
- the need to acknowledge, in regulatory policy and practice, the market-broadening effect of convergence.

The key characteristics of the convergence era are enhanced competition in markets which are more broadly defined as a result of contestability from non-traditional market participants, yet at the same time tremendous uncertainty in respect of demand, new technology, regulation and business models.

These characteristics must be understood by regulators and regulatory policy makers, to ensure that the convergent services industry develops in Australia, supported by a regulatory framework which simultaneously promotes the competition, innovation and investment necessary to ensure that consumers benefit through the availability of converged services.

In this context, Telstra articulates four principles for the regulation of convergent services. These are:

1. Regulation should be technology neutral;
2. Regulation of a service should be neutral as to who is providing the service;
3. Regulation should address only the providers of services which, because of their characteristics, it is necessary to regulate to achieve the desired policy goal; and
4. Regulation should, to the extent possible, be light-handed in nature to ensure that firms in the emerging convergent services market have sufficient commercial flexibility and regulatory certainty to invest and to innovate.

If the regulation of converged services remains asymmetric, firms in convergent industries will bring the constraints of such regulation derived in the context of their traditional industries when this is clearly inapplicable to their activities in broader, convergent markets. Asymmetric regulation is anti-competitive because it confers an arbitrary and artificial regulatory impost or advantage on some firms or classes of firms, but not on others. While competition seeks to ensure the most efficient firms succeed, asymmetric regulation effectively tilts the playing field so that the most successful firms may not be the most efficient. This ultimately disadvantages consumers by depriving them of the benefits of competition.

Convergence leads to the redefinition of markets and in general to the dilution of market power, as the process of convergence itself is one of market and industry restructuring. Regulatory policy and practice in a convergent environment must take account of competition from non-traditional sources and the supply-side substitutability of new technologies when defining markets. The market analysis underpinning regulation and its application will need to be forward-looking, recognising in particular that the structure of converging markets is by its nature dynamic.

INTRODUCTION

Telstra welcomes the opportunity to contribute to the Productivity Commission's consideration of issues affecting the broadcasting industry in the context of its review of broadcasting legislation. Telstra understands that the Competition Principles Agreement, pursuant to which this Inquiry is occurring, specifies that any legislation which restricts competition should be retained only if the benefits to the community as a whole outweigh the costs, and if the objectives can be met only through restricting competition.

Telstra notes that the key task of the Commission's inquiry is to advise on practical courses of action to improve competition, efficiency and the interests of consumers in broadcasting services, with particular focus on balancing the social, cultural and economic dimensions of the public interest, having due regard to the phenomenon of technological convergence.

In Telstra's view, the Commission has a significant task at hand. A key issue for consideration in this Inquiry will be what should be the goals of broadcasting regulation in an era of convergence.

It is questionable whether convergence is yet a key issue for the broadcasting industry. This is not to say that convergence is not occurring; rather that its impact on the broadcasting industry is only beginning to be realised. Telstra agrees with the Commission's comment that:

> *"Media owners are ... positioning themselves for this multimedia era. There are new alliances between traditional media (FTA television and radio, and newspapers) with new media (such as internet and subscription television), and telecommunications providers (including mobile telephony and multimedia)."*

The question is whether the broadcasting industry will be protected from the competitive forces of converging industries pursuant to regulatory policies similar to those which underlie the broadcasting legislation which today places some limitations on competition within traditional broadcasting. And will non-broadcasters be given the same opportunities in broadcasting as are presented to broadcasters in other converging industries?

Telstra is not, in its own right, a broadcaster, as that term is currently understood in the context of the definition of "broadcasting services" in the *Broadcasting Services Act 1992* (BSA). However, Telstra has a number of roles in the broadcasting industry, as well as telecommunications and converging industries:

1. Telstra is a provider of Internet access and on-line services, including services which in a number of respects may be said to have the "look and feel" of broadcasting to varying extents;

2. Telstra owns 50% of FOXTEL, the holder of a subscription television broadcasting licence;

3. Telstra is the owner and operator of telecommunications infrastructure which is used to distribute broadcasting, convergent and other communications services.

Accordingly, Telstra has a keen interest in convergence and the regulation of converging markets and services. Telstra is, in general, a proponent of competitively neutral legislation, to ensure that both new and incumbent firms in converging sectors experience a "level playing field" to the greatest extent possible.

BACKGROUND

Broadcasting Policy

The policy basis for the *Broadcasting Services Act 1992* is set out in section 4 of the Act:

> *Regulatory policy*
> *SECTION 4.*
> *(1) The Parliament intends that different levels of regulatory control be applied across the range of broadcasting services according to the degree of influence that different types of broadcasting services are able to exert in shaping community views in Australia.*
> *(2) The Parliament also intends that broadcasting services in Australia be regulated in a manner that, in the opinion of the ABA:*
> *(a) enables public interest considerations to be addressed in a way that does not impose unnecessary financial and administrative burdens on providers of broadcasting services; and*
> *(b) will readily accommodate technological change; and*
> *(c) encourages:*
> *(i) the development of broadcasting technologies and their application; and*
> *(ii) the provision of services made practicable by those technologies to the Australian community.*

Much of the broadcasting regulation under the BSA which has the effect of constraining competition does indeed find its genesis in the policy assumption that broadcasters are afforded the power to shape community views, which power needs to be constrained; for example, ownership and control regulation. Numerous provisions in the BSA reflect implicit choices in relation to the balance between public interest considerations and the financial interests of broadcasters; for example, content regulation, limitations on the number of commercial broadcasting licences, access requirements in relation to satellite equipment.

Competition Law

The competition provisions in Part IV of the *Trade Practices Act 1974* (TPA) apply generically to all markets, as defined in the Act, in Australia. In summary, they restrain mergers and acquisitions which would have the effect of substantially lessening competition in a market (section 50); they prevent anti-competitive agreements (section 45); they prevent the practice of anti-competitive exclusive dealing, including third line forcing (section 47); they prohibit the misuse of market power (section 46). These provisions effectively prevent conduct which could damage competition in any market in Australia.

Part IIIA of the TPA provides for access to essential facilities in certain circumstances. This Part was introduced to facilitate the liberalisation of utilities, such as electricity and gas.

Telecommunications Regulation

In July 1997 telecommunications industry-specific competition provisions were incorporated into the *Trade Practices Act 1974*. Part XIB regulates conduct in "telecommunications markets" by reference to the competition provisions in Part IV of the Act, but with additional regulation in the form of the "competition rule", which introduced a broad "effects test" and additional enforcement powers via the issue of a "competition notice". Part XIC regulates access to telecommunications services in a manner which differs in several respects from the essential facilities access regime under Part IIIA of the Act.

In short, the telecommunications industry is singled out under the Act for industry-specific competition regulation. The policy basis for this is ostensibly pro-competitive.

"Telecommunications market" is defined in section 151AF of the Act:

> *"**151AF Telecommunications Market***
> *For the purposes of this Part, a **telecommunications market** is a market in which any of the following goods or services are supplied or acquired:*
> *(a) carriage services*
> *(b) goods or services for use in connection with a carriage service;*
> *(c) access to facilities."*

This definition, in particular sub-section 151AF(b), has the effect that a broad range of services distributed using telecommunications services are potentially supplied in a "telecommunications market".

The "competition rule", established by section 151AK, is that a carrier or carriage service provider must not engage in anticompetitive conduct. "Anti-competitive conduct" is defined in section 151AJ by reference to two circumstances:

1. Pursuant to sub-section 151AJ(2):
   "A carrier or carriage service provider engages in anti-competitive conduct if the carrier or carriage service provider:
   (a) has a substantial degree of power in a telecommunications market; and
   (b) takes advantage of that power with the effect, or likely effect, of substantially lessening competition in that or any other telecommunications market."

2. Pursuant to sub-section 151AJ(3), if the carrier or carriage service provider engages in conduct which contravenes sections 45, 45B, 46, 47 or 48 of the Act and that conduct relates to a telecommunications market.

Section 151AL empowers the Australian Competition & Consumer Commission (ACCC) to issue a competition notice stating that a specified carrier or carriage service provider has contravened, or is contravening, the competition rule.

The effect of such a notice is that in any proceedings arising out of Part XIB, it constitutes prima facie evidence of the matters set out in it. Thus if the Commission institutes proceedings to recover fines (up to $10 million a day; plus $1 million per day that the conduct continues or a third party institutes proceedings, the carrier or ISP against whom the competition notice was issued bears the onus of proof.

Proposed amendments to Part XIB announced last week will provide for two different types of competition notices. A Part A competition notice could be issued more quickly than is currently the case - it need not specify the precise conduct in breach of the competition rule - yet would constitute sufficient grounds for ACCC proceedings, although it would not constitute prima facie evidence of its contents. A Part B notice would set out the details of the contravention, and have the evidentiary effect which competition notices currently have.

Part XIC of the Act imposes access obligations on carriers and carriage service providers in respect of "declared services". The ACCC can declare carriage services and services which facilitate the supply of a carriage service if to do so would promote the long term interests of end-users (LTIE). Pursuant to section 152AB, the LTIE is assessed by reference to whether declaration will result in the achievement of the following objectives:

1. the objective of promoting competition in markets for carriage services;
2. the objective of achieving any-to-any connectivity in relation to carriage services that involve communication between end-users;

3. the objective of encouraging the economically efficient use of, and economically efficient investment in, the infrastructure by which listed services are supplied.

The effect of declaration is that, in the absence of commercial agreement, to the extent that the ACCC has not accepted as reasonable an access undertaking which sets out the terms and conditions of access, the ACCC may determine the terms and conditions of access by arbitration (section 152AY). This may include application of the ACCC's Access Pricing Principles.

Convergence

The phenomenon of convergence has been described in many ways.

The European Commission in its *Green Paper on Convergence*[1] ("EC Green Paper"), defined it thus:

> *"The ability of different network platforms to carry essentially similar kinds of services or the coming together of consumer devices such as the telephone, television and personal computer."*

The Green Paper suggests that convergence may occur at four basic levels:
1. Technology and network platforms;
2. Industry alliances and mergers;
3. Services and markets; and
4. Policy and regulation.

It should be acknowledged that policy and regulation may be responsive to, or may drive, convergence.

Andersen Consulting illustrates convergence diagrammatically. The "pre-convergence world" is represented by the separate spheres of the media and entertainment industry, the communications industry and the computing industry. The "'convergent industry' world" sees these spheres intersecting, with the availability of services such as video on demand, interactive multimedia, electronic commerce, CD ROM and multimedia network equipment[2] represented in the overlap.

Cutler & Company's working definition is as follows:

> *"Convergence is the progressive integration of the value chains of the information and content industries - telecommunications, posts, broadcasting, print, multimedia and data processing - into a set of linked economic markets and a single value chain based on the use of distributed digital technology."*[3]

In Telstra's view, convergence occurs when developments in two previously independent industries lead to each developing similar and hence competing product ranges. This implies a significant broadening of the converging markets. In place of, or in addition to, multiple industries, a new arena emerges in which participants of the previously separate industries compete. Mergers aside, this must increase competition, and may even enable competition where it once did not exist. Since each industry typically brings with it quite different strengths, technologies and methods of operation, the resultant competition can be very robust.

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[1] European Commission, Green Paper on the Convergence of the Telecommunications, Media and Information Technology Sectors and the Implications for Regulation, December 1997, www.ispo.cec.be/convergencegp
[2] Andersen Consulting, *Convergence - Myth or Promise?*, 1999
[3] Dr T Cutler, "The Need for a Convergence Policy and Next Generation Regulation", in DCITA Communications Research Unit, *1998 Communications Research Forum Papers*, p1.

While definitions and concepts of convergence vary, in Telstra's view the consequences of convergence are apparent in the services that are being and will be supplied to consumers. Convergence of material importance is now widely recognised to be taking place in the communications, broadcasting and content-provision industries:

- Existing services may be supplied via new media. Essentially there is technology substitutability. For example, in addition to copper wire, two-way carriage may now be effected via new infrastructure such as HFC, and to a limited extent via satellite and terrestrial wireless, new bandwidth on existing infrastructure created by technologies such as xDSL, and hybrid technologies, such as terrestrial wireless and satellite in conjunction with a wireline reverse path (copper or HFC). Another example is in content markets, where electronic games may be provided via chip-based technologies, disk and tape-based technologies or via online services, or a combination of the above.

- Existing services may be enhanced. For example, the conversion from analogue to digital television, the availability of increased bandwidth for Internet access together with streaming technology, enhance the quality and variety of services provided to consumers.

- New services may be offered. These new services may resemble existing services supplied in traditional markets, but the use of new distribution mechanisms or the enhancement of the service are so significant that they are regarded as a new "converged" services, supplied in broader, converged markets. Datacasting is a key example. It is likely to resemble online services in some respects, but will be viewed on a television.

Convergence is significant in the context of this Inquiry because it involves the blurring of industry boundaries - such as that between broadcasting and on-line services - and enables firms from traditionally separate industries - such as broadcasting and telecommunications - to compete in converged markets. For this reason, convergence presents major regulatory challenges in the context of existing, industry-specific regulation. The inevitable question is whether existing regulation, such as the broadcasting legislation the subject of this Inquiry, premised as it is on traditional industry boundaries and clear distinctions between spheres of activity, is necessary or appropriate in the context of convergence.

Characteristics of the Convergence Era

In Telstra's view, the key characteristics of the convergence era are enhanced competition and heightened uncertainty.

Convergence Enhances Competition

Market convergence typically increases competition, and may enable competitive markets where they once did not exist.

A consequence of convergence is that firms originating in different industries may compete against one another in convergent markets. By increasing the scope for market entry, convergence renders existing markets more contestable and more competitive, broadening market definitions and generally reducing the market power of incumbent firms. Importantly, this brings the benefits of competition - new or enhanced services and lower prices - to consumers.

Examples - Competition-Enhancing Effects of Convergence

Convergence between one-way broadcasting and two-way communications provides a very sharp example of how convergence increases competition. Only a few years ago two-way broadband communications had very high start up costs and were almost uniquely supplied by telcos. Residential and small business customers were almost excluded from this market. ISDN connections were the closest such customers could get to high bandwidth access, and even in this relatively low bandwidth case, prices were high. Most other methods of transport either had very low bandwidth—copper wire—or were uni-directional—HFC cable and satellite delivery. In 1999, high bandwidth two-way connections are available over copper wire through various DSL technologies, HFC cable, and via terrestrial wireless. Geo-stationary satellites in conjunction with ordinary telephony provide similar services. As a result, prices have fallen and demand surged. There are now approximately half a million cable modem subscribers in the U.S. and 100,000 DSL customers, where there were virtually none two years ago. DTH-based internet access is now into its second year, and tens of thousands of subscribers gain access to the internet via various wireless solutions at bandwidths that exceed the 64 kb/s telephone circuit. This, however, is only the beginning of the convergence on high bandwidth two-way transport. Low earth orbiting satellite systems are expected to supply extremely high two-way bandwidth within five years. Both Hughes and Teledesic promise high bandwidth satellite links by the year 2003. At the same time the extra bandwidth provided by digitising television signals will make, in conjunction with a phone line, interactive television possible.

Other forms of convergence are also taking place within the existing two-way communications market. Mobile telephony, once seen as a market sharply distinct from fixed line service increasingly competes with the latter. In Finland and Sweden mobile penetration has increased to over half the population, and there and in a number of other places, has begun to erode fixed line penetration. More interestingly, BT Mobilenet announced a new product that combines the mobile handset with fixed line service. In both the U.K. and the U.S. many cable companies provide telephone service over HFC cable. In the U.S., after less than two years of commercial operation, cable telephone subscribers number in the hundred thousands. Internet telephony also provides another, if marginal, form of convergence, in this case between traditional circuit based and IP forms of transit.

Changes in transport are generating other sources of convergence, and a broader range of competitors in a range of industries. For example, traditionally software in the form of recordings or computer programs has been delivered on physical media (video tapes and disks, cassettes, CDs, DVDs, floppy disks and cartridges). Similarly, the printed word has been traditionally delivered by newspapers, books and magazines. The Internet, in conjunction with wide-spread access to high bandwidth, represents a direct competitive threat to such forms of delivery. This in turn is sending traditional media providers scurrying to get their material on line—another form of convergence. Web-page designers are hired by and compete with traditional media suppliers. But to a large extent web-designers did not come from and are not part of traditional media groups. They represent a new source of content supply. Because different delivery methods have different cost structures, and because different cost structures determine content as well as form, new experts have come into being that can challenge traditional experts. Some things are easier to display on paper than on screen. Designing an effective web-site is a very different skill to designing an effective magazine. Picking and choosing songs is easier to do via downloading than when purchasing a discrete piece of hardware that can be read by the eye or a computer. New technologies, new skills, new power bases, but all in the market for the glance of an eye. A third form of convergence in the content industry is an increasing emphasis on interactive entertainment. As high bandwidth two-way pipes become increasingly accessible, distributed electronic entertainment is becoming increasingly interactive. On-line business magazines allow interactive stock

market analysis, and discussion forums. Two-person at-home game machines are challenged by home computer accessed network-based games with hundreds of players. Web-television means the television itself can now serve two functions—the traditional broadcast monitor, and, in some cases simultaneous, access to the web.

As these examples demonstrate, convergence essentially leads to the redefinition of markets as the process of convergence itself is one of market and industry restructuring. Clearly regulatory policy and practice in a convergent environment must take account of competition from non-traditional sources and the supply-side substitutability of new technologies when defining markets. The market analysis underpinning this will need to be forward looking, recognising in particular that the structure of converging markets is by its nature dynamic.

Convergence Heightens Uncertainty

Convergent businesses face high levels of uncertainty, which is clearly discernible in Australian converging markets:

- *Demand uncertainty* has been most apparent in the markets in which online services are supplied. Firms providing these services, including Telstra, are still endeavouring to fathom what content or applications will succeed. In the area of electronic commerce, it is becoming clear that applications must be useful to consumers or efficiency-enhancing for businesses, but there is no certainty as to what types of electronic applications will best meet these criteria. Demand uncertainty for convergent services is illustrated by a 1999 Ovum report estimate that the number of digital television subscribers in Australia in the year 2000 to be only 103,000 and to interactive services, only 5,000.[4]

- Convergence is characterised by the deployment of new technologies, in that existing technologies may be used for new services (eg. the PSTN for the provision of xDSL) and new investment is occurring in new infrastructure - eg. HFC cable, electronic commerce platforms. Firms investing in these technologies take *technology risks*, in terms of choice of functionality, implementation and viability, often in the absence of any significant precedent or established standards. This adds up to significant commercial risk.

- Added to this is *regulatory uncertainty*. Regulation of a firm generally reduces commercial flexibility and is a factor for consideration in investment decisions. Uncertainty as to whether and how a firm will be regulated in its provision of new services increases the risk associated with investment in such services. For example, the investment by Optus Vision and Telstra Multimedia in HFC cable rollouts would not have occurred but for the assurance, through the July 1996 *Telecommunications (Carrier Associate Class Licence) Direction* which ensured minimal access obligations in relation to cable until July 1997.

- All of the above amount to significant *commercial uncertainty*. In the case of online services, the risk is enhanced by the absence of uniform profitable business models. While there is clear commercial potential in the Internet, what is not clear is precisely how to make money. Will the revenue model be based on the provision of access, content or advertising, or a combination of these? Currently around the world, no consistent, profitable, business model has yet emerged, and significant experimentation is occurring with new models appearing regularly (eg. free ISPs in the UK).

- This underlies deep uncertainty about where profit will be claimed in the emerging, but as yet poorly understood, value-chains of production. A heavy investor in the wrong parts of the chain may find their asset is used, but profit is claimed by a supplier somewhere else in the chain. As a result, vertical integration as a means of internalising such an externality becomes very attractive. However, if regulation

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[4] Ovum, *Ovum Forecasts, Telecoms, the Internet and Digital TV*, 1999, p 159.

puts constraints on vertical integration then the capacity of investors to ensure they earn a return on their investment is reduced, and too little investment takes place.

REGULATORY PRINCIPLES FOR THE CONVERGENCE ERA

A consequence of convergence is that firms originating in different industries may compete against one another in convergent markets. When industries collide, policy must be re-evaluated. Old rules and approaches may no longer have the effects originally intended.

Convergence implies a greater scope to rely on the market, rather than regulation, since it broadens fields of competition. By increasing the scope for market entry, convergence renders existing markets more contestable and more competitive. But if competition is to flourish, convergence also requires a harmonising of regulation across the relevant merging industries. The competition-enhancing effects of convergence are likely to be hindered by the distortionary effect of asymmetric regulation.

A fundamental principle of industry regulation is that all market participants should be treated alike - the level playing field. Legal structures should not treat firms differently because of their industry of origin, or because of characteristics associated with their originating industries - whether this be a reliance on particular technologies, corporate structure, business models or marketing approaches. If industries, once separate, but now converging, are each regulated differently, then competition is distorted. Firms in the most favoured industries do better than equally efficient firms elsewhere. In contrast, competition pushes the most efficient firms to the fore, regardless of origin.

In an era of convergence, the key regulatory principle must be competitive neutrality.

Remove Asymmetric Regulation

Firms competing in converging markets will bring with them strengths and competencies which, chiefly, reflect the nature and extent of their traditional business. These differing strengths and competencies will also reflect differing degrees of horizontal and vertical integration and the differing nature and extent of their economies and diseconomies of scale and scope. One thing that those firms should not bring with them, however, is the constraints of asymmetric regulation derived in the context of their originating industry, which are inapplicable to their activities in converging markets because those markets are differently defined.

The ability of such a variety of firms to enter markets and compete in them, subject to the constraints imposed by general competition law under the *Trade Practices Act 1974* (TPA), is entirely consistent with an efficient, competitive market. Such a market is one that produces a diversity of product offerings at competitive prices. Such is the potential of converging markets.

Asymmetric regulation is literally anti-competitive because it confers an arbitrary and artificial regulatory impost or advantage on some firms or classes of firms but not others. Whereas competition seeks to ensure that the most efficient firms succeed, asymmetric regulation tilts the playing field such that the most successful firm may not be the most efficient.

All regulation is in some sense distortionary. But regulation distorts least when it treats all firms and all technologies in a market in a broadly neutral manner.

Industry-Specific Regulation - Telecommunications

Telstra believes it is inappropriate in an era of convergence that telecommunications is subject to industry-specific competition regulation. It is the only industry with a specific additional layer of competition law overlaying the generic Part IV of the TPA.

Hypothetical - On-line Services - Competition Rule

Assume that two firms compete in the market in which on-line services are supplied. Both provide infotainment-type content that is accessed by their customers on the Internet. Firm A is a telecommunications carrier, while Firm B is the owner of substantial media assets which include content of the type which forms both of their on-line service offerings.

It seems likely that the market in which the Firms' on-line services are supplied is a telecommunications market. Assume that in this market - call it Market X - neither Firm A nor Firm B could be said to have market power. Assume also that Firms A and B both have market power in their traditional markets - Firm A in telecommunications markets and Firm B in a media market, for example the market in which Sydney metropolitan daily newspapers are supplied.

Say Firm A wishes to compete aggressively in Market X, and undertakes a strategy whereby it cross-subsidises its on-line services from telephony revenues. Similarly, assume Firm B's competitive strategy in Market X is funded by cross-subsidies from its print media business. This conduct is not per se illegal. Assuming that in instance it constitutes a use of market power in one market, it would only be a breach of section 46 of the Trade Practices Act if the conduct was motivated by a purpose proscribed by sub-section 46(1) - essentially to deter or damage competition or a competitor in Market X.

However, while the purpose of the conduct is rooted in fierce competition between Firms A and B, assume that the effect of the conduct is that it is more difficult for other firms to enter Market X. This could create a situation where Firm A, being a firm with market power in a telecommunications market, has breached the competition rule. Firm B, which may enjoy equivalent or greater power in its traditional media market, is not subject to the competition rule. Thus the Commission may be empowered to issue a competition notice against Firm A's illegal conduct, but the same conduct, with the same purpose and effect, by Firm B is legal and goes unsanctioned. If Firm B were disposed to regulatory gaming, the Commission's investigation may even be prompted and assisted by Firm B.

It is clear from this example that industry-specific competition regulation is a highly distortionary instrument when its application in converging markets is considered. Further, even the threat or possibility of intervention to restrain a telecommunications firm's competitive behaviour confers a distortionary competitive advantage upon competitor firms deriving advantage from their incumbent positions in other converging industries. This is particularly so given the incentives for regulatory gaming created through the mere possibility of regulatory intervention.

The industry-specific regulation of telecommunications markets was enacted on the basis that the development of a competitive telecommunications sector depended upon more effective powers to constrain anti-competitive behaviour and to promote pro-competitive access than were available under generic competition law.[5] While the validity of this policy principle is moot, Telstra's key point is that as soon as competition - the process[6] - is established, the rationale for removal of industry-specific restrictions, especially in light of market convergence, must surely be overwhelming.

[5] *Trade Practices Amendment (Telecommunications) Bill 1996*, Second Reading Speech, p1.

[6] It is important to note that, contrary to an assumption implicit arguments of many of Telstra's competitors, competition is not synonymous with the commercial interests of competitor firms. Rather, competition is the process whereby the market sorts the efficient firms from inefficient ones.

Specific Competitive Restraints - Broadcasting Legislation

Clearly a key task for this Inquiry will be to consider the policy basis for the many express and implicit competitive restraints in the *Broadcasting Services Act*, and the ongoing relevance of that policy in light of the consequences of convergence.

Key provisions the policy basis for which will need to be reviewed include:

- the limitation on the number of commercial free-to-air broadcasting licences[7] (note that this issue must also be considered pursuant to a review required by 2005 pursuant to the *Broadcasting Services Act*, clause 60 of Schedule 4);
- the requirement that subscription broadcasting licensees earn the majority of their revenue from subscriptions[8];
- restraints on multichannelling and subscription broadcasting by FTA broadcasters[9];
- the anti-siphoning rules[10];
- cross media ownership/control, foreign ownership/control and other ownership/control regulation[11];
- allocation of spectrum for digital broadcasting and datacasting.[12].

Telstra is not advocating the removal of these restrictions. There is sound policy reflecting the current and historical balance of competing interests in the context of the stated regulatory policy of the BSA (see above) underlying many of these provisions. Telstra is merely advocating that, in the context of a dynamic convergence environment, in which traditional market boundaries and traditional assumptions about diversity and power to influence may be called into question, the Commission will need to review their underlying assumptions.

In Telstra's view, as outlined below, the soundness of the policy underlying some of these provisions is already demonstrably shaky.

Anti-Siphoning

Telstra considers that the anti-siphoning rules impose unjustifiable constraint on the ability of subscription television broadcasters to provide sports programming.

Free-to-air and pay television broadcasters directly compete for the rights to sporting events. The perceived competitive threat from pay television in this arena has led to legislation that handicaps the competitiveness of providers of pay television. Section 115(1) of the BSA provides for the Minister to identify a list of events which should be available free to the general public. Subscription television broadcasters are prohibited by their licence conditions from acquiring the rights to broadcast such events unless a FTA broadcaster has also acquired the right to broadcast that event.

The Explanatory Memorandum to these provisions says that this "anti-siphoning" scheme:

> *"should ensure, on equity grounds, that Australians will continue to have free access to important events. It will, however, also allow subscription television broadcasters to negotiate subsequent rights to provide complementary, or more detailed, coverage of events."*

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[7] Section 28 Broadcasting Services Act, 1992 (BSA)
[8] Schedule 2 Clause 10 *BSA*
[9] Schedule 2, subsection.(7) (1) (m), *BSA*
[10] Section 115 *BSA*
[11] Part 5 BSA
[12] Schedule 4, section 23 (1),*Television Broadcasting Services (Digital Conversion) Act 1998*

The events on the anti-siphoning list are a broad list of sporting events in the areas of AFL, Rugby League, Rugby Union, Cricket, Soccer, The Melbourne Cup and Grand Prix motor racing. The Minister may remove an event from the list if satisfied that the free-to-air broadcasters have had a real opportunity to acquire the rights to it and have not done so within a reasonable time.

However, rather than operating as intended, these rules in Telstra's view effectively set up free-to-air broadcasters and sports rights brokers with a statutory monopoly without a countervailing obligation to show any of the events to which they have been granted statutory rights. The anti-siphoning list should reflect what is actually shown on free-to-air television.

These provision are an example of asymmetric competition regulation, which has the effect of limiting the impact on incumbent free-to-air broadcasters of competition from pay TV broadcasters for the rights to broadcast certain sporting events. It is an implicit acknowledgment that the two types of television are competitive with one another.

As outlined in the regulatory principles above, such regulation should specifically address the benefit it seeks to confer - that certain sports events may be viewed on free-to-air television. If this is the policy aim, it would appear insufficient to confer on free-to-air broadcasters a right to broadcast without also imposing an obligation to broadcast specific events. Legislative amendment should impose in respect of events on the list an obligation which, if not fulfilled by broadcasters, should result in loss of their rights in relation to those events. If, on the other hand, the true aim is to protect free-to-air broadcasters from competition, then the basis for this policy needs to be reviewed by the Commission.

Digital Television

In Telstra's view there is no clearer example of asymmetric regulation of competitors in a single market than the inconsistent treatment of the digital conversion of free-to-air and pay television services.

Pursuant to the *Television Broadcasting Services (Digital Conversion) Act 1998*, free-to-air broadcasters are to granted a fee-free licence of 7 MHz of broadcasting spectrum with which to simulcast their analogue broadcasts in digital format. This spectrum is effectively on "loan" for the eight year simulcast period, after which the equivalent of the loaned spectrum must be returned to the Government.[13]

In contrast, on 23 December 1998, the ACCC announced a public inquiry into the declaration of a technology-neutral broadband subscription television broadcasting service using line links (ie. physical infrastructure - cable - not microwave or satellite) pursuant to Part XIC of the TPA. Before cable television providers have even made the expensive transition to digital, the ACCC is effectively inquiring whether to impose "must carry" obligations - with the spectre of regulatory intervention forming the backdrop to access negotiations - upon the operators of the carriage services via which pay television programming is distributed.

The Commission's Inquiry ought to examine such inconsistencies in regulatory treatment between firms which increasingly compete in the same market (as outlined further below).

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[13] Schedule 4, section 6 (3) (b),(c), (h), *Television Broadcasting Services (Digital Conversion)Act, 1998*

Datacasting

The amount of spectrum to be loaned to free-to-air broadcasters far exceeds that required for digital conversion, and, following the tabling in Parliament of a number of reviews to occur this year, amendments to the *Radiocommunications Act 1992* will be proclaimed, to the effect that the loaned spectrum may also be used by the free-to-air broadcasters for datacasting - essentially non-broadcasting services provided to televisions using the broadcasting services bands. Firms other than broadcasters may, following determination of the ABA under section 34(3) of the BSA that spectrum be made available, acquire spectrum for datacasting through a competitive bidding process.[14] Free-to-air broadcasters who datacast will be required to pay a "datacasting charge", to be determined by the ACA such that it is "competitively-neutral" with the price paid by non-broadcasters for spectrum.[15]

In Telstra's view the price paid by the broadcasters for the right to use their loaned spectrum to datacast can never be truly competitively neutral because, unlike competitive bidders, they undertake no risk in acquiring this spectrum. There does not appear to be any policy basis for the competitive advantage thereby bestowed upon datacasters with subsisting advantage deriving from existing FTA operations, to the further disadvantage of the new entrants.

Infrastructure Access

A key asymmetry is the exemption of broadcasting infrastructure from carrier regulation pursuant to section 48 of the *Telecommunications Act 1997*. Section 48 exempts from the obligation to become a licensed carrier the operators of line links solely or principally for the supply of carriage services for broadcasting services. Unlike its predecessor, section 99 of the *Telecommunications Act 1991*, section 48 does not exempt the broadcasting "access network" - facilities or transmitters which actually deliver the signal to the intended audience - from the requirement to obtain a carrier licence.

Telstra presumes that broadcasters are taken to supply carriage services for distribution of television programmes from their transmitters to televisions only to themselves, hence they do not require a carrier licence, and are not subject to facilities access, regulation of conduct in telecommunications markets or telecommunications access regulation.

The contrast in treatment of broadcasting infrastructure by reference to whether it is used for free-to-air or subscription television broadcasting has been highlighted above. While free-to-air broadcasters are exempt from the access regime which applies to carriers, the carriage services utilised by subscription broadcasters are the subject of an ACCC access inquiry. Particularly noteworthy is the context - pay television providers are the new entrant, and cable infrastructure is new, high-tech, expensive infrastructure which constitutes new investment. It seems that policy is awry where the firms investing at significant risk to provide new technology for new services are regulated more onerously than incumbent broadcasters who continue to enjoy a statutory monopoly on their own infrastructure.

Telstra believes that the Productivity Commission should consider whether access to all broadcasting infrastructure should be regulated uniformly. Free-to-air broadcasters currently enjoy a privileged position in relation to their infrastructure, and additionally have been protected from competition from additional broadcasting licensees. Now that competition is finally emerging - in the form of subscription television services (prohibited for 20 years as a result of free-to-air lobbying) and increasingly sophisticated online services - and convergence is enhancing the utility of all forms of distribution infrastructure, review of the policy rationale for differential treatment of infrastructure access issues is warranted. Regulation - on the

[14] Schedule 4, section 27, *Television Broadcasting Services (Digital Conversion) Act 1998*.
[15] Schedule 4, 53(2), *Television Broadcasting Services (Digital Conversion) Act 1998*

basis of uniform principles focusing on the long term interests of end-users - would be warranted where the market is unlikely to procure this outcome.

Spectrum Planning and Licensing Issues

The broad principles of Telstra's position on radio spectrum planning and licensing are that:

- the radio spectrum must be managed efficiently;
- the administrative arrangements must be such that they support changes in effective spectrum usage without hindering the introduction of new services; and
- all arrangements, processes and procedures must include equitable treatment of incumbent users.

Telstra believes that the current practice of special spectrum arrangements for broadcasters is no longer appropriate, is anticompetitive and requires review.

Considering in particular the growing convergence of -broadcasting- and -radiocommunications- and the move to digitalisation, it is suggested that the view of the industry be sought on the advantages and practicality of bringing closer together the spectrum management processes for broadcasting and radiocommunications. This should lead to a clear and consistent statement for all stakeholders based on the principle of removal of industry specific arrangements for broadcasting.

The underlying intentions of spectrum management within the general radiocommunications arrangements, and within the broadcasting services bands are essentially the same: that is, to ensure efficient spectrum use and maximise the public benefits from use of the spectrum. The special spectrum management arrangements in the Broadcasting Services Act 1992 (BSA), do not appear to have delivered on the intended goals. For example, there have been very few new and competitive services introduced since 1992, despite statements by the Australian Broadcasting Authority (ABA) that indicated significant planning and licensing activities would have been complete within three years of commencement of the BSA. Additionally, the areas in which services have been introduced were not subject to spectrum congestion. This indicates that the detailed planning processes of the BSA, which were apparently intended to explore competitive issues such as the efficiency of spectrum use (ie number of channels) versus the acceptable quality of services, have not operated effectively. This also indicates that the ABA has not shown itself to be effective in managing analogue spectrum arrangements and throws doubt over their ability to handle more complex spectrum issues associated with digitalisation.

Telstra's concern with this issue relates to future spectrum bands that may be assigned as broadcasting services bands. Given the industry context of convergence, Telstra does not believe there are sound policy reasons for providing one segment of converging communications media with favourable spectrum access rights. Non-broadcasters would have to rely on the provision of the BSA (in section 34) which under some conditions allow the use of unused broadcasting spectrum for "non-broadcasting purposes' thus effectively providing them with access to spectrum in the broadcasting services bands. This is not a process that can be relied upon to deliver spectrum to potential users in a timely manner, and with technical conditions that enable efficient service delivery. Additionally, a broadcasting-first policy has the potential to significantly distort the development of emerging and new markets which rely on spectrum usage. For example, pay TV channels could be supplied within the digital sound broadcasting (DSB) bands. Given that the pay TV industry is highly competitive, with multiple competing technology platforms already in existence, Telstra does not believe there is a rationale for providing preferential spectrum access to a given segment of the industry. This may occur if the DSB band is declared as a broadcasting services band.

At a broad policy level, Telstra also believes that the broadcasting spectrum is well suited to operation under existing radiocommunications arrangements, particularly the spectrum licensing regime. The spectrum itself is suited to high value end uses, which would generate competitive bidding. Radio and television services may

or may not be the highest value use. The number of channels that are currently broadcast, and the quality level of the broadcasts, may or may not be the optimum from efficiency and consumer satisfaction perspectives. Current BSA processes are not testing, or even questioning, such issues.

Telstra understands there may be concern to protect the consumer investment in receiving equipment that exists for current broadcasting services. This investment is significant and should not be ignored. However, issues associated with determining the most beneficial use of a spectrum band (ie the public interest), and the appropriate licence tenure and certainty for the incumbent, are not conceptually different in relation to broadcasting services as compared with other radiocommunications services. Indeed, as convergence continues to occur, any apparent differences will lessen.

An immediate benefit of incorporating broadcasting spectrum into the general radiocommunications environment, beyond the recognition that traditional industry barriers have eroded, would be the potential administrative efficiencies associated with single agency management of the spectrum. Cost savings would represent a lessening of costs to spectrum operators, end-users and taxpayers generally. The rapidly growing convergence of traditional broadcasting and radiocommunications environments further multiplies these cost savings.

The favourable treatment of the broadcasting industry is abundantly evident in the free allocation of spectrum to broadcasters for digital conversion and datacasting, while other potential datacasters must bid for spectrum in a competitive process. In any event, spectrum will only be made available for datacasting by non-broadcasters after the interests of the broadcasting industry are taken into account.[16] - While the "datacasting charge" to be paid by broadcasters who datacast is intended to be competitively neutral (reflecting the charge paid for datacasting spectrum by non-broadcasters), it is unlikely to be truly so given that the broadcasters undertook no risk, and will require only an ex post facto business case, to justify their investment in the spectrum.

At a broad policy level, Telstra also believes that the broadcasting spectrum is well suited to operation under existing radiocommunications arrangements, particularly the spectrum licensing regime. The spectrum itself is suited to high value end uses, which would generate competitive bidding. Radio and television services may or may not be the highest value use. The number of channels that are currently and proposed to be broadcast, and the quality level of the broadcasts, may or may not be the optimum from efficiency and consumer satisfaction perspectives. Current BSA processes are not testing, or even questioning, such issues.

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[16] Schedule 4, 6 (4)(a), *Television Broadcasting Services (Digital Conversion) Act, 1998.*

Conclusion

As asymmetric regulation is clearly and increasingly distortionary and anticompetitive in an era of convergence, review of regulatory policy is critical. Telstra encourages the Productivity Commission to develop principles for such a review which focus on competition and competitive neutrality, economic efficiency and technology-neutrality. Increasingly it may become necessary to assign regulatory regimes and regulators not by the *industries and firms* they regulate but by the *type of services* they regulate.

Regulatory Principles

Telstra believes that it is fundamentally important that the regulation of converging markets is competitively neutral. What this means in practice is essentially captured by the set of regulatory principles outlined below. Telstra believes that it ought to be possible to achieve converging industry consensus on these principles:

1. Regulation should be technology neutral. For example, the providers of on-line services which are viewed on television should have those services regulated uniformly, whether they use cable, the PSTN, the broadcasting services bands or satellite to deliver those services.

2. Regulation of a service should be neutral as to who is providing the service. For example, the goal should be to ensure that the providers of datacasting services are regulated neutrally whether they are free-to-air broadcasters or other datacasters.

3. Regulation should address only the providers of services which, because of their characteristics, it is necessary to regulate to achieve the desired policy goal. For example:
   - ⇒ If the regulatory goal is efficient access to distribution infrastructure, then the regulation should be aimed at infrastructure service providers, and require access in accordance with competitively neutral principles to all infrastructure (rather than broadcasting licence specific exemptions).
   - ⇒ If regulatory policy aims to ensure a diversity of editorial views, regulation should be applied to those with the right to distribute their views, where such diversity may not otherwise exist. The technological means of distributing that content is per se irrelevant, although certain features of that means may be relevant to the diversity issue, for example, the reach of the distribution infrastructure, whether the views are "push" or "on-demand".
   - ⇒ If regulatory policy is to ensure competitively neutral allocation of spectrum, regulation of all spectrum allocation should be co-ordinated and focused on that goal. Currently, spectrum is bundled with a licence to push content for broadcasters, yet other spectrum users are required to bid competitively for it.
4. Regulation should, to the extent possible, be lighted- handed in nature to ensure innovation in the emerging convergent services industry is not stifled.

It may be that certain transitional arrangements are necessary, but the Government should ensure that its regulation of converging industries is progressing to accord with the above principles.

Regulatory Responsibility

As a general rule, regulatory responsibility ought to rest where the regulatory expertise lies, which is largely determined by the historical or current regulatory policy pursuant to which enabling legislation establishes the jurisdiction of the various regulators. In Telstra's view, the following arrangement would reflect the regulatory policy which Telstra advocates above:

- Regulation of competition with a view to constraining the creation or exercise of market power should rest with the ACCC applying general competition law to all industries.

- Regulation of ownership/control and content with a view to ensuring diversity and maintenance of community standards, to the extent necessary or appropriate given the inherent diversity and limitations on the effectiveness of any such regulation, should rest with the ABA.

- Regulation of spectrum and other infrastructure to effect efficient and fair allocation and licensing, and maintenance of technical standards, should be effected by the ACA.

CONVERGING MARKET DEFINITION ISSUES

Convergence leads to redefinition of markets. This process needs to be understood by regulators and regulatory policy makers, to ensure that further asymmetric regulation is not developed and imposed.

The definition of convergence quoted from Cutler above cites the key characteristics of convergence as relating to "a process of market and industry restructuring" and involving "the emergence of new economic markets based on digitisation and networking"[17]. In short, the process is all about market redefinition.

Clearly regulatory policy and practice in a convergence environment must take account of competition from non-traditional sources and the supply-side substitutability of new technologies when defining markets. This will require market analysis which is informed and forward-looking, acknowledging that the structure of converging markets is particularly dynamic.

In the context of converged markets care must be taken to ensure that regulators do not equate business models with "markets" as the ACCC appears to have done in relation to its separation of the markets for pay and free-to-air television. In respect of many convergent services, sustainable, profitable or uniform business models do not yet exist. There are a variety of models and uncertainty as to how they will develop. Differing revenue models - such as advertising vs. advertising and subscription - does not mean that services do not compete with one another.

In competition law, significant consequences flow from market definition is fundamental to findings on market power and the effect of conduct upon competition, Section 4E of the Trade Practices Act provides:

> *"For the purposes of this Act, unless the contrary intention appears, "market" means a market in Australia and, when used in relation to any goods or services, includes a market for those goods or services and other goods or services that are substitutable for, or otherwise competitive with, the first-mentioned goods or services."*

The Commission's Merger Guidelines include the following citation (at paragraph 5.38) from the Swanson Committee recommendation which resulted in the enactment of section 4E.

> *"[T]he the definition of market should ... require that, in the determination of a 'market' for particular purposes, regard shall be had to substitute products which have a reasonable interchangeability of use and which have high cross-elasticity of demand, i.e. where a small decrease in the price of a particular product would cause a significant quantum of demand for a similar product to switch to the product in question. [Trade Practices Act Review Committee (1976), Report to the Minister for Business and Consumer Affairs, p.17, para. 4.22.]"*

The case law on section 4E is particularly extensive in its consideration of the expression "substitutable for" in the context of market definition. The Trade Practices Tribunal decision in *Re Queensland Co-operative Milling Association Ltd; Re Defiance Holdings Ltd* (1976) 25 FLR 169, was cited with approval by the High Court in *Queensland Wire Industries Pty Ltd v. BHP* (1989) 167 CLR 177:

> *"So a market is the field of actual and potential transactions between buyers and sellers amongst whom there can be strong substitution, at least in the long run, if given a sufficient price incentive."*

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[17] Dr T Cutler, "The Need for a Convergence Policy and Next Generation Regulation", in DCITA Communications Research Unit, *1998 Communications Research Forum Papers*, p1.

More recently the following statement of Burchett J of the Federal Court in *News Limited v. Australian Rugby Football League* (1996) ATPR ¶41-466 at 41,667 has not been overruled:

> *"As a matter of statutory interpretation, the addition of the words 'or otherwise competitive with' [in s.4E] emphasises ... the legislative intention to specify a wider rather than a narrower market."*

Market analysis by the ACCC as it considers the new mergers and alliances which are bound to form during - indeed which characterise - the era of convergence, will require consideration of competition from non-traditional sources and the supply-side substitutability of new technologies.

What this calls for, in essence, is a dynamic analysis of relevant markets. There is already judicial authority for such an approach. In *TruTone v. Festival Records Marketing Ltd* [1988] 2 NZLR 352, the New Zealand Court of Appeal rejected a narrow market definition as:

> *"[ignoring] commercial realities. It focuses on short run phenomena. It presents a snapshot rather than a moving picture of continuing commercial activity."*[18]

In the convergence era, regulators and courts which are required to define markets need to look to the moving picture of activity which sees the substitution possibilities changing and expanding in the short term.

The need for regulators to focus their attention on the long term is an express requirement of Part XIC of *the Trade Practices Act*. The object of this Part is specifically to promote the *long term* interests of end-users. This will require more than a static view of the markets under consideration. It will require analysis of the new substitutes being brought about through convergence in the short and long term.

Yet the ACCC, in Telstra's experience, tends to define markets narrowly, with insufficient regard to supply-side substitutability resulting from converging technologies and insufficient analysis of demand-side substitutability of new services supplied in converging markets. The ACCC's current public inquiry into the declaration of a broadband subscription broadcasting carriage service using line links is illustrative. Adopting a position which is inexplicable to the pay TV industry, the Commission maintains that pay television and free-to-air television do not compete in the same market.

> *"The Commission ... considers that there is a retail pay television market (ie, a market in which consumers subscribe to pay television services) which, at this stage, the Commission believes does not include other forms of video entertainment such as free-to-air television, home video rentals and cinemas."*[19]

In Telstra's view, there are numerous indicators that free-to-air and pay television are supplied in a single market, including that:

- The regulatory treatment of free-to-air and pay television broadcasters;
- Competition between free-to-air and pay television suppliers as evidenced by:

⇒ attempts by both types of broadcaster in the regulatory arena to restrict the other's capacity to compete;
⇒ head-to-head competition for content, especially sports programming and movies;
⇒ head-to-head competition for advertising;
⇒ head-to-head competition for customers; and

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[18] [1988] 2 NZLR 352 at 360

[19] ACCC, Declaration of Analogue Subscription Television Broadband Carriage Services - Notice of Inquiry and Discussion Paper, December 1998, p6. Note the ACCC has not, at the time of writing, released its draft decision in this Inquiry, although its release is reported to be imminent.

- The degree of substitution between the two services, eg, as evidenced by the level of churn between subscription and free-to-air television services, which is indicative of a competitive market for end users (demand substitution).

The market in which pay television services are supplied is simply a segment of a wider market for retail television services. End users of pay TV only differ from end-users of free-to-air television in that they place a sufficiently high valuation on the higher quality service offered by pay television to purchase access to programming directly, rather than paying for such access through greater exposure to advertising.

Despite significant evidence to this effect provided by FOXTEL and Telstra, the ACCC appears to maintain its view that these services are supplied in two separate markets. This static view of the television market originates from the view taken in the ACCC's 1995 and 1997 consideration of proposed mergers between FOXTEL and Australis. Clearly, given the pace of development of these industries, plus the prospect of competition from converging industries, such a view should not without extensive review form the basis of the ACCC's conduct of a 1999 declaration inquiry.

The ACCC's intransigence on this point does not auger well for the regulation of converging markets in the future.

CONCLUSIONS

Convergence is redefining markets, and those markets are generally broader and more competitive than the originating ones in which the providers of converging services have traditionally competed. This significant characteristic must be recognised in the development of regulatory policy and implementation for convergent services.

In Telstra's submission, industries based on convergent services will develop optimally with regulation that provides a level playing field across the new activities occurring in converging markets. This is best achieved through the application of general, rather than industry-specific, competition law. Competition, innovation and investment (to the long-term benefit of consumers) across the converged communications, broadcasting and content-provision industries will only occur if firms have the capacity to compete in the new convergent markets on an equal footing.

In contrast to this an asymmetric or a status quo approach to regulation will result in firms from different industries bringing a range of artificial competitive constraints to these new markets. Such constraints are inappropriate at best, but are more likely harmful to efficiency and competition in the emerging, dynamic convergent markets, to the long-term detriment of consumers. Consideration of the policy goal and the services which, because of their characteristics, it may be necessary to regulate to achieve the goal, is required.

Telstra acknowledges that as the challenge of regulating convergent services industry is great, it may be that certain transitional arrangements are necessary. Telstra however urges the Government to ensure that its regulation of converging industries works towards the key regulatory principles espoused in this submission - essentially technology-neutral and competitively-neutral regulation.