



**AOL|7 PTY LIMITED**

**COMPETITIVE EFFECTS OF BUNDLING TELECOMMUNICATIONS SERVICES**

**FEBRUARY 2003**



# 1. Executive Summary

## 1.1 Background

AOL|7 appreciates the opportunity to make submissions on the Australian Competition & Consumer Commission's proposed approach to assessing whether bundling of services in the telecommunications industry will contravene the *Trade Practices Act 1974* (Cth) ("TPA").

A structural situation has arisen in the Australian telecommunications market which is unique in any developed economy in the world. There is only one supplier of local access. That supplier is the only supplier of any-to-any connectivity. That supplier is in a position to determine the strategy of the only supplier of subscription television content. That supplier, together with the second largest supplier of telecommunications services in Australia (together accounting for 90% of the total) are the only suppliers who offer discounted bundles of fixed and mobile telecommunications, online and subscription television services.

This unique structural outcome requires an appropriate policy response from the Commission. That response should be a preparedness to undertake immediate and effective enforcement of competition laws where conduct with an anti-competitive purpose or effect occurs or is likely to occur. AOL|7 submits that the results of anti-competitive bundling conduct is so pernicious that the enforcement intervention by the Commission should be on a "hair trigger" basis.

AOL|7 agrees that bundling may be beneficial to consumers and have no adverse competition effects in many circumstances. In these circumstances, bundling should not be restricted unless the conduct otherwise has the relevant anti-competitive purpose or effect.<sup>1</sup>

However, bundling has the potential to cause serious anti-competitive consequences where utilised by a vertically integrated firm with control of an essential input required for downstream competition and where access to all components of the bundle is limited to only a few firms. As has been recognised by the Productivity Commission, competition in telecommunications markets is not yet sustainable.<sup>2</sup> The anti-competitive effects of bundling are all the more devastating in markets where competition has not been fully established. One case where this is already demonstrable is in the supply of ADSL broadband online services.

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<sup>1</sup> Sections 45 and 47 of the TPA.

<sup>2</sup> Productivity Commission Inquiry Report, *Telecommunications Competition Regulation*, Report No. 16, 21 September 2001 at page xxviii.

[REDACTED]

Permitting service providers such as Telstra to bundle in this environment will not result in long term benefits to consumers.

It is therefore essential that:

- providers with substantial market power not be entitled to leverage any market power they have in one market into another;
- competitors are able to obtain access to all components of the bundles (on fair terms) offered by providers with substantial market power;
- the Commission has the necessary power to detect and address any anti-competitive conduct or threat of anti-competitive conduct immediately.

The Commission's draft Information Paper covers some of these issues. The extensive policy debate surrounding the enactment of Part XIB in 1997 is applicable to bundling, price squeezes, cross subsidisation and refusal to supply for the same reasons that such safeguards were considered necessary then. Two of the three elements of section 46 and of section 151AJ(2) are already satisfied where there is bundling by Telstra. Only the requisite "purpose", "effect" or "likely effect" needs to be established. Section 151AQ already requires the Commission to act expeditiously. Under these circumstances, the Commission should have ready to issue Part A competition notices under section 151AKA as they have proven the only immediately effective enforcement tool for preventing irreparable harm in telecommunications markets.

In this submission, AOL7 sets out the key anti-competitive consequences of bundling in the current competitive environment in Australian telecommunications markets and the mechanisms AOL7 believes the Commission should adopt to detect and address any anti-competitive conduct or threat of anti-competitive conduct.

## 1.2 Structure of the Submission

The structure of this submission is as follows:

- **section 2** summarises the current competitive environment in telecommunications markets in Australia;
- **section 3** explains the anti-competitive issues raised by bundling in the current competitive environment in telecommunications and related markets in Australia; and

- [REDACTED]
- **section 4** sets out AOL|7's proposed mechanisms for detecting and addressing anti-competitive conduct which arises from bundling in the telecommunications and related markets in Australia.

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## 2. Current Competitive Environment

### 2.1 Characteristics of Telecommunications Industry

The key characteristics of the competitive environment in Australian telecommunications markets are as follows:

- the substantial market power of Telstra in all telecommunications markets, including dial up and broadband online services in telecommunications markets;
- Telstra's control of the customer access network ("**CAN**"), access to which is required by any carrier or carriage service provider wishing to compete with Telstra;
- Telstra being a vertically integrated firm which offers customers the full range of telecommunications and related services and now offers the Foxtel subscription television service;
- Telstra being able to use its extensive customer databases to target the marketing of its services, including deciding how best to structure its bundled offerings to attract and retain customers;
- Telstra's current bundled offerings requiring customers to acquire a fixed line telephony service which is preselected to Telstra as well as one or more other services from Telstra;
- competition in telecommunications markets being limited. Telstra provides around 95% of the local access services, 80% of retail local telephony, 75% of domestic

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long distance services, 45% of mobile services and is the largest provider of retail dial up internet services with 25%;<sup>3</sup>

- Foxtel having substantial market power in the market for subscription television services, which is derived primarily from its control of critical content and customer access equipment;
- the limited scope of the access arrangements proposed by Foxtel and Telstra as part of the section 87B undertakings accepted by the Commission on 13 November 2002. In a practical sense, access to the only available subscription television service in metropolitan cities is limited to only a very few competitors, ie. those that do not compete in metropolitan Sydney, Melbourne and Brisbane. The access arrangements also require access seekers to arrange for the service to be carried on Telstra's HFC network as a condition of obtaining access to the Foxtel subscription television service;
- competition in subscription television market being very limited. Foxtel is basically the only provider throughout Australia, Optus now provides the Foxtel service (with some of its own content) and Austar does not provide services in metropolitan Sydney, Melbourne or Brisbane;
- bundling being utilised in telecommunications markets as an effective method to attract and retain customers, particularly high spend customers;
- there being incentives for Telstra to use its access to subscription television content and close relationship with Foxtel (through ownership links) to foreclose competition in telecommunications markets; and
- there being incentives for Foxtel to use control of critical content and customer access equipment to foreclose competition in subscription television markets.

## **2.2 Extent of Competition in the Telecommunications Industry**

It was recognised by the Federal Government at the time of deregulation of the telecommunications industry in 1997 that competition has not been fully established in some telecommunications markets. The Government said in the *Trade Practices Amendment (Telecommunications) Bill 1996 Exposure Drafts and Commentary*:

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<sup>3</sup> Productivity Commission, *Telecommunications Competition Regulation*, Report No. 16, dated 21 September 2001, AusInfo, Canberra at pages 99 and 129. Current figures indicate this has increased to about 32%.

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*"Telecommunications is an extremely complex, horizontally and vertically integrated industry and competition is not fully established in some telecommunications markets. There is a considerable scope for incumbents to engage in anti-competitive conduct because of the dependency of competitors in downstream markets on access to networks or components controlled by the incumbents. Furthermore, the possibility of predatory cross-subsidies by incumbents from non-competitive markets to markets in which competition exists or is emerging is a particular threat to the establishment of a competitive environment."*

In 1997, the Government envisaged that competition would be established in telecommunications markets and as a result the telecommunications-specific provisions that were incorporated into Part XIB of the TPA would be transitional in nature and apply only until competition has been established. Telstra, however, continued to maintain substantial market power in telecommunications markets. In recognition of this, the Government refined the Part XIB regime in 1999 to strengthen the Commission's powers under Part XIB to detect and address any anti-competitive conduct.

The Productivity Commission report on *Telecommunications Competition Regulation*<sup>4</sup> considered, among other things, whether Part XIB should still apply to telecommunications markets. In assessing the level of competition in telecommunications markets, the Productivity Commission concluded that competition in telecommunications markets was not yet sustainable<sup>5</sup> and that Part XIB of the TPA be retained, subject to the introduction of an appeal process.<sup>6</sup>

### **2.3 Value of Bundling**

The value of offering bundled telecommunications services is well recognised by the telecommunications industry. Bundling reduces customer incentives to use more than one service provider and reduces customer churn by making it more difficult for competitors to attract customers away from their current provider.

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<sup>4</sup> Report No. 16 dated 21 September 2001.

<sup>5</sup> Productivity Commission Report, *Telecommunications Competition Regulation* at page xxviii.

<sup>6</sup> Productivity Commission Report, *Telecommunications Competition Regulation* at page xxxvii.

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In a speech given by Dr Switkowski at the Credit Suisse First Boston conference in Hong Kong in March 2001, when discussing customers who acquire bundles from Telstra, Dr Switkowski said:

*"These customers are twice as likely to be high value and three to four times as likely to remain loyal to Telstra."*

Optus also recognises the value of bundling. In a paper presented by Adrian Chamberlain at the Australian Broadcasting Authority Conference on Radio Television and the New Media in May 2001<sup>7</sup>, Mr Chamberlain said:

*"CWO market data indicates that those customers who take a bundled set of CWO services are far less likely to churn their individual services, such as local and long distance telephony, to other service providers."*

This was supported by Mr Ted Pretty of Telstra after the approval was given to the Foxtel, Optus and Telstra content sharing arrangement, where he said:

*"We have found that those customers that do take a package are less likely to churn away from the service provider."*<sup>8</sup>

In a presentation at the 13th Annual Salomon Smith Barney Global Entertainment, Media & Telecommunications Conference, Dr Switkowski of Telstra presented figures which support Telstra's view that:

*"Single bill and bundling [are] driving consumer segment growth and churn reduction"*<sup>9</sup>.

### **3. Anti-competitive Consequences of Bundling**

#### **3.1 Specific competition issues**

In the current competitive environment in telecommunications markets in Australia, the key competitive issues that arise as a result of bundling are:-

- (a) Bundling by a provider with substantial market power in relation to one component of the bundle enables that provider to exploit its substantial market power in the tying market by extending its market power to other markets. For example, Telstra

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<sup>7</sup> *The Importance of Pay television Programming in Driving Investment in the Information Society*, 3-4 May 2001 at paragraph 1.8.

<sup>8</sup> Reported in Sydney Morning Herald, 29 November 2002.

<sup>9</sup> Presentation given on 7 January 2003.

[REDACTED]

may supply the component of the bundle in which it has substantial market power (local call services) only as part of a bundle. Alternatively, Telstra may structure the bundle by offering a service that few suppliers offer (such as subscription television services) only if the customer acquires another product from Telstra, such as dial up internet or broadband online services (or other products in relation to which the supplier faces more effective competition). Telstra may structure the bundles and the price for bundles in such a way as to encourage customers to purchase a bundle in preference to individual services.

(b) Bundling provides cross-subsidisation opportunities. In the current environment, Telstra is able to take advantage of these opportunities by bundling high margin products (such as domestic long distance) with lower margin products (such as ADSL broadband services), where markets are emerging with a number of potential suppliers seeking customers, to create bundles that are attractive to consumers and enable Telstra to recoup a reasonable overall return for the supply of both products while making it very difficult for the competitors in the emerging market to compete. [REDACTED]

(c) Bundling increases the ability of the bundle provider to attract and retain customers, which tend to be high spend customers. The attractiveness of providing a single bill leads to a significant proportion of consumers only acquiring their services from one carrier, in effect removing the customer base from contestability. Given the value to providers of bundles, the bundled offerings will increase customer churn towards providers of bundled offerings and away from pure telecommunications or online providers. As bundled offerings become more attractive, providers of bundles will increase the number and variety of bundles offered. The more services in a bundle, the greater the ability for the providers to manipulate bundle pricing while still maintaining or increasing margins. The lack of a commercial churn process that applies to ADSL broadband services further reduces customer choice and the ability of providers to compete on the merits because there are no arrangements to smoothly transition services, with customers currently experiencing an unacceptable break in service of up to three weeks when changing service providers.

(d) In circumstances such as these where few competitors have access to the Foxtel subscription television service to resell to customers, the more attractive the bundles, the more difficult it will be for pure telecommunications providers to



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compete and the higher the barriers to entry will be. Providers such as AOL|7 cannot obtain access to the Foxtel service because of the restrictive way the access undertakings have been drafted. This reduces the size of the available market for pure telecommunications or online service providers, such as AOL|7 and will lead to an increase in Telstra's substantial market power.

- (e) In circumstances where a vertically integrated firm supplies an essential input to its non-integrated competitors, the vertically integrated firm has the ability to effect a price squeeze. Telstra is in this situation in respect of the supply of fixed line telephony services because of its control of the CAN. Supply of the subscription television service by Foxtel who has control of the critical content and customer access equipment will provide Foxtel with an opportunity to effect a price squeeze in respect of services supplied to wholesale customers.

These factors reduce the competitive impact of pure telecommunications or online service providers in key telecommunications markets by removing the incentives for them to remain in the market and increasing the barriers to entry to the markets.

### **3.2 Circumstances that increase the scope for anti-competitive conduct**

One issue AOL|7 would like to make clear is that while in some circumstances bundling may have benefits to consumers and no long term anti-competitive detriments, in other circumstances bundling has no benefits as any short term gain by consumers is outweighed by the medium to long term anti-competitive effect of losing competitors in a market. A key factor in determining whether or not bundling will be anti-competitive is the particular characteristics of the market in which the bundling takes place.

As a result of the Foxtel/Optus/Telstra transactions, the dynamics of the telecommunications and related markets in Australia have changed significantly. These transactions have materially increased the risk of anti-competitive conduct. Since deregulation in 1997 telecommunications markets have always been characterised as markets in which the dominant supplier controls an essential input required by its competitors to compete at the retail level of the markets. This has meant that competition has not been fully established in these markets. As a result of the Foxtel/Optus/Telstra transactions, Telstra finds itself in a unique position in the telecommunications industry for two key reasons.

First, as Telstra was historically the monopoly telecommunications provider and presently supplies the majority of Australians with their telecommunications requirements, it has the personal details of a very large and very valuable customer base. No other competitors has

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access to a database of such size and value and it cannot be replicated by any other market participant in the foreseeable future.

Secondly, to attract and retain telecommunications customers, Telstra has now been provided with an opportunity to offer subscription television services as part of its bundled offerings in circumstances where only Optus is able to offer a competitive offering in metropolitan Sydney, Melbourne and Brisbane.

Telstra is able to use this database and its access to the Foxtel subscription television service to structure its bundled offerings to ensure they are attractive to customers. The more attractive the bundle, the higher the take up of the bundle. The higher the take up, the more impact bundling has on competition in the relevant markets.

It is the combination of Telstra's substantial market power, the fact that competitors do not have access to all of the components of Telstra's bundled offerings and the scope for anti-competitive conduct that arises from bundling in these circumstances which increases the likelihood of anti-competitive conduct taking place.

Any ability for competitors or new entrants to compete with Telstra in this new environment has been discouraged because they not only have to rely on Telstra for access to the CAN in order to supply telecommunications services, they are not able to obtain access to the critical components of the bundle and so offer competitive services. Further, Foxtel's substantial market power has been enhanced significantly by the transactions as it now finds itself in a position where it is effectively the monopoly provider of a subscription television service. Although it may appoint resellers such as Telstra, it is the Foxtel service that is being resupplied.

By way of comparison, take for example the current telecommunications markets where Telstra offers a range of bundled services, which include subscription television services. The expected competitive response to such a challenge would be for a competitor to meet the challenge by offering customers the same or more attractive services for competitive prices. As most competitors in metropolitan areas would not meet the criteria to obtain access to the Foxtel service offered under the section 87B undertakings, they would not be able to offer competitive bundles. The more successful Telstra's bundled offerings, the more difficult it will be for the competitor to compete and may mean the loss of the competitor from the market.

The competitive dynamics and effect on competition of the bundle would be entirely different in circumstances where the vertically integrated supplier does not supply an essential input to competitors and competitors are readily able to obtain access to all components of the bundle.

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In this case, the competitor would have every opportunity to offer competitive products and remain a viable competitor.

The current provisions of Part XIB and IV of the TPA are not sufficient to address the issues raised by bundling in markets with the characteristics of the Australian telecommunications markets. Special rules are required to ensure that anti-competitive conduct is detected and addressed as soon as possible.

### **3.3 Effect on Emerging Markets**

AOL<sup>7</sup> is particularly concerned about these issues in the context of telecommunications markets where competition has not yet been established, particularly in the context of emerging markets, such as the supply of broadband online services. Experience over the last 5 years indicates that it is only in the emerging markets which do not depend on acquiring essential inputs from Telstra that new entrants have been able to compete with Telstra, for example in relation to the supply of cellular mobile services. Enabling Telstra to offer bundles which force or encourage customers to acquire new services from Telstra as part of a bundle will discourage any new investment and mean that there will be limited (if any) competition in emerging markets.

Any anti-competitive conduct in these markets will have an immediate and devastating effect. The damage that can be caused by anti-competitive conduct in markets where competition has not been fully established was recognised at the time the telecommunications industry was fully deregulated. The Federal Government recognised that additional safeguards would be required to address anti-competitive conduct or the threat of anti-competitive conduct where competition had not been fully established.<sup>10</sup>

The inherent characteristics of the Australian telecommunications market, coupled with the speed with which the industry was developing, formed the foundation upon which the Government relied to support its sector specific anti-competitive conduct regime. As the Government considered in its *Trade Practices Amendment (Telecommunications) Bill 1996 Exposure Drafts and Commentary*:

*"Telecommunications is an extremely complex, horizontally and vertically integrated industry and competition is not fully established in some telecommunications markets. There is a considerable scope for incumbents to engage in anti-competitive conduct because of the dependency of competitors in*

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<sup>10</sup> Item 6 of the *Trade Practices Amendment (Telecommunications) Bill 1996 Exposure Draft and Commentary*.

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*downstream markets on access to networks or components controlled by the incumbents. Furthermore, the possibility of predatory cross-subsidies by incumbents from non-competitive markets to markets in which competition exists or is emerging is a particular threat to the establishment of a competitive environment.*

*Total reliance on the court-based processes of Part IV of the TPA to constrain such anti-competitive conduct might, in some cases, prove ineffective because of the fast pace of change in this industry. There may be difficulty, for example, in obtaining evidence of predatory behaviour supported by inappropriate internal cost allocation by horizontally or vertically integrated firms. There can be lengthy delays inherent in court-based processes, while anti-competitive behaviour in telecommunications could cause particularly rapid damage to competition because of the volatile state of the industry during the early stages of competition. Against this background, the Government has decided that Part IV alone may prove insufficient to deal with anti-competitive behaviour in telecommunications."*

The Government gave the Commission powers under Part XIB of the TPA, which were designed specifically to detect and address possible anti-competitive conduct immediately.

There is a disturbing repeat of conduct which occurred in the early 1990s when emerging competition in long distance fixed line calls provoked a similar response from Telstra as is now being seen in the discounts on ADSL broadband services offered to pre-selected customers. AOL|7 understands that in the early 1990s, Telstra commenced offering a discount on access charges and local calls on the condition customers also acquired long distance services from Telstra, in effect Telstra's "Flexi Plans" were the first bundle of services in the telecommunications industry in Australia. AOL|7 also understands that AUSTEL then required Telstra to withdraw these offers because of their clear potential to reduce significantly the addressable market for emerging competition in the long distance market. Telstra was not permitted to offer these services as part of one package until the further entry of other competitors in the late 1990's when Telstra was wholesaling access and local call services and the Commission was satisfied that there was competition in these and the long distance markets.

Given the existence of Telstra's substantial market power in a range of telecommunications markets, AOL|7 considers that Telstra should not be permitted to offer discounts on their ADSL broadband services on condition that customers pre-select to Telstra for telecommunications services until competition has been fully developed in broadband services.

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**4. Detecting and Addressing Anti-competitive Conduct**

**4.1 Commission's proposals**

From the draft Information Paper, it appears that the Commission proposes implementing imputation rules to detect a price squeeze effected by Telstra.

AOL|7 understands from the draft Information Paper that in order to detect whether a price squeeze is being effected or predatory conduct taking place, the Commission will be likely to apply the imputation tests on both qualified marginal cost and an average total cost basis. In the event conduct fails the test using average total costs but does not fail the test using qualified marginal costs, the so-called "grey area", the Commission is likely to consider other facts to determine whether conduct is anti-competitive.

AOL|7 agrees with this approach primarily because from an enforcement perspective there is no reason to adopt a tougher test as the basic test when the Commission has other means of

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determining whether conduct is anti-competitive and should take into account other factors such as those identified by NERA. These factors include that there may be efficient and legitimate business reasons for setting prices below average total cost.<sup>13</sup>

AOL|7 would also like to understand from a practical perspective:

- what type of information the Commission will seek to obtain from those it considers may be engaging in anti-competitive conduct. This information at a minimum should include details the wholesale access prices to the essential input, the costs of transforming the essential input into the final product and the retail prices in respect of all the services being supplied; and
- the period over which the Commission proposes to assess whether a price squeeze has been implemented or predatory conduct has taken place<sup>14</sup>.

It is also important that the Commission ensures when dealing with price squeeze conduct that the Telstra retail prices reflect the wholesale access charge for all components of the relevant service as well as the cost of transforming the essential input into the retail product, including any justifiable access deficit charge.

There is one point AOL|7 would like to clarify about the criteria set out in the NERA paper on imputation tests. It is not clear why NERA suggests that it is necessary that the vertical integrated firm have market power in *both* the wholesale and the retail markets.<sup>15</sup> The conditions required for a firm to be able to implement a vertical price squeeze are as follows<sup>16</sup>:

- the vertically integrated firm must be involved in both the supply of an upstream input and the retail supply of the product for which the upstream input is required;
- the downstream firm must be dependent on the upstream supply of the input from the vertically integrated firm; and


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<sup>13</sup> *Imputation Tests for Bundled Services*, A Report for the Australian Competition and Consumer Commission Prepared by NERA, January 2003 at page 33.

<sup>14</sup> Even a very short period of damaging conduct has a material effect in this emerging market because the term contracts which customers must sign to obtain ADSL broadband services reduce the addressable market each time a customer subscribes to the vertically integrated provider. For ADSL broadband services, there are also no seamless portability or churn arrangements in place (leaving aside the technical issue of the way email and website addresses could be transferred).

<sup>15</sup> *Imputation Tests for Bundled Services*, A Report for the Australian Competition and Consumer Commission Prepared by NERA, January 2003 at page 10.

<sup>16</sup> King, S: *The Potential for Vertical Price Squeeze under the Proposed Foxtel/Optus/Telstra Pay TV Arrangements*, A Report on behalf of AAPT Ltd at page 5.

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- the vertically integrated firm and downstream firm must be active competitors in the relevant retail market.

Take the supply of an ADSL broadband service as an example to illustrate how Telstra may be able to implement a price squeeze that affects suppliers in a retail market where Telstra may not have market power. Telstra controls the CAN. Access to the CAN is an essential input required by suppliers of ADSL broadband services in order to supply retail customers with an ADSL broadband service. While terminating and originating PSTN access is regulated, the charge for local exchange provisioning is not regulated. This provides Telstra with the ability to set the price it charges for provisioning at installation (thereby the pricing for access to the CAN) in a way that an efficient retail competitor is unable to buy access to the CAN and match the price Telstra offers its own retail ADSL customers. Telstra is able to do this regardless of the fact that the ADSL market is emerging and Telstra may not have substantial market power in that market simply because it has a monopoly in the supply of an essential input required for retail competition.

For this reason, the imputation rules should apply to all services supplied by a vertically integrated supplier of an essential input required by downstream competitors.

The Commission does not specifically propose in the draft Information Paper a way to deal with any price squeeze once discovered or the other issues identified by the Commission (see page 14 of the draft Information Paper). AOL|7 assumes that the Commission intends addressing these issues by use of its powers of enforcement of Part IV or XIB of the TPA.

The Commission's proposal does not recognise:

- that a competitor such as AOL|7 has no specific legal right to force Foxtel to provide a subscription television service on fair terms (unless by its refusal Foxtel is misusing its market power and proscribed purpose can be established) noting that reduction in the addressable market is exacerbated by the inability of the competing providers to obtain services in the bundled package;
- the imputation rules and method by which the Commission proposes to monitor Telstra's behaviour does not apply to Foxtel;
- none of the safeguards in the TPA effectively constrain Foxtel's ability to use its market power;
- the damage that will be caused to competition if Telstra or Foxtel engage in anti-competitive conduct and that the Part IV provisions of the TPA and the



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Commission's enforcement powers are not enough to prevent this damage from occurring.

## 4.2 Other issues to be addressed

Enforcement of behavioural undertakings and of conduct generally (as opposed to a structural solution) is the only method now available to deal with the limited competition and scope for anti-competitive conduct in the Australian telecommunications and subscription television markets. It is essential that the enforcement tools provided to the Commission are effective and rapid in dealing with anti-competitive conduct in the current environment.

Bundling in markets such as the Australian telecommunications markets where:

- there is a vertically integrated supplier of an essential input required by non-vertically integrated competitors for downstream competition; and
- access to a key component of the bundle is not readily available to the non-integrated competitors,

provides real scope for anti-competitive conduct by the vertically integrated supplier. Therefore, conduct of the vertically integrated supplier needs to be closely monitored to ensure the Commission is able to detect and address any anti-competitive conduct or threat of anti-competitive conduct.

An effective way to prevent damage from anti-competitive conduct is to provide an incentive to the party most able to manage the risk of damage to invest in managing the risk. Incentives may be provided in the form of regulation. In regulation, a punishment will act as an effective incentive to deter conduct if it is sufficiently onerous and outweighs the benefit that person would otherwise gain from acting in the prohibited manner. This already exists in Part IV of the TPA. However, the Federal Government has recognised that these provisions are not sufficient in circumstances where competition has not been fully established.

AOL|7 believes that in order to address the scope for anti-competitive conduct arising from bundling in markets where competition has not been fully established, the following steps should be implemented:

- (a) **Detection:** The only way the Commission can effectively detect anti-competitive conduct is by requiring suppliers of key services to provide all relevant information to the Commission on a regular basis to enable the Commission to determine whether or not a price squeeze or predatory conduct is being effected.

- [REDACTED]
- (b) **Deterrence:** The Commission should apply the imputation tests as set out in the draft Information Paper and take into account AOL|7's comments in section 4.1 of this submission and use the competition notice provisions in Part XIB of the TPA to deal with any anti-competitive conduct or threat of anti-competitive conduct.

The Commission should acknowledge in its Information Paper that it will consider that the effect of any of the issues outlined in section 2.1 of this submission will constitute a failure to provide a service on fair terms and that any failure to supply subscription television services on fair terms to be anti-competitive.

The Commission should also consider whether to prohibit Telstra from discounting telecommunications services as a condition of a customer acquiring a bundle until competition has been fully developed in emergent markets.

- (c) **Licence conditions:** The Commission should consider whether the ABA should be requested to impose a condition on Foxtel's subscription television broadcasting licence that Foxtel cannot refuse to supply subscription television services on fair terms and the ACA to impose a condition on Telstra's carrier licence that Telstra cannot refuse to supply telecommunications services which are essential inputs for the purposes of bundling on fair terms.

- (d) **Part XIB scope:** Part XIB has proven to be the only effective enforcement mechanism by which the Commission has been able rapidly to curtail anti-competitive conduct in telecommunications carriage service markets. The same competitive environment exists now in subscription television markets as existed at the time Part XIB was introduced in 1997 and further amended in 1999 to address the risk of anti-competitive conduct in carriage services markets. As Foxtel has scope to effect a price squeeze or engage in predatory pricing conduct, the Commission should examine whether Part XIB of the TPA and amendments implemented by the *Telecommunications Competition Act 2002* (Cth) should apply to content service providers as well as carriers and carriage service providers.