FOXTEL Undertakings Allay ACCC's Competition Concerns Over AUSTAR Acquisition

Ross Zaurrini and Ben Teeger take a look at the recent decision by the ACCC not to oppose FOXTEL's acquisition of AUSTAR. This article considers the review of the transaction conducted by the ACCC, the court-enforceable undertakings proffered by FOXTEL and the implications for the subscription television services and telecommunications industries.

In brief

On 10 April 2012, the Australian Competition and Consumer Commission (***ACCC***) announced that it would not oppose FOXTEL Management Pty Limited's (***FOXTEL's***) acquisition of AUSTAR United Communications Limited (***AUSTAR***).

In the course of a lengthy merger review process, conducted by the ACCC , FOXTEL offered (and the ACCC accepted) a court-enforceable undertaking from FOXTEL. The undertaking, which secured regulatory clearance of the transaction, prevents FOXTEL from, among other things, obtaining certain exclusive content rights.

Proposed acquisition

On 26 May 2011, FOXTEL announced its proposal to acquire AUSTAR by way of a Scheme of Arrangement (***Scheme***).[1]

FOXTEL is Australia's largest subscription television services provider. It provides services to over 1.6 million households in predominately metropolitan areas of Australia. FOXTEL offers over 200 channels, ranging from news and documentaries, entertainment and movies, sport, music and children's programming. FOXTEL is ultimately owned by Telstra Corporation Limited (**Telstra**) (50%), News Corporation Limited (25%) and Consolidated Media Holdings Limited (25%).

AUSTAR is a subscription television services provider to over 750,000 subscribers in mainly rural and regional areas in Australia, as well as the Gold Coast, Darwin and Hobart. It listed on the Australian Securities Exchange in 1999. The majority shareholder of AUSTAR is Liberty Global, Inc (a Delaware Corporation).

When the proposed acquisition was announced, then FOXTEL CEO, Kim Williams AM, described the proposed Scheme as a 'win-win transaction that delivers value to AUSTAR shareholders, synergies and growth opportunities for FOXTEL and increased services and choice for all consumers'.[2] The proposed Scheme was valued at approximately $2 billion.

The transaction was formally entered into by the parties on 11 July 2011 and was subject to a condition precedent requiring approval by the ACCC.

ACCC review

Statutory and regulatory regime

While parties to a merger are not legally required to notify the ACCC, proceeding without regulatory approval risks the ACCC (or another interested party) seeking an injunction to prevent the transaction being completed, on the basis that it contravenes section 50 of the *Competition and Consumer Act 2010* (Cth) (***Act***).

The ACCC was concerned that because FOXTEL and AUSTAR are the only significant providers of subscription television services in Australia, the proposed merger would create a near monopoly subscription television provider across Australia.

Section 50 of the Act prohibits any acquisition of shares or assets that would have the likely effect of substantially lessening competition in any market in Australia. Whether or not a transaction is likely to have that effect will depend on factors such as:

- the likelihood that the acquisition will result in the acquirer being able to significantly increase prices;
- the likelihood that the acquisition will result in the removal from the market of a vigorous and effective competitor; and
- the dynamic characteristics of the market, including growth, innovation and product differentiation.

Where there is a material risk that a transaction raises competition concerns under the Act (and therefore the potential for regulatory interference from the ACCC) , merger parties typically seek clearance from the ACCC under its informal merger clearance process. That process is governed by the ACCC's Merger Guidelines[3] and process guidelines.[4] It typically involves the ACCC gathering information from the merger parties and interested market participants to

1 A Scheme of Arrangement is a commonly used method to transfer all of the shares in one company (the Target) to another company (the Acquirer). It is a court controlled and sanctioned process under Part 5.1 of the *Corporations Act 2001* (Cth).

2 FOXTEL, Media Release: 'FOXTEL announces proposal to acquire AUSTAR', 26 May 2011, http://www.asx.com.au/asxpdf/20110526/pdf/41yw0z2wbjyq3d.pdf.

3 Australian Competition and Consumer Commission, *Merger Guidelines*, November 2008, http://www.accc.gov.au/content/item.phtml?itemId=809866&nodeId=3a4cf8c822dc673b7de0a525ac267933&fn=222_Merger%20guidelines_FA_WEB.pdf.

4 Australian Competition and Consumer Commission, *Merger Review Process Guidelines,* July 2006, http://www.accc.gov.au/content/item.phtml?itemId=740765&nodeId=31d493c38b88d05e189fc14d8a826d6b&fn=Merger%20Review%20Process%20Guideline.pdf.
Australian Competition and Consumer Commission, *Merger Review Process Guidelines Addendum,* May 2011, http://www.accc.gov.au/content/item.phtml?itemId=740765&nodeId=05044df92fd86ce01b530f0e413b1ccc&fn=Merger%20Review%20Process%20Guidelines%20Addendum.pdf.

determine whether the transaction is likely to impact on competition and, if so, in what ways. If, following an informal merger review, the ACCC decides it does not oppose a transaction, the merger parties will consider themselves free (at least for competition law purposes) to complete the transaction.

FOXTEL/AUSTAR review process

The ACCC's review of this transaction commenced on 26 May 2011 and was not completed until 10 April 2012.[5] This was an unusually long review period as the ACCC had 'stopped the clock' on a number of occasions awaiting further information from the merger parties. The ACCC also received submissions from various industry participants, including subscription television providers, free-to-air (***FTA***) television operators, content owners and telecommunications companies.

to the extent that FOXTEL's (and its shareholders') ownership of exclusive sports rights may raise competition concerns, these concerns existed independently of the proposed acquisition

On 22 July 2011, the ACCC published a Statement of Issues, outlining its preliminary views on the proposed transaction,[6] namely, that the transaction would likely result in a substantial lessening of competition in:

- the national market for the supply of subscription television services;
- the national market for the acquisition of audio visual content; and
- a number of markets for the supply of telecommunications products.

National market for subscription television

The ACCC was concerned that because FOXTEL and AUSTAR are the only significant providers of subscription television services in Australia, the proposed merger would create a near monopoly subscription television provider across Australia.

Notwithstanding that there was little direct competition between FOXTEL and AUSTAR (principally only on the Gold Coast), the ACCC's preliminary view was that the level of competition between them was likely to increase in the absence of the transaction (and that, as a result, expected increases in competition would be lost).

In particular, the ACCC considered that:

- significant technological developments (eg, the use of Internet Protocol Television (***IPTV***) and delivery of content to internet enabled devices such as gaming consoles); and
- significant industry changes which are likely to occur in the foreseeable future, including the rollout of the National Broadband Network (***NBN***),

have the potential to facilitate expansion and/or new entry by FOXTEL and AUSTAR into new product and geographic markets, thereby increasing competition between them.

Additionally, the ACCC considered that:

- alternative subscription television providers and FTA television operators are unlikely to be sufficiently close competitors to constrain the merged firm after the acquisition; and
- high barriers to entry and difficulties faced by new entrants in obtaining access to substantial television content mean that the threat of new entry is unlikely to constrain the merged firm after that acquisition. Indeed, the acquisition would increase barriers to entry and create a merged firm many times larger than its nearest rival.

National market for acquisition of audio visual content

The ACCC's preliminary view was that there was likely to be a substantial lessening of competition in the market for the acquisition of audio visual content, as a flow-on effect from the lessening of competition in the national market for the supply of subscription television services (ie, fewer subscription television providers will directly lead to fewer buyers of content).

The ACCC was also of the view that the merged firm was likely to be able to effectively discriminate against suppliers of content, on the basis that there are substantial market segments for which there is limited or no competition from FTA television operators and other audio visual content acquirers.

Telecommunications markets

The ACCC's preliminary view was that the proposed acquisition was likely to substantially lessen competition in a number of telecommunications markets. The ACCC highlighted the increasing importance of telecommunications and broadband competitors being able to provide a bundle of three or four services to consumers (including fixed line telephone, mobile telephony, subscription television and broadband internet services), particularly after the rollout of the NBN.

The ACCC also thought that Telstra, through its 50% shareholding in FOXTEL, would be well placed to provide such bundled services. Other telecommunications providers and internet service providers (***ISPs***) reportedly raised concerns that because they lack corporate or commercial links to subscription television providers of substantial scale, they would be at a disadvantage relative to Telstra in being able to provide consumers with a bundle of services. The ACCC suggested that AUSTAR was an important future competitor in providing bundled services (either by itself or in partnership with telecommunications providers and ISPs), which would be lost if the acquisition was allowed to proceed.

Following the release of the Statement of Issues, the parties were given an opportunity to provide further submissions and conduct further negotiations to attempt to allay the ACCC's competition concerns. In fact, the ACCC delayed its proposed decision three times to allow the parties to explore whether a negotiated outcome could be reached.

Court-enforceable undertaking

On 9 April 2012, the ACCC accepted from FOXTEL a court-enforceable undertaking under section 87B of the Act.[7]

Statutory and regulatory regime

Under section 87B, the ACCC may accept a written undertaking from a party to allay any competition concerns identified in connection with a proposed acquisition. The ACCC considers that such undertakings 'play a critical role in administering and enforcing' section 50 and provide a 'flexible alternative to simply opposing an

5 The total number of review days was 106. The total number of review days equals the total number business days minus public holidays and time during which the review was suspended: Australian Competition and Consumer Commission, Merger Register: 'FOXTEL – proposed acquisition of AUSTAR United Communications Limited', http://www.accc.gov.au/content/index.phtml/itemId/1044881.

6 Australian Competition and Consumer Commission, *Statement of Issues: FOXTEL – proposed acquisition of AUSTAR United Communications Limited*, 22 July 2011, http://www.accc.gov.au/content/item.phtml?itemId=998733&nodeId=42186e6c27337ea6b5f4cfe884a51426&fn=FOXTEL%20proposed%20acquisition%20of%20AUSTAR%20United%20Communications%20Limited%20-%2022%20July%202011.pdf.

7 FOXTEL Management Pty Limited, 'Undertaking to the Australian Competition and Consumer Commission', 9 April 2012, http://www.accc.gov.au/content/item.phtml?itemId=1047780&nodeId=71053914f884cb6f54a2c66869f93102&fn=FOXTEL.pdf.

acquisition'.[8] In determining whether undertakings are acceptable, the ACCC considers a range of factors, including the effectiveness of the undertaking to address competition concerns, how difficult the undertaking will be to administer, the ability of the merged firm to deliver the required outcomes, and monitoring and compliance costs. In the event that an undertaking is breached, the ACCC can seek orders from a Court for its enforcement.

The type of undertaking FOXTEL gave was a behavioural undertaking. This type of undertaking prescribes that certain conduct be carried out, directed or avoided by the merged firm on an ongoing basis to minimise its ability to exercise anti-competitive market power. Interestingly, the ACCC accepted this behavioural undertaking in the absence of a structural undertaking.[9] This is unusual because the ACCC's policy is that behavioural undertakings are 'rarely appropriate on their own to address competition concerns'.[10]

Scope of undertaking offered by FOXTEL

To address the ACCC's competition concerns (which FOXTEL did not agree with) and avoid further delay to the transaction, FOXTEL offered undertakings.

The ACCC conducted extensive market inquiries in relation to a draft version of the undertaking offered by FOXTEL. Following market feedback and further discussions with FOXTEL, the nature and scope of content addressed by the non-exclusivity provisions in the undertaking was significantly broadened to obtain the ACCC's approval

The undertaking Foxtel gave prevents it from:

- acquiring exclusive IPTV rights for a range of attractive television program and movie content, including:
    - linear channels supplied by independent content suppliers, including over 60 current FOXTEL channels and other international channels (for example Disney, ESPN and MTV);
    - Subscription Video on Demand (***SVOD***) rights to television programs that form part of a linear channel supplied by an independent content supplier;
    - movie linear channels (or movies for inclusion in a linear channel) from more than 50% of the eight major movie studios or more than 50% of the eight specified independent movie studios; and
    - SVOD rights to movies, except for an 18 month window in relation to new release movies acquired from the movie studios from which FOXTEL is not prohibited from acquiring exclusive linear rights; and
- exclusively acquiring any movie for distribution on a Transactional Video on Demand (***TVOD***) basis; and
- entering into any agreement that prevents a third party from acquiring mobile rights to the above content to combine with IPTV rights (ie, allowing third parties to deliver a bundled package of programming across a number of devices).

The undertaking does not prevent FOXTEL from acquiring exclusive rights in relation to individual sports. The ACCC considered that to the extent that FOXTEL's (and its shareholders') ownership of exclusive sports rights may raise competition concerns, these concerns existed independently of the proposed acquisition. The ACCC stated that it will nevertheless 'continue to consider whether there is a need to advocate for regulatory intervention in these markets.'[11]

ACCC green light

After accepting the undertaking, the ACCC announced on 10 April 2012 that it would not oppose the acquisition.[12] The Scheme was subsequently approved by the Federal Court of Australia on 13 April 2012.

AUSTAR CEO John Porter stated that the merger 'will create an even greater Australian media company, one that will continue the AUSTAR tradition of innovation, entertainment and customer service excellence'.[13]

FOXTEL will likely take control of AUSTAR in late-May 2012.

The extent to which the ACCC actively monitors FOXTEL's compliance with its undertaking remains to be seen

Implications

A number of important lessons can be learned from the FOXTEL/AUSTAR experience with the ACCC:

- There is real potential for ACCC regulatory approval to scuttle (or at least significantly delay) a proposed transaction in the telecommunications/media sector given the increasing concentration of ownership of particular media. In this case, the transaction took more than ten months to clear the ACCC regulatory process and, even then, only with the making of significant concessions. Some transactions, quite simply, could not withstand such regulatory delay;
- The ACCC's willingness to accept behavioural undertakings to allay its competition concerns, is interesting. For many years, the ACCC has simply refused to accept undertakings which rely solely (or even predominantly) on, in effect, a 'promise' from a merger party to limit the activity in which it engages. The extent to which the ACCC actively monitors FOXTEL's compliance with its undertaking remains to be seen;
- Notwithstanding obvious convergence in recent years across media platforms and technology, the ACCC's primary position appears to be that, for the purposes of Australian competition law, separate markets exist across different modes of content delivery. For example, the ACCC is of the view that subscription television and FTA television are in different markets (ie, they are not closely competitive). This reflects the Federal Court of Australia's decision in the C7 case;[14] and
- The ACCC's view on markets has implications for the Australian Government's Convergence Review. There is a real question to be answered; whether section 50 of the Act is adequate to protect against concentration in cross-media ownership, in circumstances where the ACCC appears likely to conclude that traditional forms of media, such as television, radio and newspapers, and dynamic forms of new media, each remain in separate markets for competition law purposes.

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8 ACCC, *Merger Guidelines* ,above n 3, at 62.

9 A structural undertaking is an undertaking which provides for one-off actions that alter the entry conditions or the relationships in a particular industry (for example, divestment of part of a merged firm).

10 ACCC, *Merger Guidelines* ,above n 3),at 63.

11 Australian Competition and Consumer Commission, News Release: 'ACCC not to oppose AUSTAR acquisition after undertaking resolves concerns', 10 April 2012, http://www.accc.gov.au/content/index.phtml/itemId/1044888/fromItemId/142.

12 ACCC, News Release, 10 April 2012 (above n 11).

13 AUSTAR, Media Release, 'AUSTAR welcomes court approval for FOXTEL transaction', 13 April 2012, www.AUSTARunited.com.au/file/609.pdf.

14 *Seven Network Ltd v News Ltd* (2009) 182 FCR 160 per Mansfield, Dowsett and Lander JJ; *Seven Network Ltd v News Ltd* [2007] FCA 1062 per Sackville J.