# ACMA review of radio broadcasting standards

## A report for Commercial Radio Australia

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# 1. Overview

## 1.1. Engagement

1. Commercial Radio Australia (CRA) has engaged the Competition Economists Group (CEG) to undertake an assessment of the economic impact of amendments to the commercial radio standards proposed by the Australian Communications and Media Authority (the ACMA).

2. In particular, CEG has been asked to estimate the impact of amendments to the standards that:

   - tighten the Advertising Standard so that integrated advertising (eg, live reads) are prohibited or so that greater prescription is imposed on how advertising should be distinguished from other content; and
   - broaden the scope of the Disclosure Standard to include persons with control over content, and/or to cover programming other than current affairs programming.

3. In addition we have been asked to provide a critique of the ACMA's research paper, *Reform of the Commercial Radio Standards: A review of the expected economic costs*, March 2011.

4. To inform our views on the amendments proposed by the ACMA, we have collected empirical evidence from a sample of CRA's member commercial radio stations by way of a survey, which is described in more detail in Appendix C.

## 1.2. Key conclusions

5. Based our research and the analysis outlined in this report we have reached the following conclusions:

   i. The ACMA's analysis of the economic/welfare impact of its regulatory proposals is deficient, as it has not weighed the benefits and costs of amending the standards.

   ii. Live reads and integrated advertising that are in the nature of product endorsement are likely to be welfare enhancing and merit, at most, modest disclosure requirements.

iii. A tightened Advertising Standard is likely to create a welfare loss to society by reducing the benefits to consumers of media and advertisers and imposing compliance costs on the industry.

iv. There may be a stronger case for regulating commercial agreements that are broader than product endorsement – such as agreements to promote a particular industry or the attributes of a company.

v. The benefits of broadening the Disclosure Standard to include infotainment programming would likely be negative.

vi. If the broadened Disclosure Standard captures agreements with the licensee relating to product endorsements it is likely to be unworkable and/or highly costly to comply with.

## 1.3. The ACMA's economic assessment is deficient in important respects

6. In its review of expected economic costs the ACMA has indicated that it will assess alternative regulatory options according to a 'total welfare standard'. We agree that this is the appropriate approach to assess a range of possible regulatory options, and that the option that creates the greatest net benefit to society should be chosen.

7. In our view however, the ACMA's analysis of the economic/welfare impact of its regulatory proposals is deficient in several respects, as outlined below.

8. First, the ACMA does not appear to have undertaken any substantive assessment of the benefits of its regulatory proposals. That is, it has not sought to estimate the incremental benefits to society of tightening (or relaxing) the Advertising Standard or broadening the Disclosure Standard. This is a serious omission as it prevents the ACMA from determining whether or not the benefits of increasing regulation exceed the costs – the comparison which is the basis of the total welfare standard.

9. We note that the ACMA relies on the outcomes of its survey of community attitudes to radio content as evidence of a need for regulation (ie, the existence of benefits). In our opinion, the ACMA's survey of community attitudes is both an inaccurate and biased indicator of the benefits of regulation. This is because a strong elicited desire for regulation need not be associated with large net benefits – any more than a strong elicited desire for shorter waiting lists at public hospitals is an indication of the net benefits of substituting resources to hospital spending and away from the production of other goods and services.

10. The use of surveys to determine regulatory policy directions is fraught with the risk of unintended consequences. This is true even for the most well designed survey because respondents are inevitably (rationally) ill-informed about the complex consequences that can flow from regulation. However, this is especially true of the ACMA survey as it does not include any quantitative assessment of consumer attitudes towards the (counterfactual) effects of regulation. In fact, to the extent that the ACMA has sought qualitative data on consumer attitudes on extended disclosure announcements or additional spot schedules, it shows that nearly as many listeners found disclosure announcements annoying and that spot advertisements interrupted their listening pleasure.

11. In reality, the potential benefits of regulation as intuitively perceived by a respondent may well be illusory. For example, consider a situation where instead of a radio presenter performing a 'live read' of a product endorsement, a well-known sportsman in a 'spot schedule' advertisement provides that same product endorsement.[1] Is society any better off as a result of this change? The answer to this question involves a number of complex interactions and depends on which type of advertisement:

    i. is more effective at communicating useful information to consumers (ie, causes consumers to alter their consumption patterns in a way that increases their welfare);

    ii. is least likely to communicate harmful information to consumers (ie, causes consumers to alter their consumption patterns in a way that reduces their welfare);[2]

    iii. costs more to produce; and

    iv. is least disruptive and/or annoying to the audience's listening experience.

12. In relation to the first two points, there is no evidence that spot schedule advertising is more effective at promoting welfare enhancing consumption patterns than integrated advertising. Moreover, there are good reasons to believe that the opposite is likely to be true (as discussed below).

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1 A 'spot schedule' is the industry terminology for a pre-recorded advertisement.

2 For completeness, we note that this analysis is not intended to minimise the "public information" or "public
2 For completeness, we note that this analysis is not intended to minimise the "public information" or "public discourse" benefits of disclosure, which are further considered at paragraphs 34 below

13. In relation to point iii) there is evidence that integrated advertising involves a lower cost of production. In relation to point (iv) when integrated advertisements are low in frequency it is least disruptive to the audience's listening experience. Taken together, the expected net benefit of any regulatory change that shifts advertising from integrated advertising to spot schedule advertising is very likely to be negative.

14. The second reason why, in our view, the ACMA analysis of the economic/welfare impact of its regulatory proposals is deficient is that it involves no evaluation of the direct cost of regulation for the industry (and society). It has not, for example, sought to estimate the administrative and compliance costs of implementing the proposed amendments to the standards.

15. Third, the ACMA's review of expected economic costs appears to focus on 'arguing the case' that the effects of its regulatory proposals will largely involve transfers between members of society rather than being costs to society as a whole (eg, a reduction in revenue from commercial agreements will lead to higher revenue from spot schedules or from advertisements/agreements in other media). However, as discussed below, the substitution of revenues may involve real economic costs if the substituted forms of advertising are less efficient (ie, less effective or more costly).[3]

16. The ACMA appears to understand this issue (at least in part) when it observes that:[4]

> *If … commercial agreements are a lower cost (more efficient) means of advertising, substitution away from commercial agreements will require additional amounts of money on standard advertisements to achieve an equivalent effect. This would be considered as an economic cost*

17. Despite this observation, the ACMA make no attempt to quantify these economic costs. This means that even if the ACMA's conclusion that revenues will be perfectly substituted within and across media platforms is accepted, it has ignored potentially substantial costs to society from that substitution.

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[3] Also, if it results in some advertising not happening at all this will come as a straight loss to society.

[4] ACMA, Reform of the Commercial Radio Standards: A review of the expected economic costs, page 2.

## 1.4. More detailed summary of conclusions

### 1.4.1. Cost benefit assessment needs to be assessed against the status quo

18. When assessing the net benefits of a change it is necessary to identify the factual and counterfactual outcomes. The factual outcome is the outcome expected from regulatory *status quo*, and the counterfactual outcome is the outcome expected from any given change to the *status quo*.

19. In the case of the Advertising Standard, the factual outcome is that integrated advertising remains subject to the existing requirements to make it distinguishable from other content. The counterfactual is that integrated advertising is prohibited or more prescriptively regulated.

20. In the case of the Disclosure Standard, the factual outcome is that only current affairs presenters are subject to the disclosure requirements. The counterfactual is that persons with potential influence over current affairs content and/or presenters of infotainment programs also become subject to the Disclosure Standard.

### 1.4.2. The incremental benefits of amending the Advertising Standard are likely to be negative

21. The key source of benefit from the proposed amendments to the Advertising Standard is that consumers' consumption patterns will become more efficient as a result of their choices not being influenced by a radio presenter's endorsement or positive discussion of a product that was not clearly labelled as paid advertising.

22. To the extent that such benefits exist, their accrual needs to be assessed as the difference in benefits between the factual and the counterfactual. The accrual of benefits can therefore be estimated as:

> *The gain in consumer surplus from consumers purchasing different products in response to spot schedule advertisements (or live reads and integrated advertisements with more prescribed disclosure) then they would have purchased in response to advertising allowed under the existing Advertising Standard.*

23. Any such gain in consumer surplus is inherently difficult to quantify, as it requires an estimate of the number of consumers who would purchase different products than they do now and an estimate of the difference in consumer surplus derived from their decision to do so. Moreover, it is perfectly possible that the gain will be negative in that consumer consumption patterns will be adversely affected by a shift from integrated advertising to spot schedule advertising.

24. Unfortunately, neither the ACMA nor we have data to quantify this effect. This is problematic given that it is the key benefit identified with the ACMA's proposed amendments to the Advertising Standard.

25. In principle, we would expect the gain from the proposed amendments to be either zero or negative. We hold this view because:

    i. Advertising is, on average, welfare enhancing to consumers and producers. Advertising plays an important role in information dissemination and as a signal of product quality to consumers. Integrated advertising is, in many circumstances, more effective in this role than 'spot schedule' advertising, and this is reflected in the premium price paid for this form of advertising.

    ii. There are existing requirements to distinguish advertising from other content on the radio, including those stipulated in the Advertising Standard and in the general trade practices law relating to misleading and deceptive conduct.

    iii. If the choice between products is such that it will be tipped in one direction or another by the endorsement of radio personalities then the intrinsic difference in consumer surplus from the alternative products is likely to be small.

    iv. The consumption decisions that are influenced by the endorsements of radio personalities may be similarly influenced by endorsements by the same or other personalities in spot schedules or live read and integrated advertisements with more prescriptive disclosure rules.

    v. Radio personalities with current affairs programming are heavily invested in their own reputation and have potentially very long lived careers. As a result, they have a strong incentive to preserve their reputation by endorsing only reputable products. By contrast, sporting personalities and other celebrities with less invested in reputation and more limited career time horizons likely have a lesser incentive to preserve their reputation.

26. We have estimated the reduction in producer surplus from less effective advertising based on the premium that is charged for live reads and integrated advertisements over spot schedules. We estimate that banning live reads and

integrated advertising would reduce producer surplus by around $83.7 million per year.[5]

27. Putting aside the likely impact of changes in listener consumption patterns, the current regulation has the key benefit of allowing flexibility in advertising formats, which in turn ensures radio audiences the most effective and least disruptive listening experience. Less disruptive advertising makes listening to the radio more enjoyable (in economic terms, creating consumer surplus). We have estimated the reduction in consumer listening enjoyment, caused by additional minutes of content being replaced by advertising, at around $291.0 million.[6]

28. In addition, if the effect of tightening the advertising standard is to lower the advertising revenues for the industry (either through lower priced advertisements on radio or a shift of advertising revenue to other media) we would expect the quality of radio programming to fall. Whilst the quality of other media would be expected to rise (with advertising revenue being diverted to them), the net effect would be negative for consumers overall. This is because the mix of quality of radio and other media will be distorted from its current (more efficient) levels.

### 1.4.3. The incremental direct and indirect costs of amending the Advertising Standard appear significant

29. The commercial radio industry incurs direct costs associated with meeting the existing Advertising Standard. We estimate the annual cost of compliance with the existing Advertising Standard at around $6.1million per year.

30. A more prescriptive Advertising Standard would require the industry to incur additional costs. These would include internal costs on training and systems, additional personnel to monitor disclosure of live reads and integrated advertisements and external costs of for example legal advice. We estimate the cost of additional training in the order of $4.8million for the industry as a whole. We discuss monitoring costs in the section on incremental costs of the disclosure standard (below).

5 We consider this to be conservative given we have not estimated any loss in benefit from moving to alternative (less effective) forms of media or estimated a loss in benefit from some products no longer being advertised.

6 As discussed in the body of the report, this estimate is based on very limited data on the nuisance cost of radio advertising.

31. In addition, more prescriptive advertising regulation would result in indirect economic costs associated with substitution of advertising away from live reads and integrated advertisements on the radio to spot schedule advertisements on the radio or advertising on other media (eg, print, television or on-line). Substitution to other forms of advertisements creates an economic cost (ie, not a transfer) if the other forms of advertisements are less efficient, that is, if they require greater production resources and/or are less effective than live reads or integrated advertisements on radio.[7] Compared to the production of spot scheduled advertisements, live reads and integrated advertisements typically involve fewer production resources. For example, producing a live read requires the input of a copywriter and does not generally require production staff. Similarly, an unscripted integrated advertisement may involve little or no production.

32. We estimate the substitution of all live reads and integrated advertisements to spot schedules to cost in the order of $100 million per year.[8]

33. We do not have sufficient data to quantify the economic cost of substitution of advertisements to other forms of media with less restrictive advertising controls. In principle this may be a reasonably significant cost if the alternative media involves higher production costs or is a less effective form of advertisement.[9] This appears to be a reasonable conclusion given the 'revealed preference' is for those ads to be on the radio rather than on the other media.

### 1.4.4. Current affairs versus other programming

34. A benefit of the Disclosure Standard is that there is a lesser likelihood that listeners' understanding of current affairs issues and public policy debates is coloured by undisclosed commercial agreements. The fact that there is scope for these kinds of commercial agreements on current affairs programs provides a basis for some restrictions relating to current affairs programmes. However, one would ideally distinguish between these kinds of commercial agreements and product endorsement agreements.

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7 We have included the difference in effectiveness of the different forms of advertising in the assessment of relative benefits of the proposed amendments to the Advertising Standard.

8 This cost consists of direct costs of approximately $17 million and $84 million of lost surplus per year.

9 We have not included the relative effectiveness of different forms of media in our assessment of the relative benefits.

35. In our view, a distinction can be drawn between agreements for product endorsements and agreements involving radio personalities in public policy discussions. Some vested interests may engage in commercial agreements with presenters and/or licensees in an attempt to elicit favourable commentary. Examples of this may relate to new taxes on a particular industry or regulation of a particular sector.

36. For the reasons already discussed, integrated advertising in the nature of product endorsement are likely to be welfare enhancing and merit, at most, modest disclosure requirements. A product endorsement can be defined as relating solely to the quality and/price characteristics of a particular product or product line.

37. It is less obvious that there is likely to be welfare benefits from other forms of commercial agreements that are broader in nature – such as an agreement to promote a particular industry or the attributes of a company (eg, statements to the effect that Company X is a good employer/ corporate citizen etc). For these forms of commercial arrangements the current disclosure requirements may be appropriate.

38. Drawing a distinction between product endorsements and commercial agreements with public policy implications may also render workable the extension of the disclosure arrangements to the licensee. Given the licensees' wide ranging relationships and agreements with advertisers and others, it is likely that any disclosure requirement that captured all of these would make current affairs programming unworkable. For example, disclosure would be required if reporting on a labour strike at any one of the multitudes of advertisers. However, if only arrangements that went beyond product endorsement were captured then this would substantially reduce the impact on current affairs programming.

39. The above discussion should not be taken to suggest that we consider that there is a clear case for disclosure regulation of non-product endorsement commentary - only that the case for this is stronger than for product endorsement.

40. The case for disclosure regulation of non-product endorsements is inherently difficult to quantify and will depend on the extent to which:

- radio presenters are willing to alter their stated views in order to attract integrated advertising revenues; and

- this is any different to their willingness to alter their stated views in order to attract spot schedule advertising;

41. Radio broadcasters have an influence on the community's knowledge of current affairs issues and the influence of that on public policy outcomes. On some matters this may be significant, whilst on others it may be small.

42. An assessment of these benefits would inevitably turn on the effectiveness of the existing Disclosure Standard at ensuring that commercial agreements are appropriately disclosed and a belief that those persons captured by the proposed amendments have commercial agreements that influence current affairs content.

43. We would, however, conclude that the benefits of broadening the Disclosure Standard to include infotainment programming would likely be negative. This is because integrated advertising on such programmes will relate to product endorsements and, for the reasons already discussed, we consider that these are likely to be welfare enhancing relative to the counterfactual.

44. The counterfactual of a broadened Disclosure Standard would be likely to have two effects. First, it would increase the time spent broadcasting statements relating to commercial agreements, and second, it would result in a substitution from commercial agreements to other forms of advertisement (eg, spot schedules or advertisements in other media). We estimate the loss in benefits from introducing hourly disclosure announcements to infotainment programming and extending disclosure requirements to the licensee at around $22 million per year[10].

### 1.4.5. Estimates of direct incremental costs of amending the Disclosure Standard

45. Licence holders broadcasting current affairs programming incur direct costs in complying with the existing Disclosure Standard. We estimate the annual cost of compliance with the existing Disclosure Standard at around $2.4 million per year, or $46,200 per year per licence holder broadcasting current affairs programs.

46. Broadening the Disclosure Standard to people other than presenters with potential influence on the content of current affairs programming will require additional administration systems to ensure that commercial agreements with

[10] We estimate the loss in benefits as the sum of the opportunity cost to the licence holder of lost advertising revenue from the time spent on disclosure announcement, consisting of 15 second statement per hour.

these people are disclosed. We estimate the cost of expanding existing administration of commercial agreements to be in order of $3.5 million per annum across the industry.

47. Broadening the Disclosure Standard to include infotainment would significantly expand the amount of programs captured by the standard. We estimate that an additional 240,688 minutes of programming across all commercial radio stations per year would be captured. We estimate the cost of administering systems to ensure that the commercial arrangements of presenters and other persons potentially involved in the content of infotainment programming to be in order of $2.8 million.

48. In addition, to ensure disclosure of what may be many commercial agreements is responsive to the changing conversations in live broadcasting, and additional personnel may be required to ensure proper disclosure. The responsibility to monitor disclosure falls on a wide range of employees of radio stations. A number of licensees indicated compliance with the standards was part of the job description of <u>all</u> employees.

49. A broadening of the disclosure standard to include commercial agreements with the licensee would substantially increase the exercise. We estimate that the cost of additional monitoring of amendments to the disclosure and advertising standards could cost in the order of $21.8 million if it involved significant real-time monitoring of disclosures and integrated advertising.

### 1.4.6. Summary of empirical analysis

50. As noted above, CEG has undertaken a survey of CRA members to gather information to allow it to undertake its own estimates of the benefits and costs of the ACMA's regulatory proposals.

51. The key estimates are summarised in the following table (not all costs and benefits have been quantified).

**Table 1: Quantifying costs and benefits of proposed amendments**

| Incremental benefits and costs quantified in this report | Annual cost (2010) | Reference section |
|---|---|---|
| *Cost of complying with existing standards* | | |
| Disclosure Standard | $2.4 million | 4.2.1 |
| Advertising Standards | $6.1 million | 3.2.3 |
| *Net benefits from proposed changes to the advertising standard* | | |
| Cost of banning live reads / integrated advertising (reduction in producer surplus) | $83.7 million | 3.1.1 |
| Cost of banning live reads (reduction in consumer surplus) | $291.0 million | 3.1.2 |
| Cost of renegotiating advertising contracts with integrated elements | $3.3 million | 3.2.3 |
| Cost of additional training to comply | $4.8 million | 3.2.3 |
| *Net benefits from proposed changes to the disclosure standard* | | |
| Incremental cost of complying if expanded to other persons with influence over current affairs | $3.5 million | 4.2.2 |
| Incremental cost if expanded to infotainment presenters | $2.8 million | 4.2.3 |
| Cost of introducing hourly disclosure statements | $21 million | 4.2.4 |
| Incremental cost of increased monitoring to comply with broadened Advertising and Disclosure Standard | $21.8 million | 4.3 |

52. The figures in the table above represent our estimates based on the available information. In the body of the report we have made explicit our assumptions and, where appropriate, undertaken sensitivity analysis around these estimates.

# 2. Issues with the ACMA's approach to reviewing the standards

53. The ACMA imposes standards (regulation) on commercial broadcasters in relation to the disclosure of commercial agreements (the Disclosure Standard)[11], advertising (the Advertising Standard)[12] and compliance (the Compliance Standard). The compliance standard is in place to ensure there is a compliance program to implement the Disclosure Standard, the Advertising Standard and other regulatory obligations and codes of practice.

54. The ACMA is currently undertaking a review of the commercial radio standards. This review comes 10 years after the standards were introduced as a result of the Commercial Radio Inquiry in 2000.

55. In February 2010, the ACMA released an Issues Paper outlining the scope for the review, including a framework for assessing whether or not to vary the standards and how any variations would be made.[13] At that time, it released a number of research papers including research on listener attitudes to radio programming and advertising.[14] The ACMA has relied extensively on this research in developing its rationale for regulation and its regulatory proposals. In addition, in March 2011 the ACMA released an economic assessment of the standards[15] and an Options Paper proposing variations to each of the standards [16].

56. We have considered the ACMA's approach outlined in each of these papers.

## 2.1. Whether or not to regulate must be based on sound economic principles

57. A threshold question for the ACMA is whether or not to regulate (or expand the regulation of) commercial arrangements and advertising on commercial radio.

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[11] Broadcasting Services (Commercial Radio Current Affairs Disclosure) Standard 2000

[12] Broadcasting Services (Commercial Radio Advertising) Standard 2000

[13] ACMA, *Review of the commercial radio standards*, Issues Paper, February 2010.

[14] Ipsos MediaCT, *Listener attitudes to advertising, sponsorship and influence on commercial radio*, Research report prepared for the ACMA, February, 2010, ("Listener attitudes research").

[15] ACMA, *Reform of the Commercial Radio Standards: A review of the expected economic cost*, March 2011.

[16] ACMA, *Review of the commercial radio standards: Options paper*, March 2011.

58. At the level of principles, the ACMA states that in its approach it will analyse the costs and benefits and consider regulation only when it is clear that the benefits outweigh the costs. This is consistent with the ACMA's general standard for regulation, that is, the total welfare standard. The total welfare standard implies that the most appropriate alternative is the one that generates the greatest net benefits for society as a whole:[17]

> *… when assessing the net benefits for the community of competing regulatory options, one of the tools the ACMA uses where applicable is a Total Welfare Standard (TWS) approach. With its foundations in welfare economics, the TWS takes into account the benefits and costs to consumers and producers and the broader social impacts directly arising from a regulatory initiative.*

59. The Issues Paper states:[18]

> *The ACMA … must clearly analyse the costs and benefits of undertaking regulatory action and needs to consider alternatives to formal regulatory action before deciding that regulation is necessary.*

60. We consider the balancing of costs and benefits to be the appropriate approach to policy making, as it is in society's best interest to adopt regulation only when it has net benefits for the society as a whole. However the analysis in this report leads us to conclude that the ACMA has not appropriately identified and analysed the net benefits from its reform proposals.

## 2.2. Reliance on 'community concerns' from listener attitudes surveys risks inaccuracy and bias in policy outcomes

61. Relying on surveys of listener attitudes to determine the need for regulation will inevitably lead to poor public policy outcomes. Such surveys give the ACMA no basis on which to weigh the costs and benefits of each regulatory option.

62. In our opinion, the ACMA's survey of community attitudes is both an inaccurate and biased indicator of the benefits of regulation. This is because:

[17] ACMA, Issues paper, page 12.

[18] ACMA, Issues paper, page 12.

- A strong elicited desire for regulation need not be associated with large net benefits. This is particularly the case when questions are asked in a qualitative manner without framing the broader public policy issues.
- The ACMA's does not capture community attitudes towards the negative consequences of regulation in a manner such that they can be compared with the positives from regulation.

63. Both of these factors are evident in the research undertaken for the ACMA.

64. First, the survey has elicited a reasonably high proportion of responses (37.8%) suggesting that listeners are 'very concerned' about advertising being distinguishable from other content on the radio. However, there is no information from the survey as to how relevant radio advertising is to listeners' subsequent purchasing decisions. As the survey is framed in the context of 'today we are asking you about your concerns regarding commercial radio', the responses need to remain within that frame also.

65. Further, the ACMA found that a majority of listeners (53.1%) accepted that there will be "blurring of advertising and other program material"[19], and that the vast majority of listeners (91.5%) had acknowledged the potential of radio talkback being influenced by commercial agreements.[20] These results suggest that the ultimate effect of product representations by presenters on radio on consumer decision-making may be small. That is, in addition to the existing standards constraining the actions of presenters and licensees, consumer are 'on guard' to the influence of advertising on radio content.

66. Second, where the listener survey has sought qualitative data on consumer attitudes for some of the consequences of regulation (eg, extended disclosure announcements or additional spot schedules), it shows that nearly as many listeners who favoured some regulation found disclosure announcements annoying (56.8%) and that advertisements in general interrupted their listening pleasure (61.2%). See Figure 1 below.

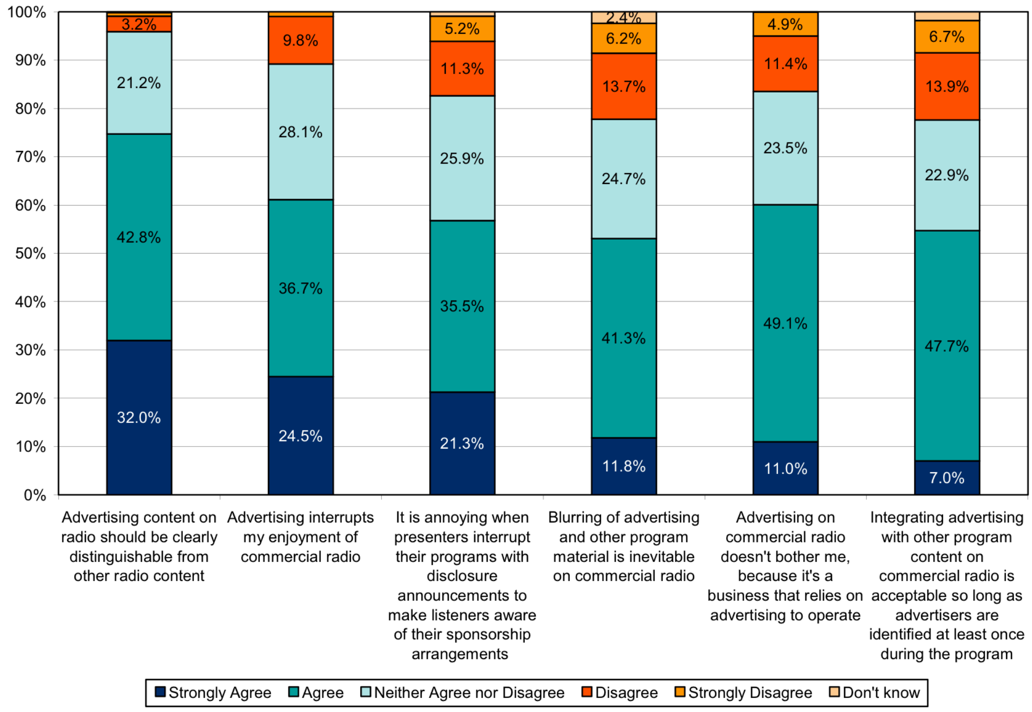
67. As such, the ACMA's survey results give a mixed qualitative picture. On the one hand they indicate that people are concerned about distinguishing advertising from content on radio, but on the other hand they are concerned with the level of

[19] ACMA, Listener attitudes research, page 36.

[20] ACMA, Listener attitudes research, page 33.

advertising on radio interrupting their listening. This research therefore tells the ACMA very little about the cost benefit equation of a regulatory intervention, which would make advertising more distinguishable but led to a greater number of interruptions to programming content.

**Figure 1: Reproduced Figure 18 from ACMA listener attitudes survey**




*Source: ACMA, Listener attitudes survey*

68. An example from another policy area may assist in illustrating our concerns with the ACMA's reliance on surveys of consumer concerns in policy making.

69. It is easy to imagine that a consumer survey is likely to elicit strong community desire for improved hospital funding. If the questions are asked cumulatively one may elicit strong desire for very significant reductions in, or elimination of, waiting times for elective surgery. However, the respondents to such a survey may well be unaware of the complexity of health system and the role of waiting lists in limiting cost blowouts in the health budget (and consequent increases in taxation levels with potentially compounding economic costs associated with high levels of taxation). If actually implemented, the respondents may actually find they are

worse off under the 'waiting list reduction' policy that they profess to support in a survey.

70. There are, of course, many other examples where surveys of customer preferences may indicate a desire for regulation that they find is detrimental to their welfare once it is imposed. For example, price control and rationing of petrol was politically popular in the wake of dramatic increases in the world price of crude oil in the early 1970's. However, the actual implementation of this regulation had unintended consequences and, given this experience, is now generally accepted as a poor policy response.[21]

71. Indeed, it would be rational for most individuals to be uninformed about such unintended consequences because informing oneself about such issues is costly in terms of the respondent's time, and the individual respondents are not themselves charged with making the relevant decisions. This highlights the need to treat surveys of preferences amongst (rationally ill informed) respondents with a high degree of scepticism.

72. In our view, survey evidence of consumer preferences should not be used as a measure of the net benefits of regulation. In our view, expressed views about the relative desire for regulation are unlikely to reflect the relative benefits of a policy because respondents are unlikely to be informed about:

- current levels and operation of regulation;
- the direct and indirect costs of substituting spot schedules for integrated advertising live (including but not limited to the differential cost of production of these kinds of advertising) ; and
- the consequent impact on:
  - the listening experience for consumers of the programs most significantly affected;
  - the economics of radio stations (and radio station programming); and
  - the economics of companies, including rural companies, attempting to effectively communicate to listeners the quality of their products.

[21] This link (http://www.palgrave.com/PDFs/0716799561.Pdf) is to a chapter of Nobel Prize winning economist Paul Krugman's (with Robin Wells and Kathryn Grady) "economics" text book (Worth Publishers) that deals with price controls.

73. This is true even if the survey was designed in an attempt to lessen these problems. However, it is especially true given that ACMA's community attitudes survey respondents were primarily asked about their concerns regarding commercial agreements and advertising disclosure.

## 2.3. Incomplete definition of the policy 'problems' to be addressed

### 2.3.1. Defining the 'problem' the Advertising Standard is seeking to address

74. The ACMA describe the need for the Advertising Standard in the following terms:[22]

> *Regulation requiring that advertising be distinguishable responds to the key challenge that unless commercial radio listeners can discern whether certain broadcast material is in fact advertising, then they are not in a position to know who is seeking to persuade them. It recognises that it may not be clear to listeners whether on-air promotion of organisations, their products, services or issues has been motivated by the existence of a commercial arrangement with the organisation concerned.*

75. However, the ACMA's motivation for regulation is insufficiently articulated because the knowledge that a representation or endorsement of a product or service is an advertisement does not itself create an economic benefit to consumers or society.

76. The economic benefit of that knowledge arises from the greater utility consumers may gain from the 'better choices' they make as a result of that knowledge. By 'better choices' we mean more efficient choices, that is, that maximise the utility of the consumer and direct resources in the economy to achieve that outcome. Regulation therefore provides benefits only to the extent that it changes consumer choice, leading to higher social surplus from consumers buying and producers supplying higher surplus producing products and services.

77. In considering whether to amended the Advertising Standard the ACMA needs to apply a more robust framework than it current approach which amounts to 'knowledge is a benefit, therefore more knowledge provides greater benefits'. In our view the ACMA needs to carefully weigh any incremental benefits to consumers of any greater knowledge from extending the Advertising Standard.

22 ACMA, Issues Paper, Page 37.

78. The ACMA is not starting from a blank slate. The existing Advertising Standard requires licensees to ensure that advertisements are distinguishable from other programs. The test in the standard requires that advertisements be presented in such a way that a 'reasonable listener' is able to distinguish them for other program content. The advertising standard applies to all program formats.[23] The ACMA's research indicates that a higher proportion of consumers believe that advertisements "should be clearly distinguishable from other radio content".[24] The existing Advertising Standard is framed directly to address this outcome.

79. The ACMA has also conducted recent research (in small sample focus groups) that indicates that a high proportion of radio listeners could distinguish live reads from programming content.[25] The same research does however indicate that some forms of advertising that is integrated into the content (eg, in the form of interviews) were not distinguishable from other content to a large number of listeners.

80. The ACMA has not however undertaken any research as to the quantity of advertising that is less distinguishable and the influence it has on consumer decision-making. It has also noted few breaches of the existing Advertising Standard. The absence of this type of research or wide scale breaches makes it difficult to articulate a clear framework for assessing the expected incremental benefits for tightening of the Advertising Standard.

81. Notwithstanding this, the ACMA has developed a proposed variations that seek to tighten the Advertising Standard by:

- requiring all advertising to be distinguishable at the time the commercial material is broadcast;
- having specific regulation for 'integrated advertising' in one of the following ways:

23 The Advertising Standard is additional to general trade practices law requirements that advertising not be misleading or deceptive. That is: a person must not, in trade or commerce, engage in conduct that is misleading or deceptive or is likely to mislead or deceive. This law against misleading and deceptive conduct requires that the impression left by advertising, promotions or representations not mislead consumers as to the features of the product (including price, value or quality). False statements are prohibited under this broad provision.

24 ACMA, Issues Paper, page 37.

25 ACMA, Issues paper, page 42.

- maintain the 'reasonable listener test' but apply the research concerning listeners' particular difficulties in distinguishing integrated advertising in making its decisions;
- prohibit integrated advertising; and
- explicitly state the program standard that integrated advertising must; (a) contain details of the commercial sponsor at the start of the advertisement, and (b) have the tone and style of an advertisement.

- expand the definition of 'consideration' to include both direct and indirect benefits and interests.

82. We note that the ACMA defines integrated advertising to include scripted live reads, live crosses, paid interviews and product placements. In our research a number of licensees considered that it was important to distinguish between these forms of advertising. This appears to be consistent with ACMA's own research that shows that the majority of listeners had no trouble identifying live read scripts as advertisements even when they were read proximate to other content, whilst integrated advertisements including a talkback call and a paid interview were less distinguishable (though 52 percent still identified the paid interview as advertising).[26]

### 2.3.2. Defining the 'problem' the Disclosure Standard is seeking to address

83. The ACMA describes the need for the Disclosure Standard in the following terms:[27]

> *The existing Disclosure Standard has been framed largely as a response to what might be described as the 'listener knowledge' problem: the commercial radio listeners have no way of knowing, without being told, that a particular presenter has a direct commercial interest in a subject being commented on or discussed.*

84. Once again, the ACMA has not adequately articulated a rationale for regulation that can be reasoned on public policy grounds. The economic benefits of increased 'listener knowledge' need to be identified.

[26] Listener attitudes survey, page 31.

[27] ACMA, Issues paper, pages 15-16.

85. In our view, the most logical rationale for regulating commercial agreements is to ensure that listeners' understanding of current affairs issues and public policy debates is not coloured by undisclosed commercial agreements. This is of benefit to society if this leads to a more efficient and effective public debate on public policy issues and policy outcomes that yield higher welfare to society.

86. The existing Disclosure Standard covers current affairs programming where such policy issues are being discussed and where the process of public debate is perceived to be at risk of being effected by commercial agreements. Consistent with the views expressed by the Australian Parliament, the existing Disclosure Standard was motivated by a view that there should be a "fair and accurate coverage of public interest matters", where public interest matters are those that are relevant to the welfare of society as a whole and are integral to public policy debates.

87. It is helpful in our view to make a clear distinction between the motivation to regulate disclosure of commercial agreements which might affect public interest or public policy matters, and those that are associated with product endorsements or consumer choices (which we have discussed above relating to the Advertising Standard). This distinction is helpful because the benefits of greater consumer knowledge in relation to these matters are very different.

88. We note that ACMA do not clearly make such a distinction. For example, in discussing whether to extend the Disclosure Standard to programming other than current affairs, the ACMA state:[28]

> *One issue for consideration in the review is whether regulation should apply to a broader range of programming than current affairs. Should such regulation also apply, for example, to a sports presenter who has a commercial agreement with a sports clothing company, or with the maker of a dietary supplement, to promote the interests of a particular sport?*

89. The ACMA has developed a proposed variation to broaden the existing Disclosure Standard. These include:

    i. Expand its application to cover more than just current affairs programs, in order to cover other material. Regulation could:

[28] ACMA, Issues paper, page 22.

- Apply to factual programs, including current affairs and infotainment programs. Current affairs programs would be defined as in the current standard. Infotainment programs would be defined as meaning 'a program that has the dominant purpose of presenting factual material in an entertaining way; or
- Apply to all public interest material whenever broadcast, regardless of the format of the program.

ii. Expand the application of the regulation to require licensees to be responsible for all of the following:

- Presenter's agreements (same as the current definition);
- Licensee agreements where a relevant presenter has an actual or beneficial interest in the licensee company; and
- Any other agreements where the person concerned has significant influence on the content of the material broadcast. The onus will be on the licensee to determine, who are the persons associated with the broadcaster that may significantly influence the program content.

90. As presented, the majority of the ACMA's proposed variations to the Disclosure Standard would capture all commercial agreements between licensees and advertisers, even when those agreements are for product endorsements. It does this by proposing to extend the Disclosure Standard to infotainment programming and potentially to all commercial agreements between presenters and licensees,[29] even when those agreements relate to product endorsements.

91. This is likely to make the Disclosure Standard unworkable and would severely limit the ability of licensees to enter into product endorsement agreements. For example, as presented, where a licensee had some control of content they would need to disclose all advertising and product endorsement agreements during broadcasts all factual programming and to the ACMA, even when those agreements relate to other programming. The number of these agreements is significant. On average radio licensees that we sampled have about 300 product endorsement agreements each, with some licensees having in excess of 1000 agreements.

92. In our view, the ACMA should differentiate between agreements where licensees or presenters are being asked to influence public policy outcomes by speaking

[29] Where those licensees might be considered to have influence over content.

favourably about a company, industry group or association with a stake in a policy outcome, and agreements relating to product endorsement.

93. It may of course be argued that the continuation of radio presenters and licensees' product endorsement agreements are implicitly based on not making unfavourable comments about a sponsor or advertiser during current affairs or public interest programming. However, this perception is unavoidable in an environment in which broadcasting is commercially operated. There will always remain a perceived risk that a broadcaster might have an incentive to avoid showing unfavourable news stories about major advertisers. However, this incentive only holds to the extent that the broadcaster is willing to give up their 'good reputation' as a broadcaster of news and/or current affairs for an advertiser. This in turn supposes that the advertiser is willing and able to compensate the broadcaster for loss of that reputation.

## 2.4. The ACMA's review of expected economic costs is deficient

94. Together with the options paper, the ACMA released a review of the expected costs of amending the radio standards, particularly the disclosure standard. We consider that the ACMA's economic analysis is deficient in a number of important respects which we discuss in the following sections.

### 2.4.1. The ACMA's conclusion in relation to economic costs and economic transfers

95. The principal conclusion of the ACMA's economic research appears to be that any 'costs to the industry' in the form of lost revenues from commercial agreements or live read/integrated advertisements (from changes to the disclosure or advertising standards) are unlikely to be economic costs to society. The ACMA argues that this is because:

- a reduction in revenue to presenters (or others) from lost commercial agreements due to broader disclosure requirements would be offset by an increase in revenue from paid advertising; and
- a tighter advertising requirement for radio might largely shift revenue from advertising on commercial radio to advertising on other forms of media (eg, television, print, internet)

96. The ACMA characterises the substitution of revenues between parties as economic transfers that do not result in true economic costs to society (ie, that

negatively impact on economic welfare). In our opinion this conclusion is incorrect.

97. This is obvious if you were to simply hypothesise a regulatory proposal which banned all advertising on commercial radio. Following the ACMA's conclusion this would not result in any economic harm if the revenues lost by the industry were transferred to other media. This is clearly incorrect in this case as the entire welfare society gained from commercial radio would be lost including:

- the additional welfare listener's receive from listening to radio compared to consuming other forms of media (which will be lost as the industry would cease);
- the additional surplus society received from businesses advertising more effectively or efficiently on radio than they can on other media;
- the additional surplus society gained from employing staff and resources in radio as opposed to their next best alternative.

98. Whilst this hypothesis is clearly extreme, it serves to demonstrate the nature of costs that might be expected to arise from the regulation of advertising on radio. That is, regulations that raise the cost of advertising on radio would be expected to lessen the profitability of radio station and hence the quality of their content. This is a cost to listeners who prefer radio to content on other media. Similarly, if advertising revenue is shifted to media which is less effective or higher cost, this comes at a cost to society. These are potentially important economic costs that the ACMA has not quantified in its review of expected economic costs.

99. The ACMA appears to understand this issue (at least in part) when it observes that:[30]

> *.. if commercial agreements [live reads] are a lower cost and more efficient means of advertising, substitution away from commercial agreements [live reads] will require additional resources to be allocated to standard advertising to achieve a given outcome. This would represent a cost to society.*
>
> *It is necessary to consider whether strengthening the … Standards would generate benefits to individuals in their roles as citizens or consumers to*

30 Review of expected economic costs, page 20.

*determine whether these costs are justified and the change is likely to increase total welfare.*

100. However, despite this observation, the ACMA do not quantify these economic cost or benefits. This means that even if the ACMA's conclusion is accepted that revenues will be substituted within and across media platforms, it has not been able to assess whether these costs to society outweigh the benefits of regulation.

101. These issues are complex and the ability to quantify the costs and benefits of regulation are restricted by the availability of reliable data. For example, consider a situation where instead of radio presenter performing a 'live read' of a product endorsement a well-known sportsman in a 'spot schedule' advertisement provides that same product endorsement.[31] Is society any better off as a result of this change? The answer to this question depends upon which form of advertising:

   i. is more effective at communicating useful information to consumers (ie, cause consumers to alter their consumption patterns in a way that reduces their welfare);
   ii. is least likely to communicate harmful information to consumers (ie, cause consumers to alter their consumption patterns in a way that reduces their welfare);
   iii. costs more to produce; and
   iv. is least disruptive to the audience's listening experience.

102. In this report, we seek to answer these questions with the limited empirical evidence available.

### 2.4.2. The ACMA's analysis of substitution of revenues

103. The bulk of the ACMA's review of economic costs is spent on examining anecdotal and empirical evidence to test whether commercial agreements are perfect or imperfect substituted for spot schedule (paid) advertising (ie, to estimate the cost of broadening the Disclosure Standard).

[31] 'A spot schedules' is the industry terminology for a pre-recorded advertisement.

104. The ACMA state that if they are good substitutes then:[32]

> *… it would be reasonable to conclude there are little or no economic costs … associated with strengthening the Disclosure Standard.*

105. For the reasons discussed above, we do not believe this conclusion can be drawn even if they are found to be good substitutes. Nevertheless, in the following sections we discuss the evidence presented by the ACMA.

106. Before considering that evidence, we note that the ACMA also briefly[33] analyses the potential costs associated with tightening the Advertising Standard. However, the extent of that analysis is to conclude that it 'too hard', using industry-wide data, to distinguish whether the introduction of the existing Advertising Standard in 2001 caused a substitution of advertising revenues from radio to other media.

107. As a result it is left unclear as whether these forms of advertising are 'good substitutes' and hence whether the ACMA consider there to be large or small economic costs associated with regulation of advertising.

108. Beyond the analysis of industry wide revenue figures it would have been helpful for the ACMA to analyse the economic costs that would be expected even if these forms of advertising were substituted following the introduction of the Advertising Standard. This would include an analysis of i) the differential cost of producing ads on different media; ii) the relative effectiveness of the same advertising spend on different media; and iii) the impact on the quality of radio of a loss of revenues.

*2.4.2.1. Anecdotal evidence*

109. The ACMA presents testimony from a number of previous inquiries. It concludes based on this material that:

> *The testimony of the commercial radio industry … implies that any reduction in revenue from commercial agreement is likely to be mitigated through substitution to paid advertising on commercial radio. Advertisers may also switch some proportion of their commercial agreement dollars to*

[32] ACMA, Review of expected economic costs, page 12.

[33] In one or two pages.

*another advertising medium, such as television, the internet or in-store advertising.*

110. In our opinion the testimony presented by the ACMA suggests that standard advertising are unlikely to be a good substitute for many of the commercial agreements which were the motivation for the previous inquiries (and the existing Disclosure Standard). As indicated in the testimony of Mr Michael Edmonds (of RTF) the commercial agreements with presenters:

*'weren't … about advertising [they were] about newsworthy issues'*

111. That is, the agreements were to illicit favourable comment (or avoid unfavourable comment) in news and current affairs broadcasts. This may have been to influence policy outcomes or to minimise damage to brands due to newsworthy events. We understand that they were not commercial agreements entered into with the purpose of the presenter directly endorsing products. Whilst it may be that companies could in the alternative to having these commercial agreements buy airtime (or full page ads in the newspaper[34]) to explain their opinion on the news or to rebuild their brands following adverse events, standard advertising (ie, product advertising) will not achieve the same outcome.

112. By this observation we do not therefore conclude that there were not net benefits to introducing the Disclosure Standard in 2001. The purpose of this observation is to recognise that there may have been costs to society from the 2001 Disclosure Standard (perhaps outweighed by the benefits) and distinguish between commercial agreements and agreements relating to product endorsements, the latter of which may be more substitutable with standard advertisements (though not without associated economic costs as discussed in this report).

*2.4.2.2. Empirical evidence*

113. As part of that review, the ACMA conducted an econometric analysis of advertising revenues for a sample of 25 radio stations over the period from 1995/96 to 2004/05. The ACMA's finding from this study as that the introduction of the 2001 Standards was associated with an increase in annual advertising revenues of $1,365,767 for stations with commercial agreements. This result was significant at the 7% level.

[34] As described in the testimony of Bernard Carney of GIO.

114. The results of this study are used in support of the ACMA's conclusion that revenues lost from commercial agreements due to increasing regulation are not costs to society, since it claims that increased revenues from advertising will offset these.

115. We consider that there are number of limitations and potential issues with the ACMA's regression analysis that it is important to highlight. These include:

- that the ACMA's study does not, and is not able to, support its conclusion that declining revenue from commercial agreements due to changes regulation will be offset by greater revenue from advertising to the point that such changes can be thought of as causing economic transfers, rather than costs to society;
- the design of the ACMA's regression appears likely to result in a spurious estimate for the increase in advertising revenues following the 2001 Standards because of interactions with the fixed time effects variables. These issues can be indirectly observed by the improbably large coefficient that the ACMA estimates; and
- the ACMA has conducted its study using data up to and including 2005/06 only, and not using the last three years of data that would have been available to it.

116. Our comments on the ACMA's study are necessarily based on reading the ACMA review and Appendix 1 in particular. We have not been able to collect sufficient data from CRA members to be able to replicate, or even approximate, the ACMA's analysis.

# 3. Economic impact of amending the Advertising Standard

117. In analysing the economic impact of the proposed amendments to the advertising standard, we have distil the ACMA's regulatory proposals down into two counterfactual scenarios:

- prohibiting integrated advertising and live reads; and
- making live reads more costly and hence less attractive (by explicitly requiring advertising to be distinguishable at the time or start of advertising, and/or have the tone and style of an advertisement).

118. The factual scenario for each is to maintain the status quo.

## 3.1. Incremental benefits of amending the Advertising Standard

119. The potential source of benefit from the proposed amendments to the Advertising Standard over the existing standard is that consumers' consumption patterns will become more efficient as a result of their choices not being influenced by a radio presenter's endorsement or positive discussion of a product that was not clearly paid advertising.

120. To the extent that such benefits exist, their accrual needs to be assessed as the difference in benefits between the factual and the counterfactual. The accrual of benefits can therefore be estimated as:

> *The gain in consumer surplus from consumers purchasing different products in response to spot schedule advertisements (or live reads and integrated advertisements with more prescribed disclosure) then they would have purchased in response to advertising allowed under the existing Advertising Standard.*

121. Any such gain in consumer surplus is inherently difficult to quantify, as it requires an estimate of the number of consumers who would purchase different products and an estimate of the difference in consumer surplus derived from that decision. Moreover, it is perfectly possible that the gain will be negative in that consumer consumption patterns will be adversely affected by a shift from integrated advertising to spot schedule advertising.

122. Unfortunately, neither the ACMA nor we have data to quantify this effect. This is problematic given that it is the key benefit identified with the ACMA's proposed amendments to the Advertising Standard. In principle, we would expect this gain to be either zero or negative. We hold this view because:

i. Advertising is, on average, welfare enhancing to consumers and producers. Advertising plays an important role in information dissemination and as a signal of product quality to customers. Integrated advertising is, in many circumstances, more effective in this role than is 'spot schedule' advertising and this is reflected in the premium price paid for this form of advertising.

ii. There are existing requirements on advertising on radio, including those in the Advertising Standard, and also the general trade practices law relating to misleading and deceptive conduct.

iii. If the choice between products is such that it will be tipped in one direction or another by the endorsement of radio personalities then the intrinsic difference in consumer surplus from the alternative products is likely to be small.

iv. Those consumption decisions that are influenced by the endorsements of radio personalities may be similarly influenced by endorsements by the same or other personalities in spot schedules or live read and integrated advertisements with more prescriptive disclosure rules.

v. Radio personalities with current affairs programming are heavily invested in their own reputation and have potentially very long lived careers. As a result, they have strong incentives to preserve their reputation by endorsing only reputable products. By contrast, sporting and other celebrities with less invested in reputation and more limited career time horizons likely have a reduced incentive.

123. In relation to point (i) above, we note that firms that have newly entered a market or who are introducing a newly improved product offering may be more disposed to use integrated advertising. This is a particularly useful strategy for such a firm precisely because their brand recognition and or knowledge of their new product might be low and they wish to leverage off the radio personality's recognition. Firms will only be prepared to pay the associated premium for integrated advertising if they believe that the product they are selling is of sufficiently high quality to be successful.

124. This logic might apply to a local butcher in a regional centre who is running a one-day only promotion, a large car manufacturer launching the latest model of one of its cars or a telecommunication company with a newly designed service price/quality package. The key point is that firms who believe that they have a

product that consumers are likely to desire are more likely to pay premium prices for premium advertising than other firms. If these firms are denied the opportunity of premium advertising by regulation this may be detrimental for consumers and for those firm's incentives to develop new services in the first place.

125. As discussed above, we would caution against using surveys of community attitudes to radio advertising disclosure as a substitute for a proper assessment of the benefits of more prescriptive regulation of advertising.

126. In relation to point (ii), the loss of benefits resulting from the proposed amendments needs to be assessed as the difference in benefits from the factual, in which live reads and integrated advertisement are allowed, and the counterfactual in which they are banned or made more costly. The loss in benefits can therefore be estimated as:

- the reduction in producer and consumer surplus from less effective forms of advertising (or a loss in surplus from some products no longer being advertised at all); and
- the reduction of enjoyment for radio listeners from the substitution of live reads and integrated advertisements for spot schedule advertisements.

127. In relation to point (iii) we note that for products which are differentiated by branding, a large proportion of the utility gained by consumption is wrapped up in the 'status' of the product. In such cases, a large proportion of the perceived difference in the product may be illusory and may even be tied to the 'status' of the individual or group endorsing the product.

128. In relation to the fourth dot point (iv), we note that it may be true that if integrated advertising is not perceived as an endorsement but as objective information then similar information presented in a spot schedule may not be as persuasive. To the extent that spot schedules can't similarly contain 'objective information' (which may depend on the skill of the advertising agency) then this represents the best case for modest regulation of advertising content.

129. Finally, in relation to the fifth dot point (v) we simply make the point that rather than endorsements by radio presenters being presumed to lead to worse consumer consumption decisions the opposite may likely be true.

### 3.1.1. Loss in surplus because advertising is less effective

130. Live reads are arguably more effective than spot advertisements, and thus more desirable to both advertisers and commercial radio broadcasters (evidence of this is discussed in the following section). Our analysis shows that the per minute revenue derived by commercial radio for live reads is around 4 times higher than that derived from spot advertisements[35].

131. Implicitly this means that, if live reads were banned, the lost revenue would have to be derived elsewhere, such as from spot advertisements. As many more spot advertisements than live reads are required to derive the same total revenue, the total amount of advertising on commercial radio would need to increase (assuming there was no leakage of revenue to other media).

132. In order to estimate the impact on welfare of banning (or reducing the number of) integrated advertisements we have constructed a stylised model of the market for advertising on radio.

133. Consistent with the economics literature we have thought about the market for advertising on radio as a two-sided market in which advertisers on one side of the market gaining surplus from buying air-time on radio at a prices less than their willingness to pay, and listeners on the other side of the market must 'pay' the nuisance cost of advertising in order to receive the radio content. We assume that licensees operate in a competitive environment such that any surplus they gain on one side of the market is competed away in the other side of the market.

134. We estimate the surplus to advertisers from their current mix of live reads (including integrated advertising) and spot scheduled advertisements. We assume separate demand and supply curves for live reads and spot schedules advertisements with the demand for live reads reflecting their greater effectiveness (discussed below) and the supply curve reflecting the greater potential for live reads to impact on listenership when they are high in number.

135. We then estimate the impact on the surplus earned by advertisers if they can no longer purchase live reads and must purchase spot schedule advertisements. In our model we require the station continues to earn zero profits, that is, they must

[35] Our analysis, based on results derived through the CEG survey, shows that the average premium for live reads, live crosses and integrated advertisements amounts to 4.1 times over spot scheduled advertisements

sell an additional volume of spot schedule advertisements to keep profits constant.

136. See appendix A for a further discussion of the approach.

137. In summary we find that live reads are important in a number of ways, since they:

- are an important source of surplus for advertisers in their own right; and
- support radio stations by allowing lower prices for spot schedule advertisements due to the high margins stations can earn from this form of advertising (on average three times greater than spot schedule rates);

138. Banning live reads is likely to affect the market for advertising in two separable stages. Firstly, many advertisers who previously sought live reads may seek spot schedule advertising instead. This represents an increase in demand for this service, leading to an increase in price and quantity consumed. Depending upon the perceived substitutive value of this and other options for advertisers, some surplus may be lost in this transition.

139. A further effect is that, due to the removal of the margins earned on live reads, prices for spot schedule advertisements will need to increase in order for station profitability to remain at the same level. This may entail further price increases, over and above those caused by the increase in demand, leading to some industry consolidation and a decrease in supply.

140. The overall effect is such that prices for spot schedule advertising are likely to increase significantly if live reads are banned. The overall volume of spot schedule advertisements may either increase or decrease, depending upon the relative magnitude of substitution from live reads to spot schedule advertising and any subsequent industry consolidation.

141. We have populated a stylised model of this market based on price and quantity inputs sourced from our survey of CRA members. We have conservatively assumed that the production costs of spot schedule ads to be the same as live reads, on a per minute of airtime played basis. We find that when live reads are banned, consumer surplus for advertisers falls across the industry from $476.7 million per year to $393.0 million per year, a fall of 18%. This is despite live reads constituting just 4% of current radio advertising time.

**Two-sided market for advertising on radio**

In the economic literature, broadcasting markets are commonly analysed as having two-sides with the content provider (the commercial radio licensees in this case) acting as an intermediary between advertisers (as agents for sellers of goods and services) and listeners who consume goods and services.[36]

Advertising allows commercial radio licensees to profitably provide content which is valued by listeners. However, in order to be profitable (make a normal return on investment), licensees sell air-time to advertisers who wish to connect to listeners who may potentially consume their goods and services.

Commercial radio licensees compete for a listening audience with other commercial and non-commercial radio licensees as well as with television, print, on-line and other forms of media.[37] They compete by broadcasting content which is of interest to listeners at the same time as broadcasting advertising which, beyond its information and entertainment content, will be a nuisance to listeners. The reaction of listeners to advertising may be to divert their attention or to switch to other radio or media providers.[38]

Commercial radio licensees balance the amount (and mix) of advertising and content in a way which maximises their profits. That is, they trade off the incremental revenue they receive from different forms of advertising with the costs incurred in broadcasting that content. In this two-sided market the costs incurred in broadcasting advertising includes the 'cost' associated with customers being annoyed by the advertising and switching over to competing media - resulting in a loss of listenership and hence revenue from advertising.

[36] See for example, Rochet, J.-C. and Tirole, J. (2006), Two-sided markets: a progress report. The RAND Journal of Economics, 37: 645–667.

[37] The increasing array of media offerings and the highly differentiated content on radio suggests that competition for the listening audience is vigorous.

[38] There may also be technological responses. In television, digital recording devices can be used to avoid advertisements. Similar technologies may be developed for digital radio.

We observe that live reads and spot schedules have different cost characteristics. In particular, live reads and integrated advertising have very low costs when they are few in number, this is because they do not significantly disrupt the flow of content. However, when they are large in number they would significantly disrupt the programming content and will likely lead to a great number listeners switching off. In contrast, spot schedules have a more uniform cost as they increase in number an incrementally increasing length of break between content.

#### *3.1.1.1. Integrated advertising more effective*

142. Integrated advertising is a particularly effective form of advertising, and therefore more attractive to advertisers than spot scheduled advertising. It is more effective because integrated advertising enables the advertiser to maximize the connection with potential customers by getting inside the editorial of the broadcast. Integrated advertising is particularly popular with radio advertisers, because of the intimate nature of the medium and the 'friendly' relationship that a listener will build up with a station and its presenters over time.

143. A study conducted in 2009 the United Kingdom by Absolute Radio researched how listeners respond to sponsorship and promotional activity such as live reads when compared to hearing no commercial activity at all or solely hearing spot airtime. The study found that much greater benefits are associated with sponsorship and promotions such as a live read compared to spot airtime, and strong levels of awareness and recall can be achieved with live reads. The study further found that sponsorships and promotions can achieve very high emotional connection with listeners[39].

### 3.1.2. Loss in surplus because listening pleasure is reduced by more spot ads

144. If tighter regulation of integrated advertising leads to a greater number of spots ads, consumers will be harmed by a reduction in listening pleasure. The impact on welfare from the 'nuisance cost' of advertising is well recognised in the economic literature.[40]

[39] Absolute Radio, Amplify Research - Proving the value of sponsorship and promotions
http://www.absoluteradio.co.uk/about/sales/research/amplify_summary.pdf

[40] Anderson, S and Coate, S. (2005) "Market Provision of Broadcasting: A Welfare Analysis", Review of Economic Studies 72, pages. 947–972.

145. Although reliable data on monetary value listeners place on an advertisement free commercial radio experience is very scarce, there is some information available which we can use for illustrative purposes. An American study by Edison Media Research has shown that, on average, Americans would be willing to pay $US8.83 ($6.75 in 1999 prices) a month in exchange for advertising free stations[41]. This is equivalent to about $AU2.41[42] per week, and relatively closely aligned with the cost of for example subscriptions to advertising free online music content[43].

146. Our analysis has shown that radio stations broadcast, on average, 10 minutes of advertising in the hour, which amounts to about 1680 minutes of advertising to week, or 16.67 percent of the weekly broadcasting time. This means that, if the average Australian listens to 1680 minutes radio per week, they are likely to hear approximately 160 minutes of advertising. This is a conservative estimate as it assumes that advertisements are spread evenly across the day. More likely there are more advertisements during the times when most Australians listen to the radio, such as breakfast morning and afternoon drive peak times - however it is also possible that listeners switch between stations during advertisements. If the average person is willing to pay $AU2.41 per week to get rid of approximately 160 minutes of advertisements, this implies that the cost to that person of each minute of advertisement is around $0.015.

147. Given this estimate of the cost per minute of advertising to a listener, it is possible to estimate the cost to all commercial radio listeners of banning live reads.

148. Our analysis shows that commercial radio broadcasts, on average, 67.6 minutes of live reads per week. If we assume that live reads derive four times as much revenue as spot reads, this means that there will be 203 additional minutes of advertisements broadcast each week ((67.6 * 4) – 67.6), to make up the same revenue.

149. This means that the average person that listens to 960 minutes of commercial radio a week, is likely to hear about 19.3 additional minutes of advertising per

41 "Will Your Audience Be Right Back After These Messages?" The Edison Media Research/Arbitron Spot Load Study June 1999

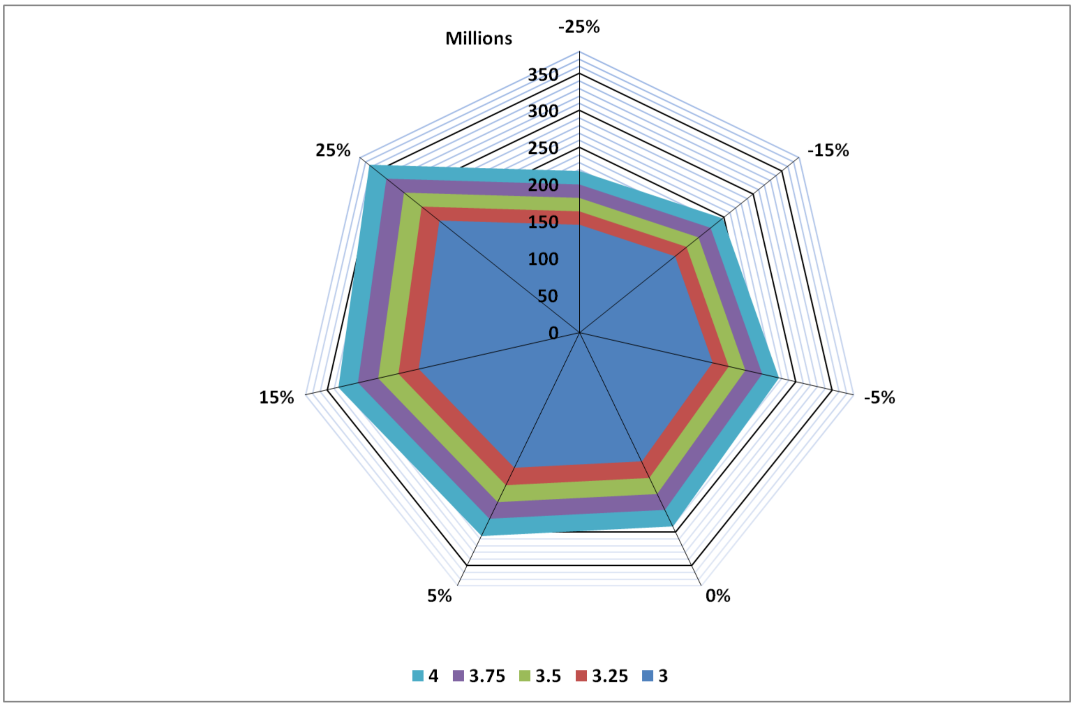
42 Exchange rate based on 2010 average from OANDA.com

43 Spotify.com is a service that provides access to a significant amount of music content online. The service is free but includes advertisements. At a cost of £4.99 per month is it possible to upgrade the service to make it advertisement free. This subscription cost equates to $AU2.10 per week (average 2010 exchange rate from ONANDA.com). http://www.spotify.com/uk/about/what/

week (as opposed to other content). At a cost to each consumer of $0.015 per minute, this amounts to a total cost to all Australian commercial radio listeners of $5.6 million per week, or $291.0 million per year. Our general impression of this estimate is that it appears high and may be a reflection of the limited data on nuisance costs of advertising. However, even if this estimate is reduced in orders of magnitude it remains significant.

150. This estimate cost is sensitive to the assumptions and inputs. The below chart illustrates how the total cost to Australian commercial radio listeners change with the relative revenue derived from live reads and spot advertisements respectively (from 3 to 4 times as much for live reads), and the cost to the consumer of an additional minute of advertisement (plus/minus 5, 10 and 25 percent of $AU0.015). The chart shows that although the results are sensitive to the inputs, they are still very high at $145.5 million with the most conservative inputs, ranging through to $363.8 million.

**Figure 2: Cost to consumers of banning live reads – sensitivity analysis**




*Source: CEG survey, Edison Media Research & CEG analysis*

## 3.2. Incremental costs of amending the Advertising Standard

### 3.2.1. Costs if ads shift to from live reads to scheduled spots

151. Tightening the regulation of integrated advertising will mean that advertising is redirected to other forms of advertising on the radio (i.e. spot scheduled advertising) If integrated advertising was considered to have greater effectiveness, lower production cost and greater flexibility that of spot scheduled advertising, spot scheduled advertising is not likely to be a perfect substitute for integrated advertising.

152. For example, we understand from discussion with station managers that pre-recorded advertisements are more expensive to produce than some integrated advertisements, in particular, live reads. This is because in addition to a creative strategy and copywriting costs, there are also costs associated with production of the advertisement. This could make radio less attractive for smaller advertisers with a limited budget, or advertisers that just want a once-off announcement or air-time spot.

153. This may be a particularly important issue for regional areas and other advertisers with a low willingness to pay. For these advertisers the cost of developing a spot ad may be prohibitive or be a material drain on their business with negative consequences for their customers.

### 3.2.2. Indirect costs if ads shift to less efficient media

154. If integrated advertising becomes less attractive, or unavailable as an option due to new regulations, this portion of revenue is likely to be redirected to other forms of advertising. If the other forms of advertising are perfect substitutes, then this would be a transfer of revenue between parties, and not an economic cost on society as a whole.

155. This could come at a significant cost to commercial radio, advertisers and listeners if radio advertising is proven to be more effective than television, print or internet advertising and also less costly.

156. Radio advertising appears to have a number of specific features not available to substitute media. It was described to us for example, that radio is ‘local’ and able to specifically target a geographic audience, it is flexible and immediate, and it is also intrusive in a way that other media substitutes are not during everyday activities such as working, driving or grocery shopping.

157. A study conducted by Millward Brown involving nearly 5500 interviews in continuous research tracked awareness and attitudes to 17 brands advertised on TV and/or commercial radio. The study found that radio in isolation was measured to be three-fifths as effective as TV at raising advertising awareness, and this result was achieved at one-seventh of the cost. The study also found that adding radio to TV ads has a 15 percent multiplier effect, that is, if 10 percent of a given TV budget is re-deployed onto radio, the efficiency of the campaign in building awareness increase on average by 15 percent.[44]

158. This research indicates that moving advertising away from radio into other media is not a close substitute.

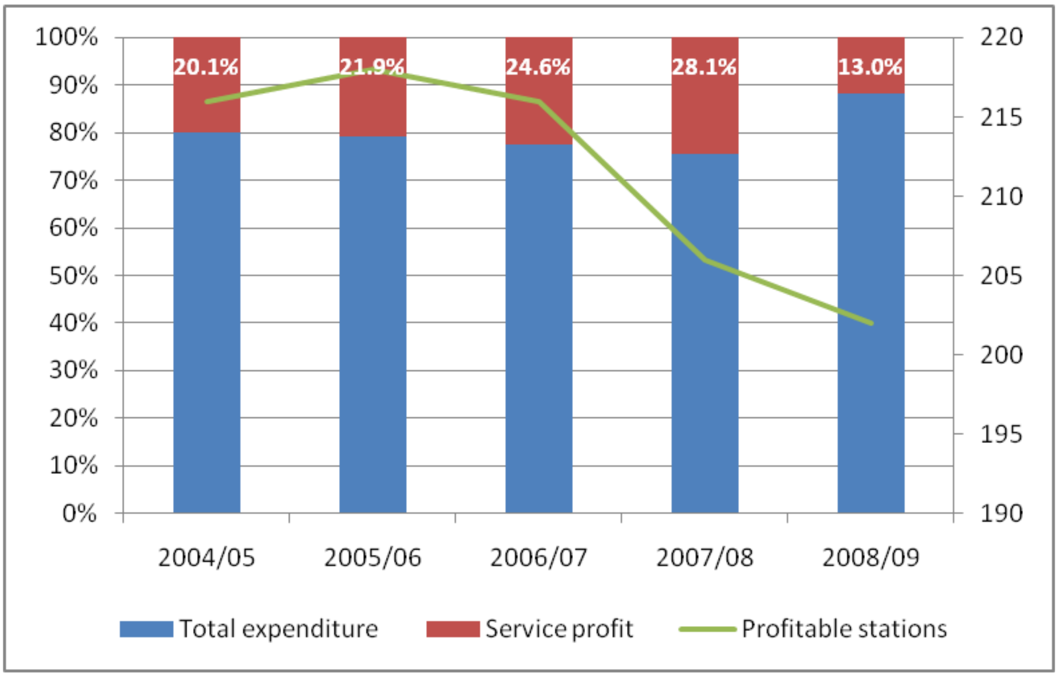
159. We also consider the indirect loss in surplus from lower quality radio broadcasting. This arises because changing the mix of advertising on radio will inevitably lead to a reduction in revenue to the radio industries. Whilst these revenues may be picked up by other media the intervention will reduce the surplus that listeners were receiving from radio. Whilst this would be partially offset by the increase in surplus to consumers of other media (which have higher advertising revenue) there would be a net loss to society. This is, by definition, because the existing preferences of consumers across radio and other media would be being distorted by differential regulation.

160. As we noted above in relation to our market modelling (see section3.1.1), a forced shift in advertising from live read or integrated advertising to spot schedules would be expected to lower overall revenues and cause some industry consolidation. This effect would be exacerbated if revenue shifted to other media. It is noteworthy that many stations are not profitable and many others are marginal.

[44] Radio Advertising Bureau, The Radio Multiplier Study – How Radio Drives Ad Awareness Four Times More Cost-Effectively Than TV.

http://www.rab.co.uk/rab2009/showContent.aspx?id=466

**Figure 3: Service profit as percentage of total service revenue, average of all stations, and total number of profitable stations (out of 261)**




### 3.2.3. Direct costs incurred by radio licensees as a result of tightening the Advertising Standard

161. The existing advertising standard requires that a ‘reasonable’ listener is able to distinguish advertising from other content. Commercial radio currently incurs costs such as salaries, employee on-costs, payments to external contractors etc to ensure compliance with this standard.

162. We have estimated the total cost of compliance with the advertising standard by way of the CEG survey. We collected data relating to the specific compliance costs for all stations in our sample, a total of 34 stations. This data has been scaled up to the industry level, which consists of 261 commercial radio stations. Table 2 shows that the compliance cost for the stations in our sample, on average, are $23,435 per annum. This implies an industry-wide cost estimate of around $6.1 million.

**Table 2: Compliance costs for existing advertising standard**

| | Industry total | Sample average |
|---|---|---|
| Salaries and wages | $4,634,985 | $17,759 |
| Employee on-costs | $880,217 | $3,372 |
| Payments to external contractors | $81,159 | $311 |
| Fees for legal services | $519,800 | $1,992 |
| Other | $435 | $2 |
| **Total costs** | **$6,116,597** | **$23,435** |

*Source: CEG survey & analysis*

163. The ACMA has proposed amending the current advertising standard in two general ways. The first amendment involves banning integrated advertisements and live reads. The second involves making the regulations around integrated advertisements and live reads more stringent, for example by requiring that such advertisements have the 'tone and style' of an advertisement.

164. It is difficult to quantify the exact incremental compliance costs which would be associated with either of these amendments. Nevertheless, it is likely that both amendments would cause an increase on the costs to commercial radio of complying with the advertising standard.

165. Banning integrated advertisements and live reads would result in a large portion of advertising agreements having to be renegotiated. We collected data on the number of advertising agreements which include integrated advertisements. On average, the stations in our sample had 304 advertising agreements including one of integrated advertising, live reads or live crosses. The distribution is illustrated in Table 3, where the bottom third consists of zero and 77 agreements including an integrated element, the middle third between 77 and 200, and the top third between 200 and 1760.

**Table 3: Distribution of advertisement agreements containing an integrated element**

| Percentile | 1/3 | 2/3 | 3/3 |
|---|---|---|---|
| Number of agreements | 0 - 77 | 77 - 200 | 200 - 1760 |

*Source: CEG survey & analysis*

166. This suggests that a relatively large number of advertising agreements would need to be renegotiated as a result of the proposed amendment. We have also been told by station managers that it is common practice to sell advertising as a package of several forms of advertising, including advertising with integrated elements, suggesting that entire sales practices and systems may need to be restructured.

167. The cost of renegotiating contracts containing integrated advertising is likely a function of the cost for advertising employees. We collected data on the number of advertising sales employees at each station, as well as their total salaries and on-costs.

168. Table 4 shows that the stations in the sample, on average, have 10 advertising sales employees with a combined salary and on-cost expense of $1.3 million per year. This implies that on the industry level, the cost estimate of all advertising sales employees is over $336 million. Increasing these costs by even 1 percent, would impose an incremental cost of almost $3.3 million on the commercial radio industry. Likely the percentage increase would be much greater, given the number of advertising agreements that contain integrated elements.

**Table 4: Cost of advertising employees**

| | Industry total | Sample average |
|---|---|---|
| Advertising sales employees | 2,667 | 10.22 |
| Salaries & on-costs for advertising employees | $335,982,532 | $1,287,289 |

*Source: CEG survey & analysis*

169. It also has to be taken into consideration that, if integrated advertisements are banned, then some portion of the current compliance costs, as estimated in Table 2, are no longer going to be incurred.

170. If the advertisement standard is made more stringent, requiring advertisements to have the 'style and tone' of an advertisement, additional costs are also likely to be incurred. This is because it would be necessary for the stations to train their staff on the new requirements of the standard and also to increase their monitoring of advertisements as they are broadcast in real time.

171. To estimate training costs to comply with more stringent regulation we have collected data on employee salaries from the most recent B17 forms and also total employee numbers. If for example stations need to undertake an additional

two days of training for 75 percent of their staff to ensure compliance with more stringent rules, this would cost sampled stations, on average, $18,524 per year, implying an annual cost estimate of $4.8 million for the industry as a whole.

172. Monitoring costs are more difficult to quantify. These costs are likely to be a function of the current compliance costs which we estimate at $6.1 million. The costs of increased monitoring are discussed in more detail in section 4.3.

# 4. Economic impact of amending the Disclosure Standard

173. In analysing the economic impact of the proposed amendments to the current affairs disclosure standard, we have distilled them into three counterfactual scenarios:

- applying to any other agreements where the person concerned has significant influence on the content of the material broadcast;
- expanding the application of the disclosure standard to apply to infotainment programming in addition to current affairs programming; and
- Introducing a requirement for regular broadcasting of pre-recorded announcements making relevant disclosure requirements.

174. The factual scenario for each is maintaining status quo.

## 4.1. Incremental benefits of amending the Disclosure Standard

175. A potential benefit of the Disclosure Standard is that there is a lesser likelihood that listeners' understanding of current affairs issues and public policy debates is coloured by undisclosed commercial agreements. The fact that there is scope for these kinds of commercial agreements on current affairs programs provides a basis for some restrictions relating to current affairs programmes.

176. We would however draw a distinction between agreements for product endorsements and agreements involving radio personalities in public policy discussions. For the reasons already discussed, integrated advertising in the nature of product endorsement is likely to be welfare enhancing and merits, at most, modest disclosure requirements. A product endorsement can be defined as relating solely to the quality and/price characteristics of a particular product or product line.

177. It is less obvious that there is likely to be welfare benefits from other forms of commercial agreements that are broader in nature – such as an agreement to promote a particular industry or the attributes of a company (eg, statements to the effect that Company X is a good employer/corporate citizen etc). For these forms of commercial arrangements the current disclosure requirements may be appropriate.

178. Drawing a distinction between product endorsements and commercial agreements with public policy implications also has the following benefits.

179. First, it allows the ACMA to refine its thinking in relation to whether the Disclosure Standard should apply to infotainment or other factual programming. Once it is recognised that the ACMA need not be concerned with agreements relating to product endorsement, it follows that it should not apply the Disclosure Standard to other programming. This follows because agreements relating to that programming are unlikely to have scope beyond product endorsement and would be captured by the Advertising Standard.

180. Second, it would mean that the Disclosure Standard could be made workable. As it is presented in the ACAM's Options Paper it is unworkable because of licensees' wide ranging relationships and agreements with sponsors, advertisers, suppliers, contractors and others would be captured. For example, imagine the disclosure that would be required if commenting on a labour strike at any one of the multitudes of advertisers. However, if only arrangements that went beyond product endorsement were captured then this would substantially reduce the impact on current affairs programming.

181. The above discussion should not be taken to suggest that we consider that there is a clear case for disclosure regulation of non-product endorsement commentary - only that the case for this is stronger than for product endorsement.

182. The case for disclosure regulation of non-product endorsements is inherently difficult to quantify and will depend on the extent to which:

- radio presenters are willing to alter their stated views in order to attract integrated advertising revenues; and
- this is any different to their willingness to alter their stated views in order to attract spot schedule advertising;

183. Radio broadcasters have an influence on the community's knowledge of current affairs issues and the influence of that on public policy outcomes. On some matters this may be significant, whilst on others it may be small.

## 4.2. Incremental costs of amending the Disclosure Standard

### 4.2.1. Costs of complying with the existing Disclosure Standard

184. Currently, commercial radio stations that broadcast locally produced current affairs programs incur costs of complying with the existing Disclosure Standard relating to salaries and on-costs for employees, payments to external contractors, fees for legal services etc.

185. We estimate the total cost of compliance with the disclosure standard by way of a survey. We collected data relating to the specific compliance costs incurred by those stations in our sample that broadcast locally produced current affairs, a total of 12 stations. This has been scaled this up to industry level by assuming that 55.5 stations broadcast locally produced current affairs programs in total.

186. Table 5 below indicates that the stations in our sample broadcast on average 3,043 minutes a week of locally produced current affairs programs, which is approximately 30 percent of the total available broadcasting time. On average, the stations have five current affairs presenters and incur annual compliance costs of $46,204. This implies a total industry-wide compliance cost estimate of just below $2.4 million.

**Table 5: Compliance costs for existing disclosure standard**

| | Industry total | Sample average |
|---|---|---|
| Minutes of local current affairs programs | 168,724 | 3,043 |
| Number of current affairs presenters | 291 | 5.25 |
| Salaries and wages | $1,211,078 | $21,841 |
| Employee on-costs | $195,622 | $3,528 |
| Payments to external contractors | $23,611 | $426 |
| Fees for legal services | $377,372 | $6,806 |
| Other | $585,311 | $10,556 |
| **Total costs** | **$2,392,995** | **$46,204** |

*Source: CEG survey & analysis*

187. With more stringent regulation on disclosure of commercial agreements, these costs will increase.

### 4.2.2. Costs of extending the Disclosure Standard to persons other than current affairs presenters

188. The ACMA has proposed expanding the application of the current affairs standard to other persons which could potentially influence content of current affairs programs, for example producers and managers. This would mean that a significantly larger number of persons become subject to the standard.

189. To estimate the cost of expanding the application to more persons with potential influence over current affairs content, we collected data on the number of persons involved in the production of current affairs programs, including producers, managers and other staff.

190. We have scaled up the current compliance costs by the number of additional persons which would become subject to the standard given the proposed amendment, assuming that 30 and 50 percent respectively of these costs are fixed (i.e. will not change with the number of people). We have assumed that stations which indicated that they do not allow employees other than presenters to enter into commercial agreements incur an incremental cost of zero.

**Table 6: Incremental cost of expanding disclosure standard to other persons with potential influence over current affairs programs**

| | Industry total | Sample average |
|---|---|---|
| Current affairs producers, managers & other staff | 444 | 8 |
| Incremental compliance costs assuming 30% of total costs are fixed | $3,549,827 | $64,018 |
| Incremental compliance costs assuming 50% of total costs are fixed | $2,535,591 | $45,727 |

*Source: CEG survey & analysis*

191. Table 6 indicates that in our sample, on average, each station had an additional 8 employees involved in the production of current affairs programming. Expanding the application of the disclosure standard to include these persons would result in an incremental cost of between around $46,000 – $64,000 per station per year. This implies an industry-wide incremental cost estimate of between $2.6 and 3.6 million. This is in addition to the current compliance costs of $2.4 million.

### 4.2.3. Costs of extending the Disclosure Standard to infotainment programs

192. The ACMA has also proposed another variation to the disclosure standard – to expand the application of the disclosure standard to other types of programs, for example infotainment programs.

193. To estimate the cost to the industry of expanding the application of the disclosure standard to infotainment programs we collected data on the minutes of locally produced infotainment programs and the number of presenters. We used the ACMA's definition of an infotainment program[45], but allowed the stations to categorize their own programs as potentially part of this definition. In total there were 12 stations in our sample that broadcast locally produced infotainment programs.

194. For stations with no current affairs programs (i.e. stations that do not currently have systems or processes in place for the purpose of compliance with the disclosure standard), we estimated the compliance cost as the average cost of compliance per presenter from the current affairs standard ($2,392,995 / 291 see Table 5), multiplied by the number of infotainment presenters for that station. We assumed a cost of zero for stations that do not contractually allow presenters to enter into commercial agreements.

195. For stations with current affairs programs we estimated the incremental compliance costs as for the expansion to additional persons, i.e. by scaling up the costs by the additional number of presenters assuming that 30 and 50 percent respectively of the compliance costs are fixed.

[45] A program that sole or dominant purpose of which is to present factual information in an entertaining way, and which employs presenters to do so (ACMA Options Paper 2011 p. 22)

**Table 7: Incremental cost of expanding disclosure standard to infotainment programs**

| | Industry total | Sample average |
|---|---|---|
| Minutes of locally produced infotainment programs | 240,688 | 922 |
| Number of infotainment presenters | 645 | 2 |
| Cost for stations with no current affairs programs | $2,584,148 | $12,572 |
| Incremental cost for stations with current affairs programs assuming 30% of total costs are fixed | $190,567 | $3,437 |
| Incremental cost for stations with current affairs programs assuming 50% of total costs are fixed | $136,119 | $2,455 |

*Source: CEG survey & analysis*

196. Table 7 shows that in the sample, on average, 922 minutes of locally produced infotainment programs are broadcast. The stations have on average 2 infotainment presenters.

197. The average cost of expanding the standard to infotainment programming for stations that do not have current affairs programs, and are thus not current subject to the disclosure standard, is $12,572 for sampled stations, and $2.6 million for the industry. The average incremental cost for stations already subject to the disclosure standard ranges from $136,000 to $191,000. This, again, is in addition to current costs and potentially in addition to costs of expanding to other persons which count influence current affairs content.

### 4.2.4. Costs of extending the Disclosure Standard to require regular disclosure of commercial agreements

198. The ACMA has raised the prospect of another possible variation to the Disclosure Standard – a requirement for regular (possibly hourly) pre-recorded announcements of relevant commercial agreements in lieu of alternative requirements for presenters to read these disclosures.

199. This proposal would potentially avoid some of the compliance costs associated with staff and training, since only those individuals responsible for producing the regular announcements would need to be fully aware of the relevant commercial

agreements and the station's obligations. However, we expect that some of these costs would not be avoided.

200. We consider that these announcements are likely to be perceived by listeners as akin to advertisements. That is, as information that is not associated with the primary purpose for the consumer in choosing to listen to radio. As such, it is likely that radio stations must broadcast the statements during time that would otherwise be used for advertising. If stations allow the statements to replace content, then this may lead to consumers switching to other stations or media.

201. If pre-recorded disclosure statements were to completely replace time used for paid advertising, then this would result in a direct loss for radio stations of approximately $22.0 million per year, based on 15 seconds of pre-recorded statements applied across all stations.

## 4.3. Monitoring disclosure and integrated advertising

202. The ACMA has proposed strengthening both the existing current affairs and advertising standards, requiring both more disclosure of commercial agreements and more distinguishable advertising.

203. One consequence of these proposed amendments is that commercial radio could be required to monitor more closely all broadcast content to ensure compliance. This would be a significant burden on the industry given the large number of agreements and the wide range of content covered in current affairs (and infotainment) programming.

204. We have estimated the incremental compliance cost by estimating the cost of adding one additional employee for monitoring, as well as a fixed legal fee and external contractors fee to prepare the station for the strengthened regulation. We have applied these incremental costs to all stations which have current affairs content, infotainment content and/or integrated advertisement.

205. Adding an additional employee for a station in our sample will, on average, result in an estimated incremental cost of $61,590. On the industry level, this implies an incremental cost estimate of $16 million. If we on top of that assume legal fees and external contractors' payments of $5,000 each per station per year, this adds another $2.6 m to the industry total incremental cost, just for monitoring compliance. This is illustrated in the below table.

**Table 8: Incremental costs of monitoring**

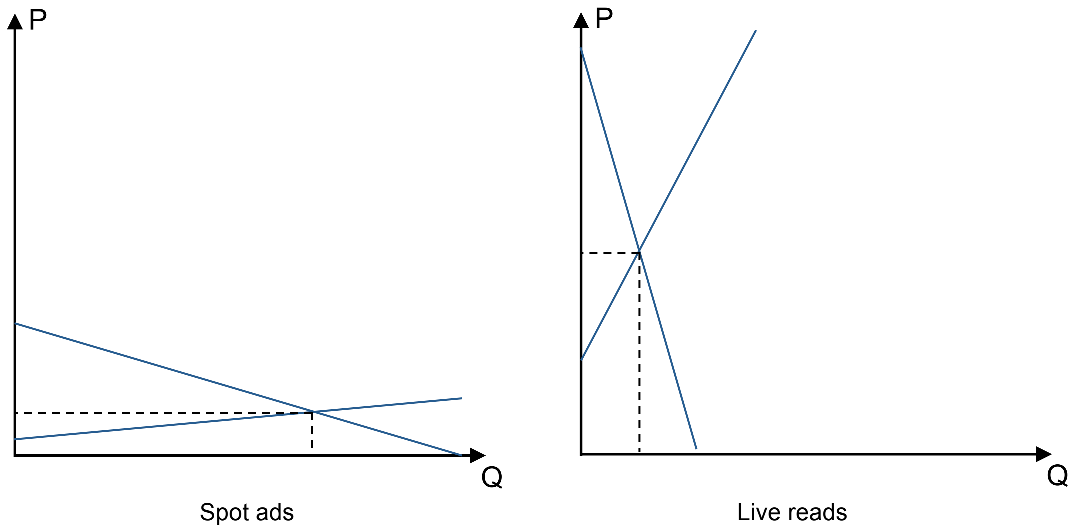
| | Industry total | Sample average |
|---|---|---|
| Cost of an additional employee | $16,074,872 | $61,589 |
| Legal fees | $1,305,000 | $5,000 |
| External contractors' payments | $1,305,000 | $5,000 |

*Source: CEG survey & analysis*

# Appendix A. Estimating surplus from advertisements

206. Prior to proposed regulation banning live reads, the market for live reads is characterised as having much higher prices than for spot ads, associated with less responsive demand and perceived higher value for these products.

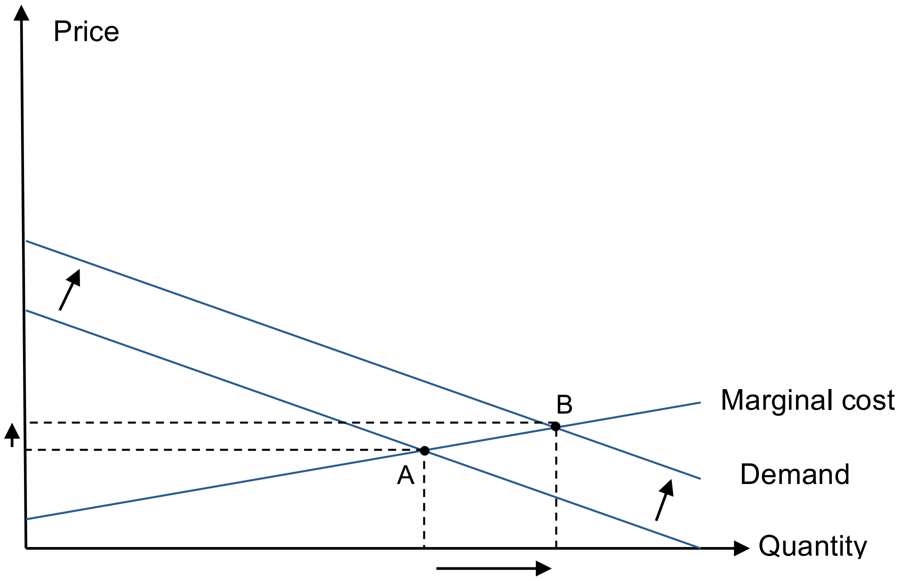
**Figure 4: Pre-regulation markets for spot ads and live reads**




207. If a ban is placed on live reads, then all things being equal this is will increase demand for spot ads, since the two are, to some extent, substitutes. Given the greater efficiency of live reads from the perspective of advertisers (reflected in its higher prices) the increase in demand for spot ads minutes may actually be higher than the minutes of live reads that are lost as a result of a ban.

208. The effect of this change is shown below in the move from A to B, resulting in increases in the price of advertising and the quantity consumed.

**Figure 5: Increase in demand for spot ads**




209. It is reasonable to assume that the radio advertising industry is competitive, since it is characterised by a large number of competitors and choices for advertisers. In competitive markets, economic profits are zero over the long run. That is, any profits reflect a reasonable return on capital.

210. This concept is important because profits made on live reads contribute toward maintaining the overall profitability of the radio industry. To the extent that greater margins are made on live reads, these cross-subsidise prices for spot ads. If live reads are banned, then a source of profitability is lost to the radio industry that must be recovered from general advertising products.

211. Although a ban on live reads may cause an increase in demand for spot ads, this does not mean that profitability for this product increases to the extent that it compensates for the lost profitability of live reads. Indeed, the opposite is likely since the value of live reads is much higher, per minute, than for scheduled spot ads.

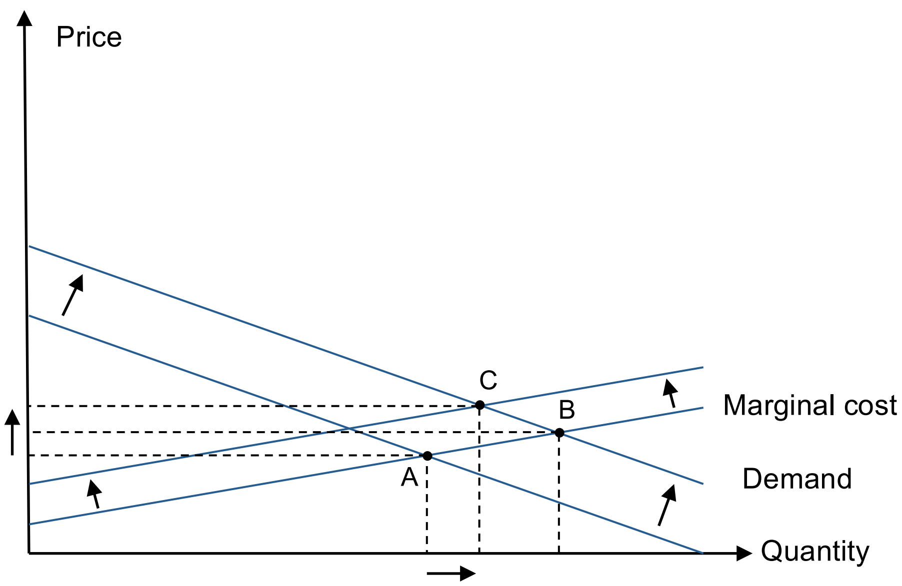
212. Consequently, for the industry in general to maintain profitability, some firms may exit over time in a process that reduces volumes and increases prices back to levels of profitability consistent with zero economic profit. This further effect is

shown in the diagram below as a movement from B to C. The overall increase in price from A to C has two components:

- the increase in demand for spot ads generated by the ban on live feeds; and
- the decrease in supply for spot ads caused by the removal of the cross-subsidy from live feeds.

213. The overall effect on the quantity of ads supplied is, in principle, ambiguous. In the chart below, the overall effect is a slight increase in quantity. In practice, the quantity of advertising minutes may be likely to increase with substitution of minutes from live reads, unless the industry consolidation is very large.

**Figure 6: Decrease in supply for spot ads**




214. In sum then, the banning of live reads will likely increase prices for spot ads, and may increase the number of spot advertising minutes overall. The effect on consumer surplus in the advertising market would be negative – some of the lost consumer surplus from the ban on live feeds could be made up in the spot advertising market in moving from point A to point B in the figure above. However, the contraction in supply from point B to point C ensures higher prices and lower overall consumer surplus relative to the base case.

# Appendix B. Critique of econometric analysis

215. The ACMA has included an econometric study in its review of the expected economic costs.[46]

## B.1 Results of the study do not support the ACMA's conclusions

216. The ACMA's econometric study is limited in its scope and in what it seeks to estimate. The study is not designed to estimate the degree of substitutability between advertising revenue and revenue from commercial agreements. Furthermore, it is unable to do so in any case since the ACMA states that it does not have data relating to revenue from commercial agreements.[47]

217. Taken at face value, without review of the underlying assumptions used to generate them, the ACMA's econometric results indicate that the introduction of the 2001 Standards was associated with an increase in annual advertising revenues of $1,365,767 for stations with commercial agreements. However, this result does not establish the extent to which advertising commercial agreements are substitutes from the perspective of radio stations. That is, it does not show how much lost revenue from commercial agreements is associated with its calculated average increase in advertising revenues.

218. If advertising and commercial agreements were 'perfect' substitutes from the perspective of customers, then we would expect any decrease in revenues from commercial agreements to be exactly offset by greater revenues from advertising. The ACMA's econometric study does not indicate, and is not able to indicate, whether this is the case. Nonetheless, the conclusions that the ACMA draws from the results of its study give a strong flavour of this:[48]

> *Analysis of the commencement of the Disclosure Standards in 2001 showed that there was a material increase in advertising revenue at affected commercial radio stations after the introduction of the standards in*

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46 ACMA, *Reform of the Commercial Radio Standards: A review of the expected economic costs*, March 2011, hereafter the 'ACMA Review'.

47 Review of expected economic costs, page. 12.

48 Review of expected economic costs, page. 20.

*2001. This supports the hypothesis that changes to the Disclosure Standard that result in a reduction (increase) in revenue earned by presenters from commercial agreements will be accompanied by an increase (decrease) in conventional advertising revenue earned by the licensees that employ those presenters. This impact is best characterised as an economic transfer between parties connected by an employer/employee relationship, rather than an economic cost to society.*

219. The existence of substitution possibilities for commercial agreements does not mean that there will be no economic cost to society of raising the cost of providing this service – or in the ACMA's words a transfer between parties. To make this claim requires a number of assumptions, including:

- that the nature of the substitution is perfect;
- that both services are provided with equal cost and efficiency, a caveat made by ACMA directly subsequent to the quote above; and
- there are no sunk costs that might inefficiently (from society's perspective) be stranded and effectively duplicated as a result of such actions.

220. Since ACMA's econometric analysis is unable identify the degree of substitutability between commercial agreements and advertising, it cannot simply assert that such substitution opportunities render the imposition of new restrictions on commercial agreements as an economic transfer.

## B.2 Design of the study may give rise to spurious estimates

221. The ACMA's regression analysis is conducted over the period 1995/96 to 2005/06 across 25 radio stations, 17 of which reported having commercial agreements and 8 of which did not.

222. The regression equation used by the ACMA was:

$$\begin{aligned} \textit{Advertising revenue}_{i,t} = {} & \textit{commercial agreements}_{it} \\ & + \textstyle\sum \textit{radio station-specific effects}_{it} \\ & + \textstyle\sum \textit{time-fixed effects}_{it} \\ & + \varepsilon_{it} \end{aligned}$$

Where:

- *Advertising revenue* $_{it}$ is the dependent variable
- i = individual radio station observations
- t = financial year observations
- *commercial agreements* indicator variable is set equal to one when standards were in place and the licensee has (or employs a presenter which has) at least one commercial agreement (treatment group), and zero for licensees without commercial agreements (control group).
- ∑*radio station-specific effects* $_i$ is an indicator variable for each of the radio stations and captures differences between radio stations e.g. + $\beta_1 2CC_{it}$ + $\beta_2 2DU_{it}$ … etc for each radio station.
- ∑*time-fixed effects* $_i$ is an indicator variable for each financial year and captures changes in revenue common to the industry e.g. + $\beta_{27} 1995/96_{it}$ + $\beta_{28} 1996/97_{it}$ … etc for each financial year.
- $\varepsilon_{it}$ is an error term that captures the effects of missing variables or random effects.

223. The ACMA does not state which was the first financial year in which it set the commercial agreements indicator variable to one to model the effect of the introduction of the 2001 Standards. We assume that this is likely to be the 2001/02 financial year.

224. The way in which the ACMA have set up its regression means that the commercial agreements variable will be strongly correlated with the existing time fixed-effects variables. This means that it is possible for the commercial agreements variable to appear significant even where it may not play any role in explaining advertising revenue. This may be associated with reduced significance for time fixed-effect

225. Although it is not possible for us to investigate within the ACMA's data why this is occurring, it is possible to replicate the same effect in a simple example. We generate panel data with 10 firms and 10 time periods, with each firm in each year having advertising revenue generated randomly and independently with a mean of $5 million and a spread of $1 million either side of the mean. We assume that commercial agreements on all these firms are regulated after year five.

226. Given the construction of the data, there is no reason to expect the coefficient on commercial agreements to be significant – we know that advertising revenues will not increase or decrease, on average, after year five. However, using the ACMA's functional form, we find that we do achieve a significant result for this coefficient, and that this is associated with reduced significance for the time fixed-effects variables from year six.

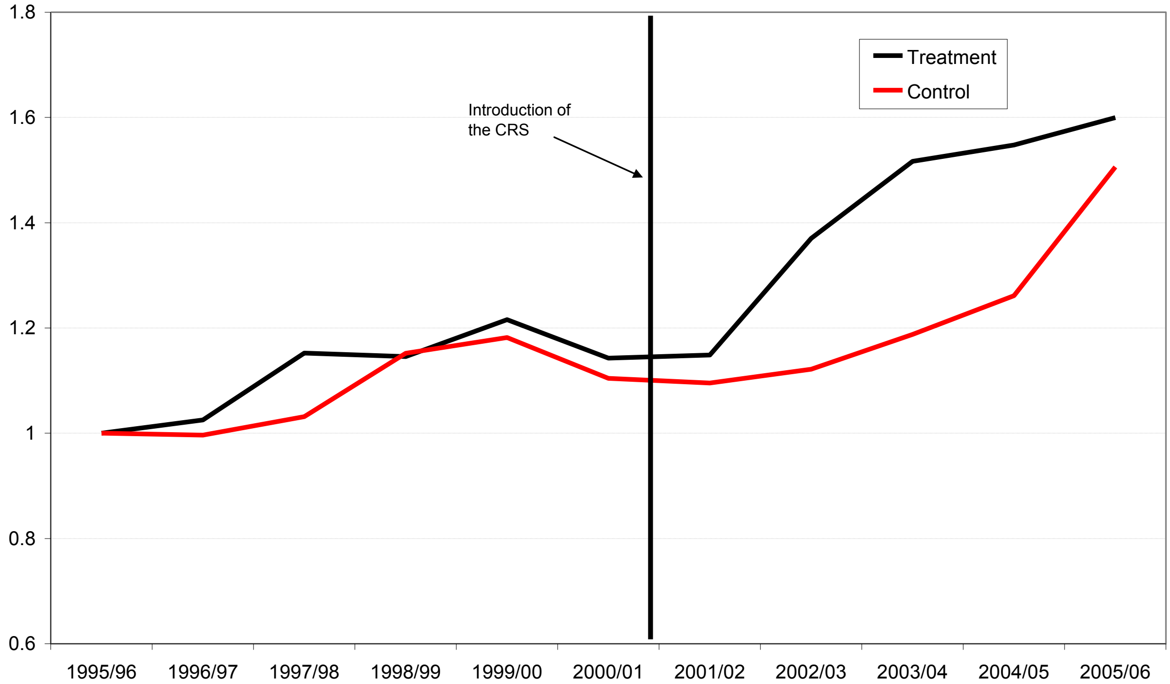
227. This result may also be consistent with the surprisingly high value that the ACMA estimates for its coefficient – as the ACMA itself states, its finding appears to suggest that 22% of current advertising spend is due to restrictions imposed by the 2001 Standards. We find this suggestion implausible.

## B.3 Time series is arbitrarily ended at 2005-06

228. The econometric analysis conducted by ACMA is based only on data sampled during the period from 1995/96 to 2005/06. We find it unusual and undesirable that ACMA would not utilise the full extent of the dataset of advertising revenues that it has available to it, particularly where it does not seek to explain the exclusion of the three most recent years.

229. ACMA's own chart, copied below,[49] shows that after the introduction of the 2001 Standards, this period had higher advertising revenue growth for stations with commercial agreements.

[49] Review of expected economic costs, page. 15




230. It is noticeable that the line associated with the control group, or those stations without commercial agreements, appears to be converging with the treatment group in 2005/06. To the extent that this convergence continued, or the control group actually passed the treatment group, after 2005/06, then this would have a potentially important effect on the value and significance of the coefficient attributed to the increased value of advertising revenues gained from reduced commercial agreement opportunities.

# Appendix C. Survey of CRA members

231. For the purpose of undertaking this empirical analysis we have surveyed a sample of commercial radio stations on a number of aspects regarding their employees, programming, advertising and costs.

232. There are 261 commercial radio stations in Australia. Given the time constraints and broad context of the ACMAs review, and thus the scope of our assessment, it was not possible to survey all commercial radio stations in Australia. Therefore, we opted for a sampling approach which would result in the most comprehensive data set given the time constraints.

233. The total sample surveyed consisted of 41 commercial radio stations. The first 25 stations were the ones used in the ACMA's review of expected economic costs[50]. These stations were selected to enable comparison with the ACMA's expected costs of amending the current affairs disclosure standard. The remainder of the sample was selected using simple random sampling.

234. The survey was put together in consultation with Commercial Radio Australia and several of their board members. It was sent to the station managers of each of the sample stations via e-mail, along with an explanatory note. This was followed by an e-mail and/or a phone call to the station managers two or three days after the survey was sent out. This was done to ensure that any queries about the questions were addressed, and that the surveys were returned in a timely manner. Additional information was also collected in these follow up discussions.

235. As many of the survey questions contain confidential information, CEG ensured complete confidentiality of all information provided to it, also in the form of a written agreement to the stations that required it.

236. The response rate was relatively high. Out of the 41 stations that received the questionnaire 34 responded, which is a response rate of 82.9 percent. Five of the non-responses belonged to a network which chose not to participate in this study.

[50] The 25 stations included in ACMA's review are 2CC, 2DU, 2GB, 2LM, 2MAC, 2UE, 3AW, 3BBO, 4BC, 4EL, 4WK, 5AA, 5DN, 5SE, 6KG, 6TZ, 6PR, 2AY, 2MW, 2NM, 2ST, 3BA, 4GR, 4SEA and 4TOO.

237. We have scaled up the results of our questionnaire to the entire commercial radio industry, a total of 261 radio stations.

# Appendix D. Curriculum Vitae

Jason Ockerby is a founding Director of CEG - Asia Pacific. Jason has a Masters of Economics from the University of Sydney.

Jason Ockerby is an economist with over 15 years experience in competition and regulatory economics and has specialised in the areas of communications, broadcasting, energy, tax and environmental economics.

Jason has appeared before the Federal Court of Australia as an expert witness on telecommunications regulation. He has had statements on regulatory matters accepted by the Australian Competition Tribunal.

Jason has been involved in a number of significant mergers and acquisitions. He has advised the ACCC on sensitive mergers in the communications and broadcasting industry. Jason has also advised private clients on the competition effects of transactions in energy, communications, and mining industries in Australia and overseas.

Jason has worked extensively in the area of communications and broadcasting. He has advised on the full range of communications issues including: content regulation, price squeeze allegations; spectrum licensing, access price costing and regulation, universal service, M&A, resale pricing, cost of capital, imputation testing and LRIC modeling.

In addition, Jason has provided statements to regulators relating to market definition, misuse of market power and competitive effects. This evidence has led to competition remedies being sought and the commencement of Federal Court and other Court proceedings. Jason has had significant experience in advising lawyers and Counsel on economic and quantitative issues in the context of legal proceedings.

Prior to forming CEG Jason was head of economic regulation at SingTel Optus and prior to that was a consulting economist with KPMG and Arthur Andersen. Jason also worked for the Australian Bureau of Agriculture and Resource Economic where he published on natural resource and environmental economics.

In terms of geographical coverage, Jason clients have included businesses and government agencies in Australia, Europe, New Zealand, PNG, Fiji, Samoa, Singapore.

# Detailed Project Experience

## Market Design and Competition Analysis

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| **2011** | **ACCC**<br>**Merger assessment**<br>Provided advice to the ACCC on one confidential acquisition and one proposed transactions. |
| **2011** | **Telecom New Zealand**<br>**Ultra Fast Broadband**<br>Advice in relation to Telecom's participation in the Government's broadband initiative. Economic and market analysis and advice on regulatory matters. |
| **2011** | **Vodafone Hutchison Australia**<br>**ACMA**<br>Advising Vodafone Hutchison Australia in relation to regulations imposed on it by the Australian Communications and Management Authority. |
| **2010** | **Commercial Radio Australia**<br>**ACCC regulation**<br>Report for Commercial Radio Australia in relation to undertaking given to the Australian Competition and Consumer Commission. |
| **2010** | **Webb Henderson**<br>**Digital Radio**<br>Expert report on the conduct of auctions for capacity for the delivery of digital radio in Australia |
| **2010** | **Gilbert and Tobin**<br>**Joint Venture of BHPB and Rio Tinto**<br>Competition and market analysis of iron ore joint venture. |
| **2009** | **AGCOM, Italy**<br>**Development of Imputation Testing for Bitstream**<br>Provide advice and modelling of imputation testing for bitstream service, bundled with telephony (calling and access) services). |
| **2009** | **SingTel Optus, Australia**<br>**Reform of Part XIC**<br>Report for SingTel on the use of forward-looking cost models in access regimes, and impact on regulatory certainty. |
| **2009** | **Hutchison, Australia**<br>**Expiry of Spectrum Licences**<br>Advising Hutchison on the renewal of Spectrum Licences in Australia and the balance of public interest in re-auctioning or re-issuing Licences. |

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| **2009** | **Siwatibau and Sloan Solicitors, Fiji**<br>**Review of Regulatory Determination**<br>Expert statement and appearance before the Competition Tribunal of Samoa on appeal of regulatory decision on interconnection charges. |
| **2009** | **Vodafone, Fiji**<br>**Review of Price Controls on retail fixed and mobile telephony**<br>Provided expert report on role of price controls and supplementary statement in response to critique by Gans. |
| **2008** | **TERRiA**<br>**Tender to build FTTN Network in Australia**<br>Advising TERRiA on competition analysis associated with the construction and operation of a FTTN network. Developing an regulatory model, consideration of compensation issues, and asset valuation. |
| **2008** | **Van Beelen, Australia**<br>**Merger Analysis – Pharmaceuticals**<br>GSK / Astra Zeneca in-depth investigation clearance (without remedies) before the Swedish Competition Authority. |
| **2008** | **Gilbert + Tobin, Australia**<br>**Merger Analysis – New Steel Drum Manufacture**<br>Providing expert opinion to Gilbert + Tobin on the competitive implications of a merger involving new steel drum manufacture. |
| **2008** | **SingTel Optus, Australia**<br>**Structural Separation**<br>Preparation of expert report on costs and benefits of structurally separation of Telstra and the role of price discrimination. |
| **2008** | **Scottish Power, European Union**<br>**Potential acquisition of competitor**<br>Advising Scottish Power on acquisition of nuclear power stations owned by British Energy, including electricity market modelling. |
| **2007** | **SingTel Optus, Australia**<br>**Mobile Termination**<br>Advising on a range of competition matters relating to mobile termination. |
| **2007** | **“G9” Group of Telecommunications Carriers**<br>**Regulatory Undertaking to Build and Operate a FTTN Network in Australia**<br>Advising the G9 on competition analysis associated with the construction and operation of a FTTN network. Developing an regulatory Undertaking under the Australian Trade Practices Act describing the proposed operation of the FTTN. |
| **2007** | **“G9” Group of Telecommunications Carriers**<br>**Sub-loop access**<br>Expert report on potential ‘hold up’ issues in the roll out of a FTTN network and the role of regulation in resolving hold up issues. |

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| 2002-07 | **SingTel Optus, Australia**<br>**Head of Regulatory Economics**<br>Internal advice on competition and market issues including: |

**3G infrastructure sharing with Vodafone**
Analysis of competition effects of 3G network sharing alternatives. Submission to the ACCC and briefing of Mergers Commissioner on competition effects with sharing of network element and core network functions.

**Potential acquisition of AAPT**
Internal reports and briefing on merger clearance process for a potential acquisition of AAPT by Optus. Analysis of the competition effects of the merger and briefing of the ACCC staff and Mergers Commissioner.

**Part XIB competition notice**
Preparation of statement on competition effects of changes to local telephony pricing. Analysis of softening of competition resulting from incumbent raising wholesale and unbundled retail prices whilst keeping bundled retail prices constant.

**Imputation testing**
Submission to the ACCC on imputation testing in telecommunications markets. Analysis of alternative cost bases with economies of scale in retailing.

**Content exclusivity**
Submission to the ACCC on the role of content in competition for fixed and mobile broadband services and implications for current and future bidding for content rights. Analysis of 'tipping' markets and exclusion.

**Foxtel – Optus Content Sharing Arrangement**
Submissions to the ACCC on competitive effects of moving to a monopoly acquirer of content for subscription television services on markets for television services, access services and content supplies (domestic and international). Analysis of possible undertakings to mitigate competition concerns.

## Cost of Capital Issues

2008 **Clayton Utz, Australia**
**Cost of Capital**
Expert testimony to the Federal Court of Australia on alleged errors made by the Australian Competition and Consumer Commission (ACCC) in estimating the cost of capital for Telstra (the incumbent telecommunications provider)..

2008 **Telecom New Zealand, Australia**
**Cost of Capital**

Advising Telecom New Zealand on the appropriate estimation of the cost of capital associated with capital assets used to provide its universal service obligations.

**2008** **Digicel PNG, Australia**
**Cost of Capital – Country Risk Premium**
Advice to Digicel on the size and nature of the country risk in the cost of capital of private businesses competition with Government owned business in jurisdiction with sovereign risk

**2008** **Vodafone, Fiji**
**Cost of Capital**
Advising Vodafone on the appropriate estimation of the cost of capital associated with capital assets used to provide telecommunications services.

**2002-07** **SingTel Optus, Australia**
**Head of Regulatory Economics**
Internal advice on cost of capital issues including:

**Next Generation Access Services**
Analysis of CAPM risk for expected returns from deploying next generation and asset stranding risk in deploying such assets. .

**Mobile services**
Estimation of cost of capital for associated with capital assets for providing mobile telecommunications services.

**Response to Report of Professor Bowman**
Report on approach to the market risk premium and welfare asymmetry. Analysis of the lack of reliability in historic estimates and the need to adjust for international differences as capital market have evolved and transaction costs have reduced. Report on conditions necessary to support welfare asymmetry argument.

**2001** **Integral Energy, Australia**
**Cost of Capital**
Advising Integral Energy on the appropriate estimation of the cost of capital associated with capital assets used to provide electricity distribution services.

## General Regulatory Analysis

**2007/09** **Digicel, PNG/Fiji/Samoa**
**Mobile telecommunications regulation**
Advising Digicel on ongoing issues in mobile telecommunication regulation in PNG and Samoa.

**2008** **Gilbert and Tobin, Australia**
**Commercial Radio Australia**

Expert statement assessing the reasonableness of an alleged related party transaction entered into by Envestra to outsource its operating and maintenance activities to Origin Energy.

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| **2008 Australia** | **Energy Australia, TransGrid, Country Energy and Integral Energy,**<br><br>**Cost escalation forecasts**<br>Advising on appropriate forecasts for costs faced by these businesses over the forthcoming regulatory period. Used as an input into their regulatory cost modelling. |
| **2007** | **Vodafone, Fiji**<br>**Mobile telecommunications regulation**<br>Advising Vodafone Fiji on estimating the cost of mobile termination in Fiji. |
| **2007** | **T-Mobile, UK**<br>**Mobile termination cost modelling**<br>Advise T-Mobile on BT's appeal of the UK Commerce Commission's determination on the cost of mobile termination (specifically in relation to the treatment of 3G spectrum). |
| **2007** | **GSME, Europe**<br>**USO reform**<br>Developing and drafting of submission to the European Commission by the GSME on all aspects of universal service obligation reform, including: the appropriate level of obligations; the use of contestable models of provision, alternative funding models, costing of the obligations. |
| **2007** | **SingTel Optus, Australia**<br>**FTTN**<br>Advise SingTel Optus on all regulatory and competition issues associated with the construction of a FTTN network. Issues include – costing, form of price controls, capital raising and the cost of capital, drafting of undertakings, expert reports submitted to the regulator (Australian Competition and Consumer Commission). |
| **2007** | **Communications Alliance, Australia**<br>**USO reform**<br>Developing and drafting of submission to Government by the Communications Alliance (an industry body covering incumbent and new entrant fixed and mobile carriers) on all aspects of universal service obligation reform, including: the appropriate level of obligations; the use of contestable models of provision, alternative funding models, costing of the obligations. |
| **2002-07** | **SingTel Optus, Australia**<br>**Head of Regulatory Economics**<br>Internal advice on regulatory issues including:<br><br>**Local loop unbundling** |

Briefed Counsel and lawyers (Clayton Utz) in an appeal of an undertaking before the ACT. Advice on TSLRIC modelling, averaging of local loop charges, asymmetry in the cost of capital, minimum spanning tree algorithms and Steiner Tree approaches.

**Mobile Termination Rates**
Briefed of Counsel and lawyers (Gilbert and Tobin) in an appeal of an undertaking before the ACT. Advice on top down LRIC modelling, Ramsey-Boiteux pricing, network externalities and market definition in two-sided markets.

**Spectrum management**
Submission to Government on the regulation of low frequency 3G spectrum in rural areas for roaming or resale. Analysis of Government funding for CDMA infrastructure used jointly in producing low frequency 3G services in rural areas.

**Mobile Termination Rates**
Construction of a bottom up TSLRIC model of GSM mobile services in Australia. Modelling of network architecture, routing, demand and full costing and analysis.

**Internet Peering**
Submission to the ACCC on the need to regulate internet peering or an internet interconnection services. Analysis of service layers, international arrangements and economic authorities on 'tipping' markets.

**Spectrum Sharing**
A brief for Senior Counsel on the levelisation of access prices. In particular how the length of the regulatory period and allowance for cost carryover between regulatory periods affects the efficiency properties of the regulatory arrangements.

**Spare capacity in telecommunications networks**
Analysis of approaches to pricing the cost of spare capacity in telecommunications networks and the capacity needed to meet future demand.

**VoIP**
Internal paper on the future of interconnection charging regimes in a VoIP environment. Survey of international approaches and regulatory arrangements.

**Mobile termination rates**
Advice to lawyers (Gilbert and Tobin) on economic issues in the arbitration of mobile termination charges.

**Fixed wireless services**
Submissions and representation to the ACCC on the regulatory measures associated with a fixed wireless services based on a 3G (HSDPA capable) network.

**Mobile termination rates**

Preparation of submissions in support of Optus' mobile termination charge undertaking. Co-ordination of input into ACCC assessment including lawyers, expert testimony and cost modelling. Responses to submissions of interested parties and ACCC draft decision.

**Mobile termination rates**
Preparation of a top down cost model for GSM mobile services in Australia. Submission to the ACCC (and the Australian Competition Tribunal) on two-sided market analysis in mobile services and the significance of above and below cost pricing for particular services.

**PSTN and local services**
Preparation of various submissions critiquing the incumbent fixed line telephony model used to set access prices for local loop and PSTN services. Analysis of modelling principles including application of 'forward looking' TSLRIC. Review of detail costing algorithms and submissions on costing parameters, sensitivity analysis and geographic cost structures based on international benchmarks.

**Retail minus regulation**
Submission to the ACCC on the retail minus (retail) cost for pricing local telephony services. Analysis of alternative starting prices for retail minus costing and impact on competition and incentives.

**International benchmarking**
Submissions to the ACCC on declaration of mobile termination services, domestic and international roaming services. International benchmarking of mobile termination charges and approaches to setting pricing principles for declared services.

**Access deficit**
Submission to the ACCC on the need to charge an access deficit and the efficiency consequence of funding the access deficit with a levy on PSTN interconnect charges.

**Cost accounting**
Submission to the ACCC on approaches to converting historic cost to current cost asset valuation in Telstra's regulatory accounts. Analysis of Operating Capital Maintenance (OCM) and Financial Capital Maintenance (FCM) approaches.

**Transmission networks**
Submission to the ACCC on the need to regulate particular transmission services. Analysis of competitive models applicable to transmission capacity (potentially unlimited spare capacity) and the need for multiple operators to yield a competitive outcome.

**2001** **Integral Energy, Australia**
**Form of Regulation**

Advice to Integral Energy on form of regulation for distribution networks including advice and modelling of switch from revenue cap to weighted average price cap and role of demand forecasting.

**2001** **Department of Primary Industries and Energy, Australia**
**State Business Tax Reform**
Expert report for the Department of Primary Industries and Energy on a 'profit split' arrangement for determination of petroleum resource rent tax at the Northwest Shelf and Bayu-Undan LNG production facilities.

**2000** **Victorian Department of Treasury and Finance, Australia**
**State Business Tax Reform**
Advised the Department of Treasury and Finance on State business tax reform including in relation to the relative economic costs associated with payroll, stamp duty and other transaction taxes.

**2000** **Victorian Department of Treasury and Finance, Australia**
**State Business Tax Reform**
Advised the Department of Treasury and Finance on State business tax reform including in relation to the relative economic costs associated with payroll, stamp duty and other transaction taxes.

**1999** **Independent Pricing and Regulatory Tribunal of NSW**
**Various energy regulation issues**
Advice on a range of issues in regulation of the NSW energy sector.

**1999** **Australia Competition and Consumer Commission**
**Regulatory accounting**
Preparation of public report on practical issues with the implementation of the Regulatory Accounting Framework

## General Policy Analysis

**2001** **Estee Lauder, Australia**
**Valuation of Intangible asset**
Expert report on appropriate royalty charges submitted to Australia Taxation Office.

**2000** **Attorney Generals Department, Australia**
**Poker machines in developing economies**
Expert report for the Attorney General of Fiji (World Band funded) on the economic consequences of introducing poker machines in the Fiji economy.

**2000** **Various clients, Australia**
**GST replacing the wholesale sales tax arrangements**
Expert report and modelling of the impact on businesses of removing the direct and embedded wholesale tax. Clients included BHP, AGL, Telstra, and Estee Lauder.

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| **1999** | **SOCOG, Australia**<br>**The Impact of the Sydney Olympic Games**<br>General equilibrium model of the Australian economy (MONASH) shocked to determine the impact of hosting the Olympic Games in Sydney in 2000. |
| **1997/99** | **Various clients, Australia**<br>**International transfer pricing documentation and audit defence**<br><br>Expert reports for various businesses providing documentation of international transfer pricing arrangements. Clients included Glaxo-Welcome, Aventis, Wyeth pharmaceuticals, Toyota, Cochlear, Telstra, P&O, Patricks stevedores, Sharp and Fujitsu. |
| **1997/99** | **Various clients, Australia**<br>**Advanced pricing arrangements (APAs) for international transfer prices**<br>Expert reports and advice in negotiating APAs for Makita, Estee Lauder, and Microsoft. |
| **1993-97** | **Australia Bureau of Agriculture and Resource Economics, Australia**<br>**Various economic policy issues**<br>Provided input in the formulation of a number of economic policies. Publications and conference papers include:<br><br>Ockerby, J., Proctor, W. and Corder, C. (1996). Economic criteria for Exceptional Circumstances declarations under the national drought policy. Report to the Bureau of Resource Sciences from the Australian Bureau of Agriculture and Resource Economics, ABARE Project Number 1287.<br><br>Ockerby, J. 1995, 'Regional Salinity Management', Australian Commodities, vol.2, no.2, pp.218-31.<br><br>Beare, S., Gooday, J., Doyle, S. and Ockerby, J. (1995). Agriculture in the rangelands. A study of economic viability. Australian Commodities 2 (4): 498.<br><br>Mues, C., Roper, H. and Ockerby, J. 1994, Survey of Landcare and Land Management Practices: 1992-93, ABARE Research Report 94.6. Canberra.<br><br>Report on modelling water supply in SE Queensland using a linear programming model of water supply options and demand centres.<br><br>Report to the Department of Prime Minister and Cabinet on regional forestry agreements for sustainable forestry. |