FINANCIAL REVIEW

Governance concerns at News Corp

The Australian Financial Review's revelations that a News Corporation subsidiary, NDS, engaged in piracy that damaged its pay TV rivals in Australia, was involved in a runaway pay TV piracy operation in North America, and withheld an anti-piracy fix from a customer in the US, underlines the importance and value of independent journalism. The report, supported by 14,000 emails and a four-year global investigation by *Financial Review* journalist Neil Chenoweth, shines a public interest spotlight on the murky internal workings of a part of News Corporation, one of Australia's largest, most successful global companies.

That spotlight came about because, in the tradition of independent journalism that this newspaper is known for, the *Financial Review* invested in the extraordinary investigative skills of Chenoweth, a world expert on News Corporation.

His detailed, blow-by-blow account of the internal workings of Israeli-based News Datacom Systems, known as NDS, used material that NDS sought to suppress as confidential and fought to keep out of the US courts, but which has been confirmed as authentic. Despite that effort, there is more to be found out. The *Financial Review* has no intention of forming a judgment on the legality or otherwise of the practices uncovered in the emails and through Chenoweth's investigations. This investigation is not motivated by a desire to damage a rival publisher. We are simply doing our job of following the story in the public interest.

NDS was formed in the late 1990s for the legitimate purpose of protecting News Corp's intellectual property and its pay TV revenue from rampant piracy that was damaging its operations.

Pay TV operators issued smartcards to subscribers who then slotted them into set-top boxes in their home. But these cards can be hacked. The card and set-top boxes unscramble the encrypted signals from the provider, and block access to channels that the subscriber has not paid for. At the time, pay TV encryption was a rapidly developing frontier technology and pay TV providers were in a race to keep ahead of the hackers and the pirates.

The information uncovered by Chenoweth suggests that NDS attacked the pirates and prosecuted them, but in so doing obtained encryption codes for the cards operated by rivals. Using that knowledge, it promoted a wave of high-tech piracy that damaged Austar and Optus, the pay TV rivals of Foxtel, which is 25 per cent owned by News Ltd.

Foxtel is now poised to buy Austar. The piracy cost the Australian pay TV companies millions of dollars a year and undermined Austar's finances. As well as harming rivals by fostering piracy, NDS also appears to have withheld a piracy fix from client DirecTV for 15 months just as News Corp chairman Rupert Murdoch was set to buy the company in early 2000. This cost DirecTV millions of dollars in revenue, depressing the company's value. NDS was paid more than $90 million to provide security to DirecTV.

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It is not clear if top News Corporation executives knew of the NDS dirty tricks. NDS reported to the office of Mr Murdoch. The chief operating officer of News Ltd, Chase Carey, was an NDS director and oversaw NDS in the late 1990s. It may be that NDS displayed elements of a rogue operator within the News Corp stable with an agenda that did not always accord with that of its parent.

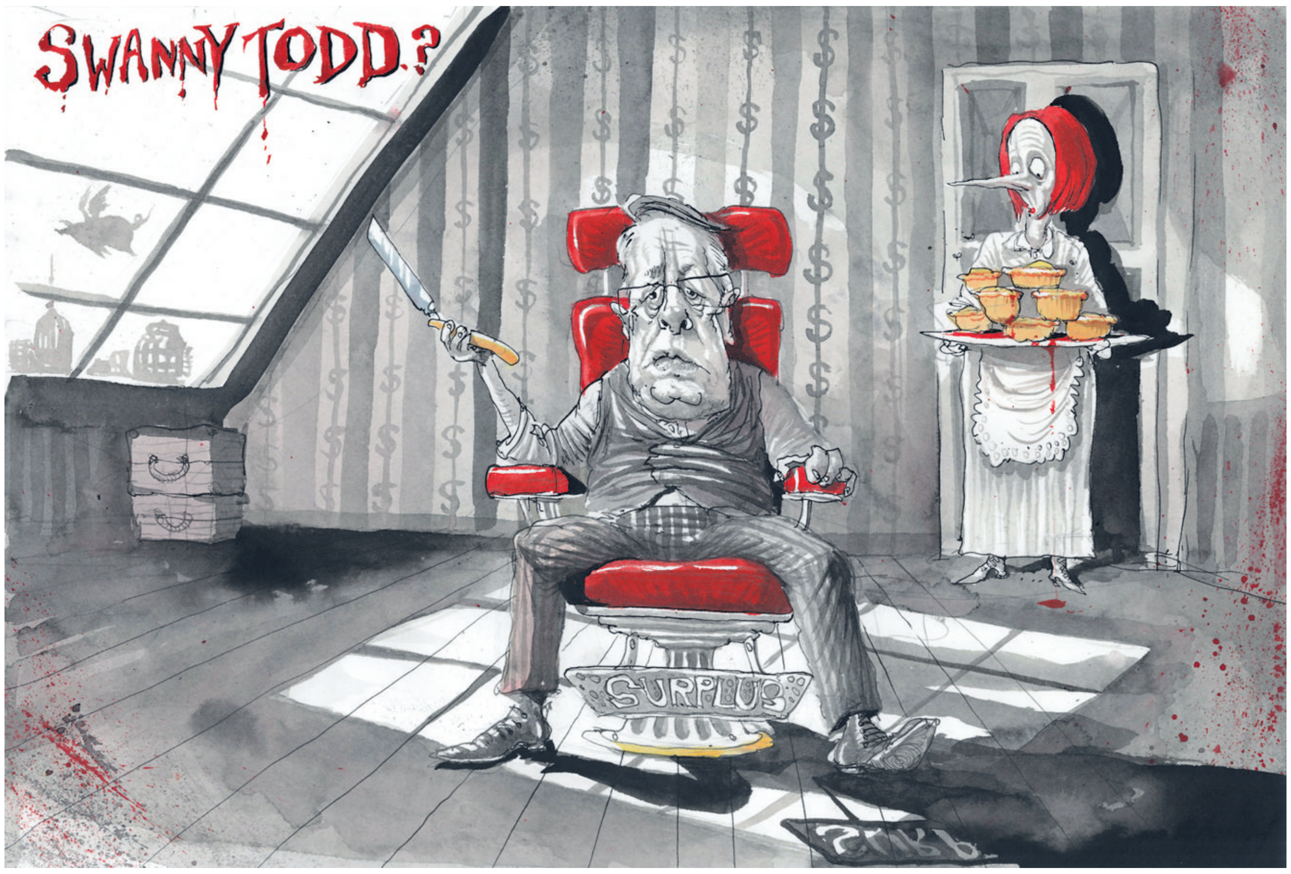
At least until now, there has been no known link between the pay TV piracy allegations and the UK phone hacking scandal that has badly damaged News International, the UK arm of News Corp. The egregious phone hacking by journalists and private investigators at News Corp newspapers and other media companies has no known counterpart in Australia.

The evidence uncovered by Chenoweth, however, reveals that NDS paid £2000 to Surrey police for information. Surrey police are at the centre of the UK phone hacking inquiry. In addition, the emails suggest that NDS intended to procure phone records in Australia illegally. The Australian Federal Police has confirmed that it has been working with UK police investigating News International since July last year, but the content of the investigation is not known.

Under Australian law at the time, hacking and piracy of smartcards was not illegal. But the evidence uncovered by Chenoweth raises legitimate questions about corporate governance, accountability and trust at an important public corporation that go beyond the question of legality. News Corp strongly disputes the conclusions of the *Financial Review*'s investigation.

However, this episode underscores the crucial role of independent journalism, and the importance of allowing the media to play its role without government or regulatory control or interference. The *Financial Review* believes the media should remain unfettered to pursue, in the public interest, the right to know. To that end, we have posted thousands of emails related to our report on afr.com and welcome further investigation into the story they tell.

GALLERY **DAVID ROWE**



Virtual learning curve

There's a seismic shift taking place in higher education, writes **Steven Schwartz**.

After 244 years, the *Encyclopaedia Britannica* is out of print. Sad news, but not exactly a shock. After all, sales had fallen by 95 per cent. It's amazing the company kept going as long as it did.

Britannica wasn't the only icon to vanish this year. Kodak (which once commanded 90 per cent of the photographic film market) abandoned photography, and there's more bad news ahead.

Not waving but drowning in a sea of red ink are EMI, the Beatles' music publisher; Nokia, the giant phone maker; and the once mighty BlackBerry maker Research In Motion.

Their business models no longer work, their products have been superseded and their customers have vanished. Like zombies in a horror movie, they are the walking dead who refuse to lie down and die.

Tech-savvy commentators can barely hide their disdain. Don't the executives leading these companies know they're doomed? Digital technology, the internet and new products (there's an app for that) have killed their business.

The least they could do is bury them before the corpses start to rot. Yet, despite the well-known advice about what to do when you find yourself in a hole, they keep digging.

Stupid, right? Maybe. But let's assume, for argument's sake, that the executives of these companies are just as smart and aware of what is happening around them as we are.

They may still elect to continue running their declining businesses because they remain profitable. Sure, their profits are declining but they may still be greater than what they could earn by abandoning what they are doing and going digital. Consider, for example, the *Encyclopaedia Britannica*.

Its main competitor was Wikipedia, which has millions of articles on every conceivable subject, is continuously updated and, most importantly, is produced and accessed free of charge.

Of course, there's a lot of rubbish in Wikipedia (especially the unkind things someone keeps writing about me), but no one doubts that it will become more authoritative over time.

The people who ran *Encyclopaedia Britannica* knew this. Nevertheless, they kept publishing the print version as it was more profitable than giving their articles away free on the web.

It may not seem obvious, but our universities are more like *Britannica* than they are like Wikipedia.

Our traditional ways of doing things are being undermined by digital upstarts. Instead of long, languid summer breaks, our internet competitors work 24/7 for 52 weeks a year.

Instead of lecturers on a stage armed with PowerPoint slides, online teaching takes place on laptops, tablets and smartphones anywhere the student happens to be. Instead of one-size-fits-all lectures, online teaching is customised to fit an individual student.

To add insult to injury, our fees are being undercut by organisations that do not think it necessary to build libraries, sporting fields and art galleries. Worst of all, our competitors include some of the most famous universities in the world.

The brave new world of digital higher education came closer last December when the Massachusetts Institute of Technology (MIT) announced a new organisation called MITx.

MITx will offer MIT courses online. According to MIT, MITx students will be able to learn at their own pace, interact with teachers, participate in student discussion groups, participate in online laboratories and be assessed for their mastery of the course.

MIT expects to reach "a virtual community of millions of learners around the world". And here is the real game changer. For a "small" fee, MITx will award credentials to successful students. Although they will not receive traditional degrees, successful MITx students will have their learning officially certified by one of the most famous universities in the world.

MITx has minted a new form of academic currency — not a degree but a certificate. Like any currency, the value of a certificate will be judged by whether it is negotiable. If students armed with MITx certificates get good jobs, the certificates will be worth a great deal indeed.

The ground is moving under our universities. The nimble ones will shift their footing but most will hold on tightly to their current business model.

Like the executives at *Britannica* and Kodak, they will still see their role as helping their institutions gracefully decline into oblivion. Too bad, it does not have to be that way.

■ *Steven Schwartz is the vice-chancellor of Macquarie University.*

NOTEBOOK *The Fed eases out*

The Washington Post, March 29.

For what seems like the umpteenth time, US Federal Reserve chairman Ben Bernanke has offered a defence of the Fed's unorthodox policy response to the financial crisis of 2008-09. Without those actions, he told an audience this week, the world economy might have gone into a "total meltdown".

In a way, it's a shame Dr Bernanke still has to go around making that obvious point, but he's right – both about the regrettable necessity of bailing out "too big to fail" firms and about the Fed's subsequent zero-interest rate policy and massive purchases of Treasury bonds and mortgage-backed securities. The US economy remains sluggish despite recent signs of growth but it would be in worse shape if the Fed had not engaged in massive monetary easing.

Still, these benefits come with risks attached. Among the biggest risks is that easy money from the Fed enables banks and firms to postpone necessary restructuring – and for Washington to postpone getting the government's long-term fiscal situation under control.

When it does come, a self-sustaining recovery will undermine the case for fiscal and monetary expansion.

Both Congress and the Fed will then have to react decisively and swiftly to undo a lot of what they've done in the past four years. They still have time to engineer a safe exit but perhaps not quite as much time as they think.