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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of)
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Implementttion of Sections 11)

objectives set forth in the Act.[1/] Specifically, while section 613 is aimed at ensuring that cable operators can not unfairly impede or restrict the flow of video programming from programmers to consumers or to other distributors, it also requires the Commission to avoid prescribing limitations that will "impair the development of diverse and high quality video programming."[2/] Section 613 also counsels the Commission to consider "any efficiencies and other benefits" that might be gained from increased growth and integration in the cable industry.[3/]

In addition to weighing the potential adverse effects and the potential benefits of horizontal and vertical concentration, NCTA urged the Commission to view the ownership provisions in the context of the various other tools that the Act provides for ensuring the flow of diverse programming to consumers and other distributors. Those tools include the "program access" provisions in section 19, the provisions governing program carriage agreements in section 12, and the leased access provisions in section 9. In particular, the recently-adopted

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1/ S. Rep. No. 92, 102d Cong., 1st Sess. 80 (1991).

2/ Section 613(f)(2)(A),(B),(G), 47 U.S.C. section 533(f)(2)(A),(B),(G); Section 613 of the Act also directs the Commission to factor in such general considerations as the cable industry's "market structure, ownership patterns, and other relationships,", as well as the "dynamic nature of the communications marketplace." Additionally, under section 613, the Commission may not impose rules that will prevent cable operators from expanding service to previously unserved rural areas.

3/ Id.

"program access" rules, which define the types of "unfair" conduct and discriminatory practices that are prohibited in the sale of cable programming, provide potent ammunition for the Commission to ensure that vertically-integrated cable companies do not hinder the availability of programming.[4/]

With the program access rules (and other provisions) as the primary defense to any anticompetitive abuse, subscriber limits and channel occupancy limits should merely serve as a protective measure against any radical transformation of the existing market structure. They should not be used as vehicles to rearrange or restructure the cable programming market where there is no evidence to support such dramatic action. Indeed, there is nothing in the record to demonstrate that, as a structural matter, competition and diversity are seriously threatened by consolidation and vertical integration in the cable industry.

Nevertheless, several commenters in this proceeding urge the Commission to adopt regulations that would unreasonably curb, perhaps even rollback, cable's growth and development. As we demonstrate below, the initial comments show that the public will be best served by the adoption of high subscriber limits and high channel occupancy limits and the continued participation by cable operators in program production. But, in any event, we believe

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4/ In the Matter of Development of Competition and Diversity in Video Programming Distribution and Carriage, MM Docket No. 92-265, First Report and Order, 58 Fed. Reg. 27658 (May 11, 1993) ("Program Access Report and Order").

that the Commission should not adopt rules until it has the benefit of further comment assessing the full impact of specific limitations.

I. THE EXISTING RECORD AND ANTITRUST LAW SUPPORT THE ADOPTION OF HIGH SUBSCRIBER LIMITS AND HIGH CHANNEL OCCUPANCY LIMITS

A. Subscriber Limits

In its initial comments, NCTA submitted that a subscriber limit in the range of 40% of homes passed will not pose any undue risk of anti-competitive behavior.[5/] Other parties recommended a 30 - 40 percent threshold, while others recommended a limit as high as 50 percent.[6/] Relying on established antitrust precedent, the commenting parties demonstrated that any of these thresholds falls below the generally-accepted market share that would constitute a monopoly or excessive market power. Indeed, as explained by Time Warner, for example, courts and commentators alike have found that a market share of less than 50 percent is insufficient to establish monopoly power.[7/] Thus, antitrust decisions have held that market shares of 30 or 40 percent would not support an inference of monopolization,[8/] and that a share of

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5/ Comments of NCTA at 15-18.

6/ _See e.g._ Comments of Tele-Communications Inc. ("TCI") (30-40%); Time Warner Entertainment Company (30-40%); Discovery Communications (50%).

7/ Comments of Time Warner at 22-24; _see also_ Comments of TCI at 17-22; Comments of NCTA at 15-18.

8/ Comments of Time Warner at 23.

at least 70 percent could be required.[9/]

Moreover, the empirical evidence shows that the success of a given programming service does not depend on its attaining any particular level of subscriber penetration.[10/] As TCI notes,

> . . . it is clear that . . . a level of penetration greater than 60-70% (the inverse of TCI's proposed horizontal limit of 30-40%) is not a prerequisite to long-term viability for video programmers. There are many popular, established program services that have been in business over an extended period of years with penetration below 60-70%".[11/]

Thus, in light of historical information, there is no basis to believe that a cable operator reaching 40 percent market share could single-handedly preclude the success of a new cable service.

In implementing the subscriber limit, NCTA and others urged the Commission to adopt only national, not regional, limits. Aside from the Congressional focus on national concentration, several parties pointed out that imposing regional limits would be particularly inappropriate since they "would deprive cable operators of the economies of scale and scope that make possible innovative regional programming, enhanced customer service

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9/ I Antitrust Law Developments (Third), 213-14 (1992) (citations omitted); United States v. Aluminum Co. of America, 148 F.2d 416, 424 (2d. Cir. 1945).

10/ Comments of NCTA at 16; Comments of Time Warner at 27-28; Comments of TCI at 24-25.

11/ Comments of TCI at 24-25; Comments of NCTA at 16-17.

capabilities, and the deployment of advanced technology."[12/] According to Continental Cablevision, for example, "clustering of cable systems on a regional basis, creates inherent operating efficiencies", including cost-effective and reliable fiber backbone networks, centralized data processing centers, more efficient employee training, and regional programming ventures and advertising efforts.[13/]

In sum, the record shows that a national subscriber limit of 40 percent preserves important efficiencies and economies of scale for the benefit of consumers without risking adverse consequences for the availability of diverse programming. Moreover, to the extent that an MSO that achieves the 40 percent subscriber limit manifests the ability to adversely affect program distribution, the Commission has rules in place to preclude such behavior.

B. Channel Occupancy Limits

With regard to vertical integration, NCTA recommended that the Commission set channel occupancy limits at a fairly high level so as not to deter continued beneficial investment by cable

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12/ Comments of Cablevision Systems Corp. at 4; see also Comments of Continental Cablevision, Cablevision Industries and Comcast Corp., Viacom International, TCI, Time Warner.

13/ See Comments of Cablevision Systems Corp.; Continental Cablevision.

operators in cable programming networks.[14/] We suggested that the Commission defer the designation of a specific limit until after issues related to the program access provision and other related provisions are resolved. But NCTA argued, and many commenters agreed, that the 20 percent threshold cited in the Commission's Notice is clearly much too low.

As Liberty Media Corporation explained, "in analyzing vertical foreclosure issues, courts consistently have found that a very substantial percentage of the market must be foreclosed even to require further analysis of potential competitive injury." In fact, no antitrust case since the Supreme Court's seminal decision on vertical foreclosure, Jefferson Parish, "has held that vertical foreclosure of less than 50% of the market poses anticompetitive concerns."[15/]

But antitrust precedent aside, overly restrictive channel occupancy limits will impair the development of new program services and threaten the survival of existing services initiated through cable investment. For example, the Learning Channel, which is partly owned by TCI, would be a likely candidate for deletion on a TCI system subject to a 20 percent limitation because it is not a well-established service. As Discovery Communications noted, "consumers would lose a valuable

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14/ See e.g. Comments of Discovery Communications; Turner Broadcasting; TCI; Viacom International; Cablevision Industries and Comcast Corp.

15/ Comments of TCI at 34-35.

programming source -- one providing six hours of commercial-free educational programs for preschoolers each weekday morning as well as remedial reading programs for adults."[16/] Unjustifiably low channel occupancy limits also would create a disincentive for cable operators to invest in new services and foreclose many of the efficiencies associated with vertical integration.

Moreover, as noted above, the newly-adopted program access rules contain "strict attribution standards" in order to ensure that all entities with potential incentives to engage in anticompetitive conduct are covered by the rules.[17/] In light of the foregoing, NCTA believes that a high channel occupancy level, i.e., at least 50 per cent or higher, is entirely justified.

In making the channel occupancy calculation, NCTA and other cable parties urged the Commission to include broadcast, PEG and leased access channels.[18/] These channels, by definition, are

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16/ Comments of Discovery Communications at 10-11.

17/ Program Access Report and Order at para. 11. Although various parties, including NCTA, advocated an attribution standard based on the existence of actual voting or working control, the Commission ruled that a cable operator has an "attributable interest" in a programmer (or is vertically-integrated) if the operator holds an equity interest of five percent or higher -- whether voting or non-voting. There is no exception (such as exists in the broadcast cross-ownership and multiple ownership rules) for cases in which a single entity holds a majority of a programmer's stock, nor is there an exception for limited partnership interests.

18/ Comments of TBS; E! Entertainment Television; Discovery Communications; TCI; Viacom International; Liberty Media Corp.; International Family Entertainment, Inc.

non-affiliated program sources and logically should be counted as part of the operator's overall programming mix. However, pay-per-channel and pay-per-program services, and multiplexed services should be excluded from the calculation since they are typically received by such a small percentage of a system's subscribers.[19/] In addition, we support those commenters who urged the Commission to grandfather existing vertically-integrated programming networks. Requiring divestiture of these services, some of which are still in the early stages of development, would only be detrimental to consumers.[20/]

Cable parties uniformly supported the Commission's tentative conclusion that the channel occupancy limits should apply only to an operator's carrriage of program networks in which that particular operator has an interest, and not to the carriage of any vertically-integrated network. And NCTA recommended that the Commission cap the channel occupancy limits at 36 channels in light of other provisions of the Act (i.e., leased access obligations).[21/] Additionally, we support those commenters who urged the Commission not to apply the limits to

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19/ See Comments of NCTA; TCI; Viacom International; Liberty Media Corporation; International Family Entertainment. As discussed under subscriber limits, there is no indication that Congress intended to include regional programmers in the ownership limitations.

20/ Comments of TCI; Viacom International; Liberty Media Corporation; Discovery Communications.

emerging technologies, such as digital compression or other technologies.[22/] There is no policy rationale for applying programming limits to digitally-compressed channels on vastly expanded systems.

Similarly, we agree with proposals to exempt new programming services from the rules, or alternatively grant them a three-year start-up grace period, in an effort to promote their development in a highly competitive marketplace.[23/] And, as NCTA and others argued, it would be appropriate to phase-out the limits for all cable systems that are subject to effective competition. In those situations, there is no incentive to discriminate against non-affiliated programmers.[24/]

Finally, concerning limits on cable operator participation in program production, NCTA argued that the Commission need not and should not impose any restrictions in light of the various other provisions in the Act addressing concentration and undue control.[25/] Other commenters, such as Discovery Communications and Affiliated Regional Communications, Ltd., made clear that

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22/ See Comments of TCI, Viacom, Cablevision Industries and Comcast Corp.; Liberty Media Corp.

23/ See e.g. Comments of Cablevision at 17; Cablevision Industries Corporation and Comcast Corporation.

24/ Comments of International Family Entertainment at 10; Viacom; Cablevision Industries and Comcast Corporation.

25/ See e.g. Comments of Viacom.

investment by cable operators is critical to the development of new and diverse programming options.

II. THERE IS NO EMPIRICAL EVIDENCE IN THE RECORD TO WARRANT A FREEZE, OR ROLLBACK, OF HORIZONTAL AND VERTICAL CONCENTRATION

Several parties have urged the Commission to cap cable industry growth and development at unreasonably low levels. In particular, the Association of Independent Television Stations, Inc. ("INTV") and the Motion Picture Association of America, Inc. ("MPAA") have ignored Congressional intent by advocating totally arbitrary thresholds with absolutely no empirical evidence to support their position.

A. INTV

In proposing an absurdly low 5 percent (or maximum 10 percent) ownership limit, INTV maintains that the Act obligates the Commission to adopt regulations that will dismantle existing cable ownership patterns. It cites Congressional concerns about increased vertical and horizontal concentration in the cable industry but fails to acknowledge other Congressional findings concerning the benefits of such concentration. Indeed, the House Report noted that

> "the growth of MSOs in the cable industry has produced some efficiencies in administration, distribution, and procurement of programming. . . . Moreover, large MSOs, able to take risks that a small operator would not, can provide a sufficient number of subscribers to encourage new programming entry."

Indeed, the House Report is full of examples of "innovative programming services that would not have been feasible without the financial support of cable system operators".[26/]

Thus, in enacting section 613, Congress did not mandate that the Commission establish limits that will constrict, or even freeze, current levels or concentration. Rather, it gave the Commission the discretion in adopting regulations to balance the potential dangers and the potential benefits of concentration.

INTV also urges the Commission to adopt regional subscriber limits on the grounds that local broadcast advertising revenues are threatened without such limits. It argues that cable operators can serve as the conduit for all competing broadcast signals in the market, and consequently become "the conduit for all local advertising." In such a scenario, INTV alleges, television stations and local cable services which compete with the cable system "find themselves at a considerable

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26/ H.R. Rep. No. 628, 102d Cong., 2d Sess. 43 (1992). Moreover, the Commission, NTIA and other agencies have acknowledged the substantial benefits that have accrued to consumers from increased horizontal and vertical integration. See Competition, Rate Deregulation and the Commission's Policies Relating to the Provision of Cable Television Service, 67 RR 2d 1771, 1794 (1990); Video Program Distribution and Cable Television Current Policy Issues and Recommendations (NTIA Report 88-233) 106 (1988).

disadvantage."[27/]

The notion that local cable systems currently possess the competitive wherewithal to threaten the local broadcast television advertising market is ludricrous. But even assuming that local advertising market share was a basis for imposing ownership limits, there is absolutely no evidence that local broadcast stations are at any "disadvantage" in the local advertising market. Indeed, in 1991, local broadcasters generated $7.57 billion in advertising, compared to $420 million received by local cable operators nationwide.[28/] And during a major period of cable's growth in the video marketplace, 1984 to 1991, broadcast advertising revenues grew almost 49%.[29/]

In any event, the legislative history to section 613 demonstrates that Congress was concerned only with national concentration in the cable industry.[30/] And, as noted earlier, regional limits would undermine certain efficiencies and hinder

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27/ It is hard to envision that local broadcasters are at any disadvantage under the new Cable Act, given that the Act guarantees that up to one third of cable channel capacity must be dedicated to broadcast stations and authorizes broadcast stations to charge for carriage of their signal. Under the must carry rules, cable operators are obligated to give preferential carriage rights to broadcast signals over other independent program services.

28/ TV & Cable Factbook at I-16 (1993).

29/ Id.

30/ Senate Report at 34 (purpose underlying subscriber limits provision is "to address the issue of national concentration.") See Comments of Continental at 1-3; Liberty Media at 30-31.

production of locally and regionally-oriented programming.[31/] Had Congress intended to enact regional limitations, it could have included such directive in the statute. Absent clear indication to the contrary, the imposition of regional subscriber limits is neither required nor appropriate.

INTV also advocates imposing a freeze on the number of cable program services owned by cable MSOs and a cap of 20 percent of existing channel capacity for carriage of vertically-integrated networks. It would also restrict cable participation in program production. INTV states that such restrictions will curtail potential cable domination of the program market and foster program diversity, but it provides absolutely no substantiation for its views. In fact, all of the available evidence indicates that vertically-integrated cable networks do not favor their affiliated networks over non-affiliated networks nor use their power to prevent new independent entrants.[32/] Nevertheless, to the extent such favoritism occurs in isolated areas, the Commission's new program access rules will prevent such anticompetitive behavior.

31/ Comments of Cablevision at 3-6.

32/ See e.g. Benjamin Klein, The Competitive Consequences of Vertical Integration in the Cable Industry, June 1989 (attached to NCTA's initial comments); Stanley M. Besen, et. al., Charles River Associates Inc., An Economic Analysis of the FCC's Proposed Cable Ownership Restrictions, February 9, 1993 (attached to TCI's initial comments); Comments of Discovery Communications at 14-15.

It is evident that by proposing unreasonably low ownership limits, INTV only wants to shackle cable's ability to develop diverse programming alternatives to broadcast television.[33/] And by suggesting that divestiture may be the proper course, INTV would have the Commission destabilize cable system ownership resulting in traumatic disruption of cable service to the public.[34/] Taken together, INTV's proposals reveal its desire to see the imposition of extremely low ownership limits on the cable industry as a means to insulate independent broadcast stations from competition.

B. MPAA

While MPAA acknowledges the Commission's charge to balance the potential benefits and the potential harm from horizontal and vertical concentration, it very one-sidely proposes a cap of 25 percent on the number of subscribers served by a cable operator and a 20 percent limit on vertically-integrated channels.

Its analysis goes no further than to note that (1) the Act has the intended effect of promoting effective competition among multichannel video programming distributors; (2) the Commission must adopt effective, workable program access and leased access regulations; and (3) that the Commission must adopt appropriate

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33/ The National Private Cable Association *et al.* concerns about alleged anticompetitive effects of vertical integration have been addressed in the Commission's program access docket.

34/ *See e.g.* Comments of International Family Entertainment.

attribution criteria. "If these conditions are not met", MPAA maintains, "we reserve the right to seek a lower cap."[35/]

But by simply describing the other provisions of the Act, which address potential anticompetitive conduct by cable entities in the program distribution market, MPAA provides no basis for imposing harsh limitations on cable growth. This is particularly so where there is no qualitative or quantitative support for such measures. In fact, as noted earlier, when the ownership limits are viewed in the context of the Act's behavioral rules, there is a strong basis for adopting much higher subscriber limits. Moreover, as we have shown, capping subscriber limits at a low level is likely to stifle investment in new programming rather than promote diversity.

Similarly, with regard to channel occupancy limits, MPAA's proposal of 20 percent is devoid of any empirical support. It simply notes that this "simple and straightforward" channel occupancy limit will help to reduce the risk that a cable MSO will favor program services in which it has a financial stake and will avoid chilling new programming investment.[36/] But so-called simplicity aside, where is the evidence that an extremely low limit of 20 percent will promote these goals? In the end, MPAA

35/ Comments of MPAA at 5-6.

36/ Comments of MPAA at 7-8.

provides nothing to justify its assertions.[37/]

C. Local Governments

Finally, the National Association of Telecommunications Officers and Advisors, the National League of Cities, and other governmental organizations argue in a joint filing that subscriber limits should be in place to curb cable market power. They suggest that a 25 percent cap would be appropriate, even if it would require some MSOs to divest current holdings. For the reasons described above, there is no legal or empirical support for a 25 percent subscriber limitation.

Additionally, the local governments seek the authority to enforce the channel occupancy limits, including requiring cable operators to submit information to the Commission on their attributable interests in programming networks. Franchising authorities would in turn access this information to enforce the rules. Under their proposal the cable operator would certify its compliance with the limits to the franchising authority and recertify such compliance prior to any change in the channel line-up.

As NCTA maintained in its initial comments, the certification approach is a singularly bad idea. It will

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37/ Another commenter, David Waterman, Adjunct Professor, Annenberg School of Communications, University of Southern California, theorizes that horizontal and vertical ownership limits should be below the 25-35 percent mark. He concedes, however, that empirical evidence to support his views is lacking at this time. Comments of David Waterman at 5, 23.

intensify, not minimize, the burden on cable operators and franchise authorities in contravention of the Act. And the vast majority of franchise authorities are not likely to have knowledge of, or the resources and expertise to determine, the ownership structure of the various programmers offered by the systems in their communities. A far better, and less burdensome approach, is for the Commission to enforce the channel occupancy limits on a complaint basis.[38/]

CONCLUSION

For the foregoing reasons, the Commission should adopt subscriber limits in the range of 40 percent and should adopt channel occupancy limits of at least 50 percent. The Commission should also not impose further limitations on a cable operator's participation in the production or creation of cable programming.