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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Implementation of Section 11(c)	)	
of the Cable Television Consumer	)	MM Docket No. 92-264
Protection and Competition Act of 1992	)	
	)	
Vertical Ownership Limits	)	

MEMORANDUM OPINION AND ORDER ON RECONSIDERATION OF THE SECOND REPORT AND ORDER

Adopted: April 5, 1995 Released: April 6, 1995

By the Commission:

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I. INTRODUCTION

1. This *Memorandum Opinion and Order* disposes of petitions for reconsideration filed by the Center for Media Education/Consumer Federation of America ("CME") and Bell Atlantic Corporation ("Bell Atlantic").[1] The petitions seek reconsideration of certain aspects of the *Second Report and Order* in MM Docket 92-264 ("*Second Report and Order*"),[2] in which the Commission, among other things, established rules limiting the number of cable channels that a cable operator can devote to video programming services in which the cable operator has an attributable interest ("channel occupancy limits").[3]

2. Generally, CME asks the Commission to reconsider the *Second Report and Order* by: (1) reducing the channel occupancy limit from 40% to 20% of activated channels; (2) reversing our decision to include over-the-air broadcast,[4] public, educational and government ("PEG"), and leased access channels when calculating total channel capacity; (3) reversing our decision to exempt local and regional networks from channel occupancy limits; (4) reversing our decision not to apply channel occupancy limits beyond a system's first 75 channels; and (5) reversing our decision to grandfather all vertically integrated programming services being carried as of December 4, 1992, the effective date of the Cable Television Consumer Protection and Competition Act of 1992 (the "1992 Cable Act"). Bell Atlantic asks us to reconsider our decision to apply the channel occupancy limits to cable systems that face actual head-to-head competition.

3. For the reasons set forth below, we deny CME's and Bell Atlantic's petitions and reaffirm our decision in the *Second Report and Order*.

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[1] A list of the parties responding to the petitions on the issue of channel occupancy limits is attached as Appendix A.

[2] 8 FCC Rcd 8565 (1993).

[3] Also currently under reconsideration in MM Docket No. 92-264 are the Commission's horizontal ownership limits, 47 C.F.R. § 76.503, and the attribution standard we adopted for both the horizontal ownership rules and the channel occupancy limits. This *Memorandum Opinion and Order* only deals with the cable channel occupancy rules, 47 C.F.R. § 76.504.

[4] CME seems to use the terms "broadcast channels" and "must-carry channels" interchangeably. In the interest of consistency, we will use the term "broadcast channel" to refer to any over-the-air broadcast station being carried by a cable system, whether they are "must-carry" stations or not.

II. BACKGROUND

4. Section 11(c)(2)(B) of the 1992 Cable Act[5] requires the Commission "to prescribe rules and regulations establishing reasonable limits on the number of channels on a cable system that can be occupied by a video programmer in which a cable operator has an attributable interest."[6] This provision grew out of Congress' concern that vertical integration in the cable industry had given cable operators the incentive and ability to favor their affiliated programmers over unaffiliated programmers.[7] As a result, Congress found that unaffiliated programmers may have difficulty in obtaining carriage on vertically integrated cable systems. In addition to impeding competition, the record before Congress indicated that vertical integration could limit the diversity of cable programming and reduce the number of voices available to the public.[8]

5. However, there was also evidence before Congress that vertical integration is not necessarily anti-competitive. The House Report cited a 1988 study by the National Telecommunications and Information Administration which concluded that common ownership of cable systems and cable programmers did not appear to have adversely affected

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[5] Cable Television Consumer Protection and Competition Act of 1992, Pub. L. No. 102-385, 106 Stat. 1460 (1992).

[6] Section 11(c)(2)(B) of the 1992 Cable Act, 47 U.S.C. §533(f)(1)(B). Congress complemented Section 11's structural constraints on vertical integration with prohibitions on specific types of unfair or discriminatory behavior. For example, Section 12 of the 1992 Cable Act prohibits, among other things, cable operators from discriminating against unaffiliated programmers in the selection, terms, or conditions of carriage ("program carriage" rules); Section 19 prohibits unfair methods of competition, and proscribes several specific practices by vertically-integrated cable operators and programming services, in order to make such programming services available to cable's competitors ("program access" rules).

[7] *See, e.g.*, Section 2(a)(5), 1992 Cable Act. Section 11's legislative history is discussed at length in the *Second Report and Order*. We restate part of that history here for the convenience of the reader.

[8] *See* Report of the House Committee on Energy and Commerce, H.R. Rep. No. 102-628 ("House Report"), 102d Cong., 2d Sess. 41, 43 (1992). The House Report also stated that some vertically integrated cable operators discriminated against unaffiliated programming services regarding price, channel positioning, and promotion. *Id.* at 41. Likewise, the Senate Report examined cable operators' exercise of "market power derived from their de facto exclusive franchises and lack of local competition" and stated that "[t]hese concerns are exacerbated by the increased vertical integration of the cable industry." Report of the Senate Committee on Commerce, Science, and Transportation, S. Rep. No. 102-92 ("Senate Report"), 102d Cong., 1st Sess. 24 (1991).

the amount or diversity of programming choices, and that the largest cable operators did not show a pattern of favoring the programmers with which they were affiliated.[9]

6. At the same time, the record before Congress demonstrated that vertical integration could produce certain legitimate benefits. For instance, the Senate Report cited testimony that "vertical integration has been the means by which we have stimulated the development of programming that was necessary to flesh out the promise of cable . . . when nobody else was really willing to step up and put up the money."[10] Similarly, the House Report cited testimony that the financial support of vertically integrated cable operators made the creation of innovative and risky programming possible.[11] In particular, these witnesses pointed to C-Span, Cable News Network ("CNN"), Black Entertainment Television ("BET"), Nickelodeon, and the Discovery channel as examples of innovative programming services that would not have been feasible without the financial support of cable operators.[12]

7. In light of these competing interests, Congress expressly directed the Commission to consider and balance the following factors in establishing "reasonable" ownership limits under Section 11: (1) ensure that no cable operator or group of cable operators can unfairly impede the flow of video programming from the programmer to the consumer; (2) ensure that cable operators do not favor affiliated video programmers in determining carriage and do not unreasonably restrict the flow of video programming of affiliated video programmers to other video distributors; (3) take account of the market structure, ownership patterns, and other relationships of the cable industry, including the market power of the local franchise, joint ownership of cable systems and video programmers, and the various types of non-equity controlling interests; (4) take into account any efficiencies and other benefits that might be gained through increased ownership or control; (5) make rules and regulations that reflect the dynamic nature of the communications marketplace; (6) impose no limitations that would prevent cable operators from serving previously unserved rural areas; and (7) impose no limitations that would impair the development of diverse and high quality programming.[13]

8. Pursuant to the statutory requirements of Section 11, the *Second Report and*

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[9] House Report at 41.

[10] Senate Report at 27, citing testimony of James Mooney (NCTA), "Oversight of Cable TV," pp. 178-79.

[11] House Report at 41.

[12] *Id.*

[13] 47 U.S.C. § 533(f)(2).

Order[14] established channel occupancy rules, including the following rules relevant here:

(a) *Percentage Limitation* -- Cable operators may devote no more than 40% of their activated channels to the carriage of programming services in which they have an attributable interest.[15] After consideration of the comments and the competing interests identified by Congress, the Commission found that the 40% limit "is appropriate to balance the goals of increasing diversity and reducing the incentive and ability of vertically integrated cable operators to favor their affiliated programming, with the benefits and efficiencies associated with vertical integration."[16] The Commission adopted the broadcast attribution rules for purposes of determining when a vertical ownership interest would be "attributable."[17]

(b) *Calculation of Channel Capacity* -- All activated channels will be included in calculating channel capacity, including broadcast, PEG and leased access channels.[18] Among other reasons, we noted that these channels promoted diversity and provided alternative sources of unaffiliated programming to subscribers in furtherance of the 1992 Cable Act's objectives.[19]

(c) *Local and Regional Networks* -- Channel occupancy limits will apply only to "national" programming services (i.e., local and regional programming services are exempt).[20] We considered such an exemption to be an important means of encouraging continued investment by multiple-system operators ("MSOs") in the development of local

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[14] Prior to the *Second Report and Order*, we issued a *Notice of Proposed Rulemaking and Notice of Inquiry*, 8 FCC Rcd 210 (1992)("*Notice*"), seeking comment on various issues relating to channel occupancy limits. Subsequently, we issued a *Report and Order and Further Notice of Proposed Rulemaking*, 8 FCC Rcd 6828 (1993)("*Further Notice*"), seeking additional comment on specific proposals regarding the adoption and implementation of the issues identified in the *Notice*, including those issues raised by Petitioners here.

[15] A cable operator may devote two additional channels, or up to 45% of its channel capacity, whichever is greater, to the carriage of video programming owned by or attributable to the operator provided such video programming is minority-controlled. The petitions do not directly ask us to reconsider this aspect of the channel occupancy rules.

[16] *Second Report and Order* at ¶¶ 68-71.

[17] *Id.* at ¶¶ 61-63; *See also* 47 C.F.R. § 73.3555.

[18] *Id.* at ¶ 54.

[19] *Id.*

[20] *Id.* at ¶ 78.

cable programming, which is responsive to the needs and tastes of local audiences and serves Congress' objectives of promoting localism.[21]

(d) *75-Channel Cap* -- Channel occupancy limits will apply to a maximum of 75 channels per system.[22] We found that since exceeding this level was possible only with the deployment of emerging technologies such as fiber optic cable or digital signal compression, the greatly expanded channel capacities provided by these technologies would help obviate the need for channel occupancy limits as a means of encouraging cable operators to carry unaffiliated programming.[23]

(e) *Grandfathering of Existing Vertical Relationships* -- All vertically integrated programming services carried as of the effective date of the 1992 Cable Act (December 4, 1992) could continue to be carried.[24] We found that the public interest would be disserved by requiring cable operators to delete vertically integrated programming in order to comply with the new channel occupancy caps. We believed that permitting the continuation of existing relationships would prevent subscriber confusion, and would minimize the disruption to existing programming services and existing carriage agreements.[25] However, once additional capacity becomes available on such a system, the cable operator may not add any additional affiliated programming until its system fully complies with the channel occupancy limits.[26]

(f) *Effective Competition* -- Channel occupancy limits will not be eliminated in communities where actual head-to-head competition exists.[27] We found that the competition standard in the 1992 Cable Act was not adopted for the same purpose as the vertical ownership limits, and thus it may not address all of Section 11's relevant concerns.

III. PETITIONS FOR RECONSIDERATION

9. We have again reviewed the record in light of Petitioners' arguments on reconsideration and find no reason to depart from our prior rulings in the *Second Report and*

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[21] *Id.*

[22] *Id.* at ¶¶ 83-84.

[23] *Id.*

[24] *Id.* at ¶¶ 93-94.

[25] *Id.*

[26] *Id.*

[27] *Id.* at ¶ 88.

Order. We briefly address Petitioners' contentions below.

A. CME Petition

10. CME filed a joint *Petition for Reconsideration* asking the Commission to reconsider several issues decided in the *Second Report and Order*. Specifically, CME asks the Commission to: (1) reduce the channel occupancy limit from 40% to 20%; (2) require that broadcast, PEG, and leased access channels be subtracted from the number of activated channels before calculating total channel capacity; (3) eliminate our exemption for local and regional networks; (4) apply channel occupancy limits beyond a system's first 75 channels; and (5) reverse our decision to grandfather all vertically integrated programming services carried as of December 4, 1992.

11. *Percentage Limitation*. In asking that the Commission lower its channel occupancy limit from 40% to 20%, CME argues that the Commission overstated the benefits of vertical integration. For instance, CME asserts that "there has been no successful launch of an unaffiliated video programmer since the cable industry began the trend toward vertical integration,"[28] and that MSO investment is not vital because programming services like CNN, BET and Nickelodeon were successful prior to any operator affiliation.[29] CME also states that the Commission ignored a potential scenario submitted during the rulemaking proceeding by the Motion Picture Association of America ("MPAA"), showing that a 40% channel occupancy limit applied to a 36-channel system could result in no channels being available for unaffiliated programmers.[30] Finally, CME contends that its proposal would not harm investment in programming services. By lowering the channel occupancy limit to 20%, CME states that many MSOs could still invest in new programming, while retention of the 40% limit "will likely chill the development of independent programming by providing a disincentive to independent investors who may want to invest in video programming but feel there would be no way to get carriage on a cable system that also owns a substantial percentage of programming."[31]

12. *Comments*. Several parties dispute CME's contentions regarding the consequences of vertical integration. Liberty Media Corporation ("Liberty Media") states that services like CNN and BET "credit their very existence to timely investments by cable operators when no one else was willing to make a similar investment,"[32] and that CME's

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[28] CME Petition at 19.

[29] *Id.*

[30] *Id.* at 15.

[31] *Id.* at 19-20.

[32] Liberty Media Opposition at 17.

proposed channel occupancy limits would "stifle investment in new programming services and disrupt existing program schedules."[33] Turner Broadcasting System, Inc. ("TBS") cites ESPN2, FLIX, and the Sci-Fi Channel as examples of unaffiliated programming which became successful even after the industry trend towards vertical integration.[34] On the other hand, the National Cable Television Association ("NCTA") contends that CME gives no support for its conclusion that the 40% limit will not prevent discrimination against unaffiliated programmers.[35] Tele-Communications, Inc. ("TCI") takes issue with CME's assertion that the 40% limit could result in no channels being made available to unaffiliated video programmers, and states that "[m]any services unaffiliated with TCI, such as the Nashville Network, Lifetime, the USA Network, and ESPN, have nearly universal carriage on TCI systems. By contrast, a number of services in which TCI has an attributable interest, such as the Learning Channel, Courtroom Television Network, and E! Entertainment, are carried on less than one-third of TCI's systems."[36]

13. In reply, CME states that while it agrees that Congress required a balance to be struck in Section 11,[37] Congress rejected the notion that ownership limits were not needed because the benefits of vertical integration outweighed the dangers.[38] By giving too much weight to the alleged benefits of vertical integration, CME argues that the Commission did not adhere to the regulatory scheme contemplated by the 1992 Cable Act.[39]

14. *Discussion*. After consideration of the various submissions, we decline to modify the 40% channel occupancy limit. As CME acknowledges, in requiring the Commission to establish "reasonable" channel occupancy limits, Congress directed us to balance the risks of vertical integration against benefits such as the development of diverse and high quality video programming. We continue to believe that the 40% limit strikes the appropriate balance between these competing objectives. We note, in this regard, that CME filed the only petition seeking reconsideration of the 40% limit. No cable operator or cable programmer filed for reconsideration claiming that the channel occupancy limit was set too low to encourage continued investment. Conversely, none of the parties that previously

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[33] *Id.* at 18.

[34] TBS Opposition at 2.

[35] NCTA Opposition at 16.

[36] TCI Opposition at note 23.

[37] CME Reply to Oppositions at 2.

[38] *Id.*

[39] *Id.*

proposed a lower occupancy limit,[40] and no unaffiliated programmers (with the partial exception of Viacom International, Inc. ("Viacom")),[41] has joined CME in claiming that the limit was set too high to deter discriminatory conduct.

15. We are not persuaded by CME's arguments to reduce the channel occupancy limit from 40% to 20%. First, CME claims that the *Second Report and Order* "erroneously ignored evidence provided by the Motion Picture Association of America ("MPAA") that a 40% limit could result in instances where no channels are available to unaffiliated programmers."[42] However, CME then quotes at length from our response (which we hereby reaffirm) to MPAA's hypothetical scenario. Generally, we pointed out that MPAA's calculation failed to take into account that broadcast, PEG and leased access channels already provided substantial unaffiliated programming, and assumed that large cable operators would drop popular, unaffiliated programming in favor of less popular affiliated services.[43] Indeed, despite vertical integration, 8 of the top 25 programming services have no cable ownership affiliation, while the identity of these popular services has remained relatively stable since 1990.[44]

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[40] *See, e.g.*, Comments of the Association of Independent Television Stations, Inc., filed February 9, 1993 (proposing to impose an immediate channel occupancy limit of 20%, and to prohibit cable operators prospectively from acquiring equity interests in additional programming services); Comments of the Motion Picture Association of America, filed February 9, 1993 (advocating a 20% occupancy limit for affiliated programming in which a cable operator has a 15% ownership interest).

[41] Viacom supports CME's request for a 20% channel occupancy limit only if we do not adopt Viacom's proposed 15% horizontal ownership limit; even then Viacom would only apply the 20% occupancy limit to those cable operators exceeding a 15% horizontal ownership level. *See* Viacom Comments at 15-18. In today's market, that means that Viacom would apply a 20% channel occupancy limit only to TCI, and possibly to Time Warner Entertainment Company, L.P. ("Time Warner"). *See First Report on the Status of Competition in the Market for the Delivery of Video Programming*, CS Docket No. 94-48 (released September 28, 1994) ("*First Competition Report*"), Appendix G-1, G-2. To the extent Viacom's suggestion requires a response, we decline to adopt a stricter channel occupancy limit for a small number of the largest cable operators on the same grounds that we decline to adopt a stricter occupancy limit for all cable operators.

[42] CME Petition at 15.

[43] *See Second Report and Order*, at n. 88.

[44] *First Competition Report*, ¶¶ 162-63; Appendix at G-14. Since 1990, only three new programming services have entered the top 25; of those services, one is vertically integrated and two are not. Also since 1990, cable operators have acquired ownership interests in two of the top 25 services and divested interests in one. *Id.*

16. Moreover, CME may have overstated the practical effect of must-carry, PEG and leased access requirements. In the absence of record evidence on this point, the Commission examined an unscientific sampling of 25 TCI and Time Warner Entertainment Company, L.P. ("Time Warner") cable systems (those being the most vertically integrated cable operators) in order to determine whether, in fact, broadcast, PEG and leased access channels occupied all, or nearly all, of the systems' unaffiliated programming channels.[45] Generally, the Commission found that, even after excluding broadcast, PEG and leased access channels (and even assuming the presence of two local or regional networks), all of the systems had capacity remaining for additional unaffiliated programming.[46] The disparity between our findings and CME's hypothetical scenario is largely due to the fact that a cable operator's theoretical must-carry requirement typically well exceeds the channels that are actually required to be devoted to that obligation. While the Commission's survey was admittedly unscientific, we do believe it lends some credence to our view that CME's worst-case scenario may have limited real world significance.

17. Next, CME claims that we overstated the benefits of vertical integration. As proof, CME states that CNN, BET, and Nickelodeon were successful prior to their relationship with cable operators, and that "there has been no successful launch of an unaffiliated video programmer since the cable industry began the trend toward vertical integration." Whether or not CNN, BET and Nickelodeon achieved some initial independent success, there is evidence in the record that these and other programmers would have had difficulty sustaining their success had it not been for cable operator investment.[47] Likewise, CME's assertion that there has been no successful launch of an unaffiliated programmer since vertical integration has taken hold was disputed by TBS, citing the recent successes of

[45] The Commission sampled 9 TCI systems and 5 Time Warner systems of 35-41 activated channels ("smaller systems"), and 6 TCI systems and 5 Time Warner systems of 48-57 activated channels ("larger systems"). The survey was based on information supplied by the cable operators themselves in the Television and Cable Factbook, Vol. 62 (1994 ed.). *See* Appendix B.

[46] *Id.* TCI smaller systems had between 5 and 11 channels available for additional unaffiliated programming; TCI larger systems had between 6 and 20 such channels available; Time Warner smaller systems had between 6 and 9 such channels available; and Time Warner larger systems had between 10 and 17 such channels available.

[47] *See, e.g., Comments of Turner Broadcasting System, Inc.*, filed 2/9/93, at 12 (at a time when TBS's "independence was very much at stake," cable operators were willing to provide long-term equity under terms others were not); *Opposition of Black Entertainment Television, Inc. to Comments of Viacom International, Inc.*, filed 2/22/94, at 2 ("[C]able investment has been crucial to establishing BET as a viable and valuable programming service.").

ESPN2, FLIX and the SciFi Channel.[48] CME did not take issue with TBS's examples on reply.

18. Similarly, there is no evidence in the record to substantiate CME's claim that the 40% limit will deter independent investors from investing in video programming, or that independent investors are currently deterred from investing in cable programming by our channel occupancy limits.

19. Finally, we disagree with CME's assertion that the Senate Report "suggested" a 20% channel occupancy limit. The Senate Report stated: "For example, the FCC may conclude that each MSO should control no more than 20 percent of the channels on any cable system . . . ."[49] Thus, the Report used the 20% figure for illustrative purposes only, while clearly acknowledging that the Commission was free to choose a different limit. This interpretation is supported by the actual wording of the statute, which simply requires the Commission to establish "reasonable" channel occupancy limits.

20. *Calculation of Channel Capacity*. CME asks that the Commission reverse its decision to include broadcast, PEG, and leased access channels when calculating system capacity.[50] CME asserts that these channels should not be counted because broadcast channels are only available to local broadcast stations, PEG channels are available only to public, educational, and governmental institutions, and leased access has limited capacity and requires unaffiliated programmers to pay for carriage.[51] CME also maintains that the legislative history indicates that these channels should be subtracted before application of channel occupancy limits.[52] Finally, CME argues that because Congress enacted three

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[48] In fact, ESPN2, a service with no cable ownership, had the highest initial market penetration of any programming service launched in the last four years. *First Competition Report*, at 81. It is unclear to what extent this success is related to "retransmission consent" negotiations between ESPN2's network corporate affiliate, ABC/Capital Cities, Inc., and cable operators. *See* 47 U.S.C. § 325(b).

[49] Senate Report at 80 (emphasis added).

[50] CME Petition at 17.

[51] CME Petition at 16-18.

[52] The Senate Report stated in relevant part:

> The intent of this provision is to place reasonable limits on the number of channels that can be occupied by each MSO's programming services. For example, the FCC may conclude that each MSO should control no more than 20 percent of the channels on any cable system, with a minimum of 6 channels

separate provisions -- channel occupancy limits, broadcast carriage requirements and leased access -- to increase the diversity of ownership and ideas in the cable industry, it would contravene Congress' regulatory intent to use two of those provisions as grounds for weakening the third.[53]

21. *Comments*. In opposition, TCI states that it is "unaware of any case where it has been deemed appropriate to exclude from the market being examined a particular quantity of output merely because it is produced by a firm other than a vertically integrated firm,"[54] and that:

> [L]eased access, PEG and must carry channels themselves constitute significant channel occupancy limits and clearly dilute the ability of a cable operator to exercise market power over all channels on it system. Therefore, such channels are properly included in the universe of channels for determining channel occupancy limits.[55]

22. NCTA argues that "excluding such channels would penalize those operators who offer a wide array of broadcast and access services by limiting their options in programming their remaining channels."[56] Further, NCTA states that mandated carriage of PEG, must-carry and leased access channels promotes the same goals (such as diversity) as channel occupancy limits.[57] In addition, Time Warner asserts that Congress' objective was diversity of programming sources, and that PEG, leased access and broadcast programming

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> being permissible. The FCC should establish [channel occupancy] rules based on the number of activated channels less the numbers of over-the-air broadcast signals carried and the number of public, educational and governmental and leased access channels carried. On a system with 54 channels, 14 of which are occupied by over-the-air signals or access channels, the limit then would be eight channels that could be occupied by programming owned by an MSO . . . "

Senate Report at 80.

[53] CME Petition at 16-18.

[54] TCI Opposition at 11.

[55] *Id.* at 11-12.

[56] NCTA Opposition at 12-13.

[57] *Id.* at 13.

are as "diverse" as any other unaffiliated programmers.[58] Time Warner states that as a result of must-carry, PEG and leased access requirements, it can no longer select the programming on an average of 30%, and in some cases as much as 50%, of its systems' channels.[59] Finally, Liberty Media asserts that simply because PEG, must-carry and leased access "also serve other objectives does not detract from their effectiveness in ensuring that cable subscribers receive programming and information from sources unaffiliated with the cable operator."[60]

23. CME replies that the purpose of channel occupancy caps was to "give independent commercial programmers a chance to get on the wire."[61] Thus, while MSOs may view PEG, must-carry, and leased access as "lost" channels, they do not benefit independent programmers, and should be excluded when calculating channel capacity.[62]

24. *Discussion*. We deny CME's petition to reconsider our treatment of over-the-air broadcast, PEG and leased access channels. CME correctly notes that the channel occupancy limits are intended to keep cable operators from filling every available channel with their own programming. But from this premise, CME draws the conclusion that channel occupancy limits must therefore be intended to give "independent commercial programmers a chance to get on the wire." The statute, however, does not distinguish between "independent" unaffiliated programmers and other types of unaffiliated programmers. Section 11 simply ensures that subscribers will have access to some kind of unaffiliated programming on a prescribed number of channels. CME does not dispute that broadcast, PEG and leased access channels are "unaffiliated" with cable operators, or that the 1992 Cable Act requires cable operators to reserve channel space for such unaffiliated programming. Thus, we reaffirm our holding in the *Second Report and Order* that it would be unreasonable to subtract such channels before calculating the system's channel capacity, since they provide the type of diverse, unaffiliated programming contemplated by the 1992 Cable Act. Further, as we noted in the *Second Report and Order*, it would be unfair to penalize those cable operators who carried the widest array of broadcast, PEG and leased access channels by decreasing the number of channels available for affiliated programming.

25. Moreover, there is no evidence in the record that "independent" commercial programmers (i.e., those with no cable ownership interests at all) are unable to obtain carriage because of our treatment of broadcast, PEG and leased access channels. To the

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[58] Time Warner Opposition at 12.

[59] *Id*. at 13.

[60] Liberty Media Opposition at 15-16.

[61] CME Reply at 7.

[62] CME Reply at 7-8.

contrary, in the Commission's sampling of 25 TCI and Time Warner cable systems described above, we found that all of the systems carried some "independent" unaffiliated programmers, with most systems carrying between 7 and 11 such channels.[63]

26. In addition, although the Senate Report's sample calculation excluded broadcast and access channels in calculating channel capacity, CME's reliance on it as an expression of Congressional intent is misplaced. As we stated in the *Second Report and Order*:

> The Senate Report language [. . .] appears to be included merely as an example to illustrate how the Commission may decide to calculate channel occupancy limits and therefore does not prohibit the Commission from adopting an alternative approach if it finds such an approach to be reasonable to promote the legislative objectives. In any event, this language is not included in the statute itself.[64]

27. Finally, we do not believe that we are weakening Congress' statutory scheme by considering the impact of other provisions of the 1992 Cable Act in establishing channel occupancy limits. Section 11 expressly gives the Commission broad discretion to fashion "reasonable" channel occupancy limits. In our view, establishing "reasonable" limits requires us to consider *all* factors bearing on the dangers or benefits of vertical integration. Thus, for instance, we believe that not only should we take into account the impact of broadcast, PEG and leased access channels, but also the impact of Sections 12 and 19 in deterring the types of discriminatory conduct that may be caused by vertical integration. Only by considering the whole of Congress' scheme can we determine the level of vertical structural limits that are "reasonable."

28. *Local and Regional Networks*. In a footnote, CME implies that the Commission should reconsider its decision that local and regional networks will not be subject to channel occupancy limits.[65] CME contends that Congress did not allow for such an exception, and quotes comments of the National Association of Telecommunications

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[63] *See* Appendix B. TCI smaller systems (approximately 36 channels) carried between 7 and 10 "independent" programmers; TCI larger systems (approximately 54 channels) carried between 9 and 13; Time Warner smaller systems carried between 5 and 14; and Time Warner larger systems carried between 9 and 14. Among the independent unaffiliated programming services being carried by the 25 systems sampled were: A & E, ESPN, CNBC, Lifetime, Prevue, The Weather Channel, WGN, Univision, Faith and Value, EWTN, Spice, The Travel Channel and National Jewish TV. *Id.*

[64] *Second Report and Order* at ¶ 54.

[65] CME Petition at note 10.

Officers and Advisors ("NATOA") during the rulemaking proceeding that "most local and regional networks are owned by large MSO's, and as such are part of the trend of vertical integration Congress meant to address with the Cable Act."[66]

29. *Comments*. Affiliated Regional Communications, Ltd. ("ARC"), Time Warner and Liberty Media argue that CME's proposal is contrary to the fundamental goals of the 1992 Cable Act, especially Section 2(a)(10), which states that there is a "substantial government interest" in the "local origination of programming."[67] ARC also cites the Congressional objective of promoting "diversity of views and information" contained in Section 2(b)(1) of the 1992 Cable Act, and asserts that regional sports programming has promoted both diversity and localism by being an outlet for local and regional sporting events which do not traditionally receive coverage from broadcast or cable.[68] ARC and Liberty Media point out that there is no basis to conclude that local news or sports programming provided by an MSO affiliate would contribute less to the goals of localism and diversity than similar programming provided by a broadcast station owned by a national network or large group owner.[69]

30. *Discussion*. We deny CME's petition to reconsider our exception for local and regional programming. CME's approach overlooks Congress' direction that we consider the benefits as well as the dangers of vertical integration in establishing "reasonable" channel occupancy limits. As we stated in our *Second Report and Order*, the exception for local and regional networks was "an important means of encouraging continued MSO investment in the development of local cable programming, which is responsive to the needs and tastes of local audiences and serves Congress' objectives of promoting localism."[70] CME does not challenge the value of local and regional programming, or our conclusion that given the cost and limited appeal of such programming, an exception may be necessary to encourage continued MSO investment. We continue to believe that consideration of these benefits of vertical integration more accurately reflects Congressional intent, and fully justifies the exception.

31. *75-Channel Cap*. CME asks that the Commission reconsider its decision not

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[66] *Id.*, quoting NATOA Reply Comments, MM Docket No. 92-264, at 10 (March 3, 1993).

[67] ARC Opposition at 4; Time Warner Opposition at note 11; Liberty Media Opposition at 16.

[68] ARC Opposition at 3-4.

[69] ARC Opposition at 7-8; Liberty Media Opposition at 16-17.

[70] *Second Report and Order* at ¶ 78, *citing* Section 2(a)(10) of the 1992 Cable Act.

to apply channel occupancy limits beyond a cable system's first 75 channels.[71] CME asserts that the danger of discrimination against unaffiliated programmers exists no matter how many channels a cable operator offers, and that "expanded channel capacity will simply mean more opportunities for MSO's to offer affiliated programming to the detriment of unaffiliated programming."[72] CME states that without channel occupancy limits, there is "a strong likelihood" that all new capacity beyond 75 channels will be filled with channels affiliated with the cable operator.[73]

32. *Comments*. Liberty Media responds that CME offers no support for its assertion that cable operators would fill any new capacity with affiliate programming, and that such discrimination would, in any case, be prohibited by Section 12 of the 1992 Cable Act.[74] Similarly, Time Warner states that cable operators will not have enough affiliated services to fill the space created by new technologies and will need programming from many other sources.[75] NCTA, Time Warner and Liberty Media argue the 75-channel cut-off is reasonable since it reflects the current maximum capacity of most cable systems,[76] while Liberty Media states that lifting channel occupancy limits after the first 75 channels gives "cable operators an incentive to deploy new technologies and improve service to the public."[77] TCI argues that "[s]ignificantly increased channel capacity will result in greater program diversity and expanded consumer choice because cable operators have the incentive to maximize the use of system capacity by seeking out innovative programming services."[78]

33. On reply, CME argues that "[i]f increased capacity will render the limits superfluous, they are not the slightest disincentive to the MSOs [to expand capacity]. And if they do affect incentive (i.e. prevent MSOs from counting on more than 40 percent of even greatly increased capacity), then the former argument is disingenuous, and the limits will be

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[71] CME Petition at 20.

[72] CME Petition at 20.

[73] *Id.* at 21.

[74] Liberty Media Opposition at 19-20.

[75] Time Warner Opposition at 17-18.

[76] NCTA Opposition at 14; Time Warner Opposition at 17; Liberty Media Opposition at 20.

[77] Liberty Media Opposition at 20.

[78] TCI Opposition at 13.

as necessary as ever."[79]

34. *Discussion*. On reconsideration, we decline CME's invitation to eliminate our 75-channel cap. There is no evidence in the record to support CME's claim that "there is a strong likelihood that all of the newly available channels will be filled by services affiliated with the MSO." Indeed, we note that in our informal survey of 25 TCI and Time Warner cable systems, none of the systems were approaching the current 40% channel occupancy limit for affiliated programming.[80] However, even if there were some basis for CME's prediction, we still believe that the vast expansion of channel capacity may obviate the need for a rigid occupancy limit. As we noted in the *Second Report and Order*, although information on how multichannel video distributors will use the additional capacity "is necessarily somewhat speculative," the record indicates that the capacity will likely be used to deliver targeted "niche" video programming services aimed at correspondingly smaller audience sizes, such as pay-per-view and "multiplexed" channels.[81] Occupancy limits in these circumstances do not parallel occupancy limits for more restricted capacity systems where most services are distributed on discrete channels to a significant portion of a system's subscribership. Accordingly, the occupancy limits can be relaxed.[82]

35. In sum, we continue to believe that the introduction of advanced technologies such as signal compression and fiber optics will reduce the need for structural occupancy limits in order to ensure programming diversity and access for unaffiliated programmers. Nevertheless, as we noted in the *Second Report and Order*, the 75-channel cap will be subject to periodic review and will be eliminated if developments warrant.

36. *Grandfathering of Existing Vertical Relationships*. CME requests that the Commission reconsider its decision to grandfather all vertically integrated programming services carried as of December 4, 1992 (the effective date of the 1992 Cable Act).[83] CME argues that because the Commission does not know how many systems would exceed the

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[79] CME Reply at 9.

[80] *See* Appendix B. TCI smaller systems devoted between 47% and 79% of the channels available within the 40% limit to affiliated programming; TCI larger systems devoted between 41% and 55%. Time Warner smaller systems devoted between 29% and 53% of the channels available within the 40% limit to affiliated programming; Time Warner larger systems devoted between 25% and 43%.

[81] *See Second Report and Order*, ¶¶ 83-84.

[82] Of course, the prohibitions against discriminatory conduct contained in Sections 12 and 19 will remain in full effect regardless of the number of channels added.

[83] CME Petition at 21.

channel occupancy caps, the Commission has "no basis for its claim that application of the limits is outweighed by the need to avoid disruption of consumer service."[84] Moreover, CME asserts that grandfathering existing vertically integrated programmers is contrary to Congress' desire to limit channel capacity "based on the market power that derives from existing levels of vertical integration."[85]

37. *Comments*. Time Warner argues that grandfathering is appropriate, since Congress requires the Commission to prescribe regulations that "take particular account of the market structure, ownership patterns, and other relationships in the cable industry"[86] In addition, Time Warner, TCI and Liberty Media assert that the rule prevents subscriber confusion and unhappiness, and minimizes disruption to carriage and service agreements.[87] Finally, Time Warner and Liberty Media argue that grandfathering does not dilute the purpose of channel occupancy limits because operators must come into compliance as new space becomes available on cable systems.[88]

38. CME replies that the amount of disruption that would ensue without grandfathering merely highlights the size of the problem Congress was trying to address; to the extent such disruption is avoided, Congress' intent in enacting Section 11 is "undermined."[89]

39. *Discussion*. We deny CME's petition to reconsider our decision grandfathering existing vertical relationships. We still believe, as we held in the *Second Report and Order*, that the public interest would be disserved by requiring cable operators to delete vertically integrated programming services to comply with the channel occupancy caps. We continue to believe that grandfathering existing arrangements will limit consumer confusion and the disruption of existing programming relationships, and is, as Time Warner points out, consistent with Congress' direction that our channel occupancy limits "take particular account of the market structure, ownership patterns, and other relationships of the cable television industry."[90]

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[84] *Id.*

[85] *Id.* at 21-22.

[86] Time Warner Opposition at 19; *see also* TCI Opposition at 14-15.

[87] TCI Opposition at 14-15; Time Warner Opposition at 19; Liberty Media Opposition at 21.

[88] Time Warner Opposition at 19; Liberty Media Opposition at 21.

[89] CME Reply at 9.

[90] Communications Act, § 613(f)(2)(C).

40. We also reject CME's contention that our decision to grandfather existing vertical arrangements "has rendered impotent" the intent of Congress to limit excessive vertical integration.[91] First, we reiterate that Congress directed us to establish "reasonable" channel occupancy limits based on a balancing of competing interests; if Congress wished to require the divestiture of existing channels it could have done so. More importantly, our decision did not grandfather non-compliance in perpetuity. Rather, the *Second Report and Order* provided that when a grandfathered cable system adds channel capacity, it cannot add an affiliated programming service until its system is in full compliance with our channel occupancy rules. Thus, the difference is more one of timing than of ultimate objectives. While CME suggests immediate divestiture of existing services to bring systems into compliance, our approach is to grandfather existing services and remedy non-compliance prospectively. We continue to believe that our approach better reflects the various interests at stake, and thus better reflects Congress' intent.

B. Bell Atlantic Petition

41. *Competition.* Bell Atlantic filed a Petition for Limited Reconsideration requesting that the Commission reconsider its decision to apply the channel occupancy limits to cable systems that face actual head-to-head competition. Bell Atlantic states that although Congress was concerned that cable operators might block independent programmers from reaching consumers, this concern is relevant only in the absence of local competition. If such competition does exist, Bell Atlantic argues that independent programmers will have alternate means of delivering their programming, and that competing distributors will have strong incentives to ensure that consumers receive valued programming, regardless of the source.[92]

42. According to Bell Atlantic, the only effect of applying channel occupancy limits to competitive systems will be that particular programs will be banned from delivery and competition and diversity will be reduced. In fact, Bell Atlantic notes that requiring new entrants to maintain a warehouse of unused capacity in the event that someone may later want to use it would impede competitive entry and prevent the development of competition in the first instance.[93] Finally, Bell Atlantic adds that in markets where one of the competitors is a video dialtone system, which is required to provide access to all programmers on a non-discriminatory basis, there is even further assurance that independent programmers will have a means of delivering their programming.[94]

[91] CME Petition at 22.

[92] Bell Atlantic Petition at 3.

[93] *Id.*

[94] *Id.* at 4.

43. *Comments*. Only CME filed an Opposition to Bell Atlantic's Petition. CME states that Bell Atlantic's argument rests on unsupported speculation about the future of the industry, and thus presents no justification as to why the Commission should drop the channel occupancy limits at this time.[95] CME also argues that because Congress specifically stated in the 1992 Cable Act that rate regulation will be lifted where there is effective competition, but did not similarly call for the lifting of ownership limits if competition developed, Congress must have intended ownership limits to apply in both competitive and monopoly markets.[96]

44. CME also disagrees with Bell Atlantic's claim that local competition diminishes the incentive or ability of cable operators to favor affiliated programmers over independent programmers.[97] First, CME points to the legislative history of the 1992 Cable Act which found that large MSOs have disfavored independent programmers through discriminatory pricing, channel positioning and promotion or outright denial of access. CME notes that Bell Atlantic has presented no evidence that local competition will eliminate this discrimination. Second, CME agrees with the point made by MPAA that competitors may themselves be vertically integrated and thus provide no alternative for an independent programmer.[98] CME also does not believe that new entrants will be unable to find sufficient programming to fill their channels; in fact, there is a plethora of new programming. CME states that it is not aware of any existing video dialtone system and that such systems will take years and billions of dollars to become operational, let alone a competitive alternative to cable, and thus cannot justify the removal of ownership restrictions.[99] Finally, CME notes that Congress apparently did not believe that a pay-for-carriage service such as video dialtone would vitiate the need for ownership limits, because it included *both* leased access and ownership limits in the 1992 Act.[100]

45. In its Reply, Bell Atlantic states that the point of its Petition was not that ownership limits should be removed whenever there is some "theoretical" possibility of competition in the future, but that ownership limits should not apply to any competition -- whether a traditional cable system or a common carrier video dialtone system -- "where

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[95] CME Opposition at 2.

[96] *Id.* at 3.

[97] *Id.* at 4.

[98] MPAA Reply Comments to *Notice of Proposed Rulemaking and Notice of Inquiry* at 9.

[99] *Id.* at 5.

[100] *Id.* at 6.

actual head-to-head competition exists."[101] Bell Atlantic also points out that while there are approximately 90 national programming channels, the competitive video distribution networks being developed will have many times this capacity, thus potentially forcing new entrants to leave a large portion of their capacity lie fallow.[102]

46. *Discussion*. On reconsideration, we decline to modify our decision to enforce channel occupancy limits in systems which face actual head-to-head competition. With respect to Bell Atlantic's argument that channel occupancy limits are even less necessary in markets where competition exists and one of the competitors is a video dialtone service, we cannot find, at this time, that video dialtone will completely eliminate the problems caused by vertical integration. Under video dialtone, a telephone company must provide sufficient capacity to serve multiple video programmers, and must expand capacity as demand increases to the extent technically feasible and economically reasonable. At this point, there are only eight commercially licensed video dialtone services in the country. None of these systems is yet operational; until that time, it is unclear whether a video dialtone system will fully address the concerns raised by channel occupancy limits. In addition, the practical effect of several recent court cases is that certain telephone companies may now provide their own programming to subscribers in their service areas.[103] Thus, we do not believe that video dialtone in its current state can provide sufficient justification to reconsider our decision to enforce our channel occupancy limits in systems which face actual head-to-head competition.[104]

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[101] Bell Atlantic Reply at 2.

[102] For example, Bell Atlantic's proposed video dialtone system in New Jersey will be capable of providing a minimum of 384 channels upon completion. *Id.* at 3.

[103] *Chesapeake & Potomac Tel. Co. of Virginia v. United States*, 42 F.3d 181 (4th Cir. 1994); *US West, Inc. v. United States*, No. 94-35775, D.C. No. CV-93-01523-BJR (9th Cir. Dec. 30, 1994); *BellSouth Corp. v. United States*, 868 F. Supp. 1335 (N.D. Ala. Sept. 23, 1994); *Ameritech Corp. v. United States*, 867 F.Supp. 721 (N.D. Ill. 1994); *NYNEX Corp. v. United States*, Civil No. 93-323-P-C (D. Me. Dec. 8, 1994); *GTE South, Inc. v. United States*, C.A. No. 94-1588-A (E.D. Va. Jan. 13, 1994); *United States Tel. Assoc. v. United States*, Civ. No. 1:94CV01961 (D.D.C. Feb. 14, 1995); *Southwestern Bell v. United States*, No. 3:94-CV-0193-D (N.D. Tex. March 27, 1995). In light of these decisions, on January 20, 1995, the Commission issued a *Fourth Further Notice of Proposed Rulemaking* in CC Docket No. 87-266 (FCC 95-20) to consider changes in its video dialtone rules and to consider the extent to which Title II and Title VI of the Communications Act apply to telephone companies providing video programming directly to subscribers in their telephone service areas over video dialtone facilities.

[104] We also note that Bell Atlantic's argument that new multichannel video programming distributors with expanded capacity may be forced to leave channels fallow is irrelevant because our channel occupancy limits do not apply beyond 75 channels.

47. The remaining arguments raised in Bell Atlantic's Petition have already been considered and rejected in our *Second Report and Order*.[105] In the *Second Report and Order*, we concluded that we should not eliminate channel occupancy limits in communities where effective competition exists because we found that the effective competition standard was not adopted for this specific purpose and because it is not clear that the presence of effective competition for any cable system will address all of the relevant concerns that Congress expressed in enacting Section 11 of the 1992 Cable Act.[106] For example, we noted that if a competing multichannel distributor is also vertically integrated, without channel occupancy limits, unaffiliated programming services may continue to be denied access from either outlet, thus frustrating the diversity and competition objectives of the 1992 Act.[107]

48. Finally, we also agree with the point raised by CME that the statutory exemption from regulation for cable systems subject to effective competition is very limited: Congress explicitly stated in the statute that, in systems which faced effective competition, *rate regulation* would not be necessary. Thus, it is reasonable to assume that had Congress intended for *all* cable regulations to be eliminated where systems became subject to actual head-to-head competition, this statutory exemption would have been drafted much more broadly. Nowhere in either the language of Section 11 or its legislative history does it state that the presence of actual head-to-head competition will render the channel occupancy limits unnecessary.

49. We therefore conclude that there is insufficient evidence in the record before us to warrant elimination or modification of our channel occupancy limits in systems that face actual head-to-head competition. However, as we indicated in the *Second Report and Order*, we remain aware that Congress has indicated that a primary objective of the 1992 Act was to rely on the marketplace to the maximum extent possible, and that the legislation was intended to protect consumer interests in the receipt of cable service "where cable television systems are not subject to effective competition."[108] Thus, as competition develops and we gain more experience with the rules, we will further analyze our rules and the industry as a whole to see whether vertical ownership limits should be phased out.

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[105] In the Comments filed in response to our *Further Notice*, operators took essentially the same position as Bell Atlantic and argued for the elimination of the vertical ownership limits in communities where effective competition has been established. MPAA and NATOA opposed eliminating these limits, for basically the same reasons advanced by CME.

[106] 8 FCC Rcd at 8603.

[107] *Id.*

[108] 8 FCC Rcd at 8603.

IV. CONCLUSION

50. For the reasons stated above, we deny CME's and Bell Atlantic's petitions for reconsideration. At the present time, we believe that our channel occupancy rules continue to represent an appropriate balance of the various statutory objectives identified by Congress. We will re-examine these rules in the future, however, should it be warranted by new evidence or a change in the cable marketplace.

V. REGULATORY FLEXIBILITY ANALYSIS

51. Pursuant to Sections 601-602 of the Regulatory Flexibility Act, Pub. L. No. 96-354, 94 Stat. 1164, 5 U.S.C. § 601 *et seq.* (1981), the Commission's final analysis is as follows:

52. *Need and Purpose for Action*: This action is being taken to address petitions for reconsideration of the channel occupancy rules adopted by the Commission to implement Section 11(c) of the 1992 Cable Act.

53. *Summary of Issues Raised by the Public Comments in Response to the Initial Regulatory Flexibility Analysis*: There were no comments received in response to the Initial Regulatory Flexibility Analysis.

54. *Significant Alternatives Considered*: We have analyzed the comments submitted in light of our statutory directives and have, to the extent possible, minimized the regulatory burden on entities covered by the ownership provisions of the 1992 Cable Act.

V. ORDERING CLAUSES

55. Accordingly, IT IS HEREBY ORDERED that pursuant to the authority in Sections 1, 4 and 613 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151, 154, and 533, the petitions for reconsideration filed in this proceeding by the Center for Media Education/Consumer Federation of America and Bell Atlantic Corporation ARE DENIED.

FEDERAL COMMUNICATIONS COMMISSION

William F. Caton

William F. Caton
Acting Secretary

APPENDIX A

MM DOCKET 92-264

Petitions for Reconsideration of *Second Report and Order* in MM Docket No. 92-264, 8 FCC Rcd 8565 (1993)

Bell Atlantic
Center for Media Education/Consumer Federation of America

Comments/Oppositions to Petitions for Reconsideration

Affiliated Regional Communications, Ltd
Center for Media Education/Consumer Federation of America
Liberty Media Corporation
National Cable Television Association
Tele-Communications, Inc.
Time Warner Entertainment Co., L.P.
Turner Broadcasting System, Inc.
Viacom International, Inc.

Replies to Comments/Oppositions to Petitions for Reconsideration

Bell Atlantic
Black Entertainment Television, Inc.
Center for Media Education/Consumer Federation of America
Liberty Media Corporation
National Cable Television Association
Time Warner Entertainment Co., L.P.
Turner Broadcasting System, Inc.