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FCC 95-314

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C.

In re	)	
	)	
Review of the Prime Time	)	MM Docket No. 94-123
Access Rule, Section 73.658(k) of the	)	
Commission's Rules	)	

REPORT AND ORDER

Adopted: July 28, 1995; Released: July 31, 1995

By the Commission: Commissioner Barrett concurring and issuing a statement; Commissioner Chong issuing a statement.

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I. INTRODUCTION

1. The Commission's Prime Time Access Rule ("PTAR") generally prohibits network-affiliated television stations in the top 50 television markets ("Top 50 Market Affiliates") from broadcasting more than three hours of network programs (the "network restriction") or former network programs (the "off-network restriction") during the four prime time viewing hours (*i.e.*, 7 to 11 p.m. Eastern and Pacific times; 6 to 10 p.m. Central and Mountain times).[1] The rule exempts certain types of programming (*e.g.*, runovers of live sporting events, special news, documentary and children's programming, and certain sports and network programming of a special nature) which are not counted toward the three hours of network programming.[2] PTAR was promulgated in 1970 in response to a concern that the three major television networks -- ABC, CBS and NBC -- dominated the program production market, controlled much of the video fare presented to the public, and inhibited the development of competing program sources. The Commission believed that PTAR would increase the level of competition in program production, reduce the networks' control over their affiliates' programming decisions, and thereby increase the diversity of programs available to the public. PTAR also came to be viewed as a means of promoting the growth of independent stations in that they did not have to compete with Top 50 Market Affiliates in acquiring off-network programs to air during the access period.

2. On October 20, 1994, the Commission adopted a *Notice of Proposed Rule Making* ("*Notice*") in this docket to conduct an overall review of the continuing need for PTAR given the profound changes that have occurred in the television industry since 1970.[3] As we stated in the *Notice*, inherent in our regulatory mandate is the continuing responsibility to review our rules and policies to determine whether, in light of prevailing market conditions, such rules and policies continue to serve the public interest. In response to the *Notice*, we received a substantial number of comments from interested parties, including economic and empirical analyses of the effects of repealing or retaining the rule.

3. Based on this record, we conclude that PTAR should be extinguished. The three major networks do not dominate the markets relevant to PTAR. There are large numbers of sellers and buyers of video programming. Entry, even by small businesses, is relatively easy. There are a substantially greater number of broadcast programming outlets today than when PTAR was adopted in 1970 due to the growth in numbers of independent stations. In addition, nonbroadcast media have proliferated. Viewers can choose from program offerings on cable, so-called "wireless" cable, satellite television systems, and VCRs. Under these market conditions, PTAR is no longer needed to promote the development of non-network

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[1] *See* 47 C.F.R. §73.658(k). PTAR's restrictions also extend to stations owned by a national television network in the top 50 markets. *Id.*

[2] 47 C.F.R. § 73.658(k)(1)-(6).

[3] 9 FCC Rcd 6328 (1994).

sources of television programming. We also find, given these market conditions, and the record before us, that the rule is not warranted as a means of promoting the growth of independent stations and new networks, or of safeguarding affiliate autonomy. Indeed, the rule generates costs and inefficiencies that are not now offset by substantial, if any, benefits.

4. We thus find that the public interest warrants the repeal of PTAR. In scheduling repeal of the rule, we believe a one-year transition period is appropriate to provide parties time to adjust their programming strategies and business arrangements prior to the elimination of a regulatory regime that has been in place for 25 years. We consequently will make repeal of PTAR effective August 30, 1996.

II. BACKGROUND

A. The Structure of the Industry

5. We begin by summarizing briefly how the market for the purchase and sale of television programs operates.[4] Television stations obtain programming for delivery to their viewers in a variety of ways. First, stations that affiliate with a television network obtain an entire package or schedule of programming directly from their network. This network "feed" is delivered to affiliated stations via satellite. Affiliated stations then broadcast the network programming to their local audiences. Some of the network feed is comprised of programs produced in-house by the network, such as the nightly national news and some entertainment programming. Much of the network feed, however, consists of programs produced by independent program production companies, with the network acting as a broker between these suppliers and its affiliated stations.

6. Affiliated television stations also program portions of the broadcast day independently of their network. They air locally originated programming, primarily local news, public affairs, and sports programming. They also obtain programming from suppliers called "syndicators," entities that sell programming to television stations, primarily on an individual basis. In contrast to a network feed which supplies a schedule of network programming pursuant to an agreement between the network and a station, a syndicator licenses programs for exhibition on a station-by-station, program-by-program basis.

7. Each of the original three major networks, ABC, CBS, and NBC, has over two hundred affiliates nationwide. (Each of the networks also owns and operates a number of stations throughout the country.) They each reach 99 percent of U.S. television households.[5] The Fox Broadcasting Company has developed as a fourth network, with over 150 affiliated

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[4] A more detailed description of the structure of the television industry and the history of PTAR is set forth in the *Notice*, 9 FCC Rcd at 6330-36.

[5] Viacom Comments at App. B.

stations (as well as a number of its own "owned and operated" stations). (Fox also has over 40 secondary broadcast affiliates throughout the country.[6]) The percentage of U. S. television households capable of receiving Fox network programming is 97 percent as of February 1995.[7]

8. Recently, two new networks have been launched. The United Paramount Network ("UPN"), owned by subsidiaries of Chris-Craft Industries, Inc.,[8] began service on January 16, 1995, with 96 affiliates. UPN had 67 percent coverage through primary affiliates and an additional 16 percent coverage through secondary affiliations for a total coverage of 83 percent.[9] A recent report indicates that UPN has added nine new affiliates -- three primary and six secondary -- to increase their audience reach to 86.5 percent, including coverage by primary affiliates of 73 percent.[10] WB, affiliated with Warner Brothers (which, in turn, is owned by Time Warner), began broadcasting on January 11, 1995, with 47 affiliates and superstation WGN. WB has a national reach of 78 percent, with 18 percent of this reach achieved through cable delivery on WGN.[11] Neither Fox, UPN, nor WB, however, falls within the definition of "network" for purposes of PTAR. None offers more than fifteen hours of prime time programming per week, a prerequisite for a "network" as defined for purposes of the PTAR rules.[12]

9. There are now over 450 local commercial broadcast stations that are not affiliated with the ABC, CBS, or NBC networks. While these stations have traditionally been called "independent" stations, approximately 300 of these commercial stations are now affiliated with and obtain several hours of prime-time programming from the Fox, UPN, or WB networks. Approximately 150 of these stations are affiliated with Fox. Some of these stations have dual affiliations.[13] In addition to airing this network programming, independent stations air some

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[6] By "secondary," we mean that the affiliated station airs only part of the network schedule of programs or delays the broadcast of these programs to a different time period.

[7] Viacom Reply Comments at 29.

[8] Paramount Pictures Corporation, a subsidiary of Viacom, Inc., has provided funding and assistance in the launch of UPN. Paramount also holds a contingent ownership interest in UPN. Viacom Comments at 3 n.4.

[9] Viacom Comments at 9.

[10] *See* Steve Coe, "UPN Affiliates Meet for First Time," *Broadcasting & Cable*, June 26, 1995, at 17.

[11] Comments of Oliver E. Williamson & Glenn A. Woroch at 5 (the "WW Study").

[12] *See* 47 C.F.R. § 73.662(f).

[13] *See* INTV Comments at 23.

locally originated programming. Much of their programming, however, is obtained from program producers or syndicators. These programs include movies previously shown in theaters, television series previously aired on network affiliates (*i.e.*, off-network programs such as reruns of *The Cosby Show*), and series produced for first-run viewing on the independent stations (*e.g.*, *Star Trek: The Next Generation*).

10. PTAR affects the market for programming in several ways. First, it has created an "access period" from 7 to 8 p.m. Eastern and Pacific times (from 6 to 7 p.m. Central and Mountain Times) during which ABC, CBS, and NBC affiliates in the top-50 markets air non-network programming.[14] PTAR thus affects the programming seen by viewers of the Top 50 Market Affiliates, and the affiliates' advertising revenues from air time sold during this programming. Second, PTAR increases the demand for syndicated first-run programming by the Top 50 Market Affiliates, given that they must turn to non-network programming during the access hour. Third, by precluding the Top 50 Market Affiliates from showing off-network programs in the access period, PTAR also effectively reserves a supply of popular off-network programming for purchase by independent stations and affiliates of Fox, UPN, and WB in these markets.

B. The History of PTAR

11. PTAR was originally adopted in 1970, in conjunction with the Commission's financial interest and syndication ("fin/syn") rules.[15] At the time, the networks were viewed

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[14] There are certain exceptions to this rule. *See supra* note 2. As a result of industry practice, broadcasters have generally scheduled the access period for the first hour of prime time, but a number of affiliates in markets affected by the rule broadcast exempt network news programming for half an hour of the access period, effectively reducing the access period to a half hour.

[15] *Report and Order* in Docket No. 12782, 23 FCC 2d 382 (1970) ("*PTAR I*"). As originally adopted, the fin/syn rules imposed broad constraints upon the financing, ownership, and broadcast syndication of television programs by television networks. Like PTAR, these rules were intended to promote diversity of program sources, and the fin/syn limitations imposed on the networks were a response to their perceived insurmountable advantage over independent producers in providing programs to their affiliates. *Id.* at 386. In 1991, the Commission modified the fin/syn rules, *see Report and Order* in MM Docket No. 90-162, 6 FCC Rcd 3094, *modified, Memorandum Opinion and Order*, 7 FCC Rcd 345 (1991), but that decision was overturned and remanded to the FCC on appeal to the United States Court of Appeals for the Seventh Circuit. *See Schurz Communications, Inc. v. FCC*, 982 F.2d 1043 (7th Cir. 1992). In response to the Court's remand, and after further proceedings, the Commission relaxed the fin/syn rules further and scheduled the complete expiration of the rules for November 1995. *See Second Report and Order* in MM Docket No. 90-162, 8 FCC Rcd 3282 (1993) ("*Fin/Syn Second R&O*"), *recon. granted in part, Memorandum Opinion and Order*, 8 FCC Rcd 8270 ("*Fin/Syn MO&O*"). The Court of Appeals affirmed these actions in *Capital Cities/ABC, Inc. v. FCC*, 29 F.3d 309 (7th Cir. 1994). On April 5, 1995, the Commission initiated a scheduled final review of the fin/syn rules. In this review, the burden is on proponents of the rules to

as dominating the television marketplace. The Commission believed that this "modest action [would] provide healthy impetus to the development of independent program sources, with concomitant benefits in an increased supply of programs for independent (and, indeed, affiliated) stations."[16] The Commission also expressed its hope that diversity of program ideas would be encouraged by limiting the networks' ability to influence programming during a portion of prime time. PTAR has also been seen as promoting the growth of independent stations and new networks.[17]

12. PTAR was adopted as a structural mechanism to promote the Commission's diversity goals.[18] The Commission has in the past adopted regulations that directly seek to promote certain types of programming as a means of providing greater viewpoint diversity.[19] PTAR, in contrast, is an indirect effort to promote program diversity by seeking to increase the variety of program sources (*i.e.*, source diversity), and, as some parties argue, program distributors (*i.e.*, outlet diversity).[20] The rule as originally conceived was not designed to

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demonstrate that they should be continued beyond their scheduled expiration date. The Commission has also sought comment on whether, in the event these parties fail to carry their burden of proof, the expiration of the fin/syn rules should be accelerated. *Notice of Proposed Rule Making* in MM Docket No. 95-39, FCC 95-144, released April 5, 1995.

[16] *PTAR I*, 23 FCC 2d at 395.

[17] The Commission denied several petitions for reconsideration that challenged *PTAR I* on the grounds that it violated the First Amendment and exceeded the Commission's authority. *Memorandum Opinion and Order* in Docket No. 12782, 25 FCC 2d 318 (1970), *aff'd*, *Mt. Mansfield Television, Inc. v. FCC*, 442 F.2d 470 (2d Cir. 1971). Shortly thereafter, however, the Commission instituted a new inquiry and rulemaking proceeding, which considered modifying or repealing PTAR. Ultimately, the Commission issued a decision, *Report and Order* in Docket No. 19622, 44 FCC 2d 1081 (1974) ("*PTAR II*"), which retained PTAR in a substantially revised version. *PTAR II* never became effective when disputes over its effective date led to an injunction by the U.S. Court of Appeals for the Second Circuit staying implementation of the rule and urging the Commission to undertake additional analysis. *National Ass'n of Indep. Television Producers and Distrib. v. FCC*, 502 F.2d 249 (2d Cir. 1974). In reviewing PTAR in the wake of the Court's injunction, the Commission decided in 1975 to abandon *PTAR II* and reinstate a slightly revised version of *PTAR I*. *See Second Report and Order* in Docket No. 19622, 50 FCC 2d 829 (1975) ("*PTAR III*"). *PTAR III* was generally upheld on judicial review and the *PTAR III* provisions are essentially the same as the rule in effect today.

[18] *Further Notice of Proposed Rule Making* in MM Docket No. 91-221 and MM Docket No. 87-8 ("*TV Ownership Notice*"), 10 FCC Rcd 3524, 3546-50 (1995) (describing FCC diversity goals); *Fin/Syn Second R&O*, 8 FCC Rcd at 3302 (same).

[19] For example, in 1949 the Commission adopted its *Report on Editorializing by Broadcast Licensees*, 13 FCC 1246, 1247, which, among other things, stressed the duty of all licensees to devote a "reasonable amount of time" to the discussion of public issues.

[20] *TV Ownership Notice*, 10 FCC Rcd at 3549-50.

promote a certain kind of speech, but to increase the variety of non-network speakers.[21] The Commission subsequently carved out exceptions to the rule so that the rule would not prevent the broadcast during the access period of certain types of programming that served the public interest, *e.g.*, children's programming and news and public affairs programming.[22]

13. PTAR has been subject to criticism over the years. Several observers have faulted the rule for not achieving its goal of improving the television industry's economic structure and performance.[23] In fact, they maintain that it has had the unintended effect of lowering the quality and diversity of access-period programming.[24] The Commission itself was prompted to reexamine the need for the rule shortly after it was initially adopted.[25] It ultimately retained the rule in a 1975 decision, rejecting a number of arguments for repeal by stating that it was "persuaded that the rule has not yet been fully tested."[26] A number of Commissioners nonetheless expressed reservations about continuing the rule.[27] In 1980, the Commission's Network Inquiry Special Staff concluded that PTAR should be repealed because, among other

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[21] *PTAR III*, 50 FCC 2d at 847 ("[T]he rule was designed to lessen the tendency of licensees which led them to carry network or off-network programming, in order that the voices of other persons might be heard.").

[22] *See supra* note 2. *See also PTAR III*, 50 FCC 2d at 848 (certain types "of programming important to the public -- those included in the exemptions [to the rule] -- have been somewhat reduced in amount, or, in the case of children's programming, have not been available at the most appropriate time. Therefore, since it was the Commission's rule which has had this effect, we have an affirmative duty to relax our restraint to permit such programming to be made more readily available.").

[23] *See* Thomas G. Krattenmaker & Lucas A. Powe, Jr., *Regulating Broadcast Programming* 72-74 (1994); Krattenmaker, "The Prime Time Access Rule: Six Commandments for Inept Regulation," 7 Comm/Ent L.J. 19 (1984).

[24] Krattenmaker & Powe, *Regulating Broadcast Programming* at 73.

[25] *See supra* note 17.

[26] *PTAR III*, 50 FCC 2d at 837.

[27] *See, e.g., id.* at 888-89 (concurring statement of Commissioner Reid) ("[I] am still not convinced that the rule really is in the public interest. To that end, I would expect that we will gain some definitive factual material from the continuance of PTAR and we will simply have to 'wait and see.'"); *id.* at 890 (dissenting statement of Commissioner Robinson) ("Even television critics who would ordinarily not count themselves as network fans grumbled at the program product that followed in the wake of the [adoption of PTAR]. They still do; plainly the rule has not caused the 'wasteland' to breed lilacs.").

things, it did not appear to further any Commission policy to regulate in the public interest.[28] The Commission did not, however, act on the staff's recommendation, and PTAR remains in force today.

C. The *Notice* and the Positions of the Parties

14. Prompted by the criticism of the rule, and the dramatic changes in the television marketplace since the adoption of PTAR, several parties filed petitions with the Commission challenging the rule in whole or in part.[29] In April 1994, the Commission solicited and received public comment on these filings. On October, 25, 1994, we issued the *Notice* to establish a more complete record, calling specifically for economic and empirical analysis of the continuing need, if any, for PTAR.

15. In response to the *Notice*, ABC, CBS, and NBC filed comments arguing that PTAR should be repealed in its entirety.[30] An economic study of the rule prepared by Economists, Inc., on behalf of the networks was submitted in support of this position (the "EI Study"). According to these parties, the networks do not dominate video distribution or programming and do not have the leverage to dictate programming choices to their affiliates. Nor do they believe PTAR is necessary to foster the growth of independent programming or independent stations. In fact, they argue that PTAR distorts the programming market and has resulted in less diverse programming. According to these parties, PTAR deprives the networks and their affiliates from taking advantage of the efficiencies of network programming and has resulted in a loss of consumer welfare. A number of parties also maintain that PTAR is an unconstitutional abridgment of the First Amendment rights of the networks and their affiliates.[31]

16. Representatives of the first-run syndication industry, independent television stations, and a number of public interest groups favor retention of the rule.[32] They argue that

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[28] Network Inquiry Special Staff, *New Television Networks: Entry, Jurisdiction, Ownership and Regulation* Vol. I at 510-13 (1980) ("*Network Inquiry Study*"). *See Notice*, 9 FCC Rcd at 6336 (describing study).

[29] *Notice*, 9 FCC Rcd at 6329-30 (listing petitions).

[30] Fox filed reply comments supporting this position. The Bureau of Economics of the Federal Trade Commission filed comments questioning the economic rationale for PTAR.

[31] *See* Comments of ABC; First Media Television, L.P.; Freedom of Expression Foundation; Freedom Forum; and The Media Institute.

[32] *See* Comments of the Association of Independent Television Stations, Inc. ("INTV"); Friends of Prime Time Access; King World Productions, Inc.; Media Access Project/People for the American Way ("MAP/PAW"); UPN Affiliates Association; and Viacom, Inc. The Chief Counsel for Advocacy

it is constitutional. They fear that elimination or modification of PTAR will result in the re-emergence of the three network "funnel" for programming that the rule sought to eliminate. They claim that elimination or relaxation of PTAR will undermine affiliate autonomy. According to these parties, repeal would also cause significant harm to independent program producers and to independent stations. They also assert that repeal of PTAR will undermine the development of UPN and WB as new networks. On behalf of INTV, King World, and Viacom, The Law and Economics Consulting Group filed an economic study (the "LECG Study") to support retention of the rule.

17. Another set of parties -- the Coalition to Enhance Diversity (the "Coalition"), the Network Affiliated Stations Alliance ("NASA"), and Westinghouse Broadcasting Company -- argue that the off-network provision of PTAR should be repealed while the restriction on the number of hours of network programming (including first-run syndication by the networks) should be retained.[33] According to these parties, the off-network provision unnecessarily limits the programming choices of the Top 50 Market Affiliates and discourages investment in network programming. The network restriction should be retained, however, because they believe that networks continue to have the power to dictate affiliate programming. An economic study prepared by Oliver Williamson and Glenn Woroch (the "WW Study") on behalf of the Coalition was filed in support of this position. The Motion Picture Association of America ("MPAA") filed comments arguing that the network restriction should be retained without addressing the off-network provision of PTAR. MPAA filed comments on behalf of Buena Vista Pictures Distribution, Metro-Goldwyn-Mayer, Paramount Pictures, Sony Pictures Entertainment, Universal City Studios, and Warner Brothers.[34]

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of the Small Business Administration ("SBA Chief Counsel") also filed comments supporting retention of PTAR.

[33] The Coalition is made up of a group of producers (including, *inter alia,* The Walt Disney Company and MCA Inc.), network affiliates (Burnham Broadcast Company, Hubbard Broadcasting, KVOA Communications, Providence Journal Company, Pulitzer Broadcasting Co., and Scripps Howard Broadcasting Co.), and trade unions (the Screen Actors Guild and the Writers Guild of America, east and west). Coalition Comments, Exh. A.

[34] MPAA Comments at 1 n.2. On July 20, 1995, the National Telecommunications and Information Administration ("NTIA") submitted an *ex parte* filing in this proceeding that urged the Commission to conclude tentatively that PTAR should be repealed, but to delay the effective date of repeal for five years to monitor further industry and regulatory developments. NTIA attached to its filing a report of its staff concerning PTAR's impact on viewer welfare. In a letter dated July 21, 1995, the Coalition objected to NTIA's submission because it was filed one day before the beginning of the Sunshine Agenda period, thus precluding private parties from filing a response to it. *See* Letter of Diane S. Killory, Counsel for the Coalition, July 21, 1995. *See also* 47 C.F.R. § 1.1203. However, the arguments and evidence presented in NTIA's submission have been submitted by other parties in earlier filed comments in this proceeding which we address herein. Since we have not specifically relied on NTIA's filing in this proceeding, the Coalition's concern is mooted.

III. THE FRAMEWORK FOR ASSESSING THE CONTINUING NEED FOR PTAR

18. The task before us is "to assess the extent to which [PTAR] serves the Commission's 'public interest' mandate to maximize consumer welfare, as opposed to merely protecting individual competitors in the communications industry."[35] In assessing the continued efficacy of the rule, we need to examine whether under today's market conditions it is necessary to promote our competition and diversity goals. On the basis of the extensive record before us, we will evaluate the factual and economic assumptions underlying PTAR as well as the costs the rule may impose. As stated in the *Notice*, "the ultimate decision to retain, modify or eliminate the rule will turn on a weighing of its costs against its benefits."[36]

19. Specifically, we assess the continuing need for PTAR as follows: *First*, we will evaluate whether the networks dominate the markets relevant to the rule, or would be likely to dominate them in the absence of PTAR. *Second*, we assess the costs imposed by the rule. *Third*, taking into account our findings regarding whether the networks dominate and the costs of the rule, we analyze whether the rule is necessary as a means of pursuing the benefits of fostering independent programming, promoting the growth of independent stations and new networks, and safeguarding affiliate autonomy. In particular, we assess whether PTAR provides public interest benefits by altering competitive opportunities in the following three ways:

- *First*, by carving out a portion of prime time to be used for non-network use, the rule made it easier for independent producers to sell their programming to Top 50 Market Affiliates.

- *Second*, the rule provided independent stations with more programming choices than affiliates in an effort to foster their growth and that of new networks.

- *Third*, the rule reduced the networks' role in dictating their affiliates' prime-time programming choices by forbidding Top 50 Market Affiliates from broadcasting more than three hours of

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[35] *Notice*, 9 FCC Rcd at 6348. *See also Second Fin/Syn R&O*, 8 FCC Rcd at 3302 ("Altering the distribution of profits among private parties is not, and never has been, a proper or desirable function of the Commission."); *Memorandum Opinion and Order* in MM Docket No. 87-24, 4 FCC Rcd 2711, 2723 (1989) (stating that the Commission's "goal is, of course, to see that the *public* interest is served, not to maintain an inefficient distribution scheme that favors [certain competitors]") (emphasis in original).

[36] *Notice*, 9 FCC Rcd at 6348.

network or off-network programming during prime time.[37]

20. Examining the evidence taken from the record before us, we conclude that repeal of PTAR will not jeopardize the competition and diversity goals that prompted the Commission to adopt the rule in 1970. The networks and their affiliates do not dominate video programming distribution or the video programming production market and are unlikely to do so without PTAR. The record also indicates that PTAR is no longer warranted as a means of providing independent stations a competitive advantage. Moreover, repeal of the rule will not threaten the station base or jeopardize the further development of the new networks, WB and UPN. Finally, the record does not support the argument that affiliates need the rule to reduce the networks' asserted ability to control affiliate programming choices.

21. This conclusion is consistent with our 1993 decision to repeal the fin/syn rules, which was upheld on appeal by the U.S. Court of Appeals for the Seventh Circuit.[38] We determined that repeal of the fin/syn rules was warranted given the increased competition facing the networks and the conditions in the television programming marketplace. These conditions included the decline in network audience share since the fin/syn rules were adopted, the increasing demand for television programming created by the emergence of the Fox network and cable networks and the growth of independent television stations, the intense competition among the three established networks for programming, and the increasing ability of first-run distribution to be a fully comparable alternative to network distribution for program producers.[39] Based upon these findings we eliminated a number of the fin/syn rules immediately and set a timetable for repeal of the remainder.[40]

22. Our review of PTAR raises many of the same diversity and competition issues

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[37] *Notice*, 9 FCC Rcd at 6347-48. Both INTV and LECG claim that this analytical framework fails to take into account the fact that broadcast programming is a public good. INTV Comments at 38-39; LECG Study at 7-8. They never explain, however, what relevance this has to PTAR. Broadcast programming has indeed been described as a public good in that consumption (viewing) by one person does not reduce the program viewing available to another viewer. *See* Krattenmaker & Powe, *Regulating Broadcast Programming* at 40-41. But all broadcast video programming (including affiliate and independent programming) is a public good, making this concept irrelevant to our review of PTAR.

[38] *See supra* note 15. Our 1993 *Fin/Syn Second R&O*, 8 FCC Rcd 3282, followed an earlier ruling of the Court of Appeals which vacated our 1991 fin/syn decision. The Court of Appeals found that this 1991 decision, which modified but retained the fin/syn regime, was arbitrary and capricious. *Id.*

[39] *Notice of Proposed Rule Making* in MM Docket No. 95-39, FCC 95-144 at ¶ 4 n.7, released April 5, 1995; *Fin/Syn Second R&O*, 8 FCC Rcd at 3303-10.

[40] Under this timetable, the remaining fin/syn rules are set to expire on November 10, 1995. The Commission initiated its scheduled final review of the rules in April 1995. *See supra* note 15.

that led us to repeal the fin/syn rules. As with the fin/syn rules, we conclude that PTAR is no longer warranted. We describe the basis for this conclusion in the following sections using the analytical framework outlined above and in the *Notice*.

IV. THE NETWORKS AND THEIR AFFILIATES DO NOT DOMINATE MARKETS RELEVANT TO PTAR

23. The Commission's adoption of PTAR in 1970 was premised on a view that the three networks dominated television programming. The parties debate whether this remains true today. Proponents of the rule argue that the networks still dominate. Advocates of repeal argue that the networks do not dominate programming.[41] Our analysis of the record leads us to conclude that neither the networks nor their affiliates dominate video programming distribution or the video programming production market.

24. A business can dominate a market, *i.e.*, exercise undue market power,[42] by acting alone or together with other businesses.[43] An entity with a large enough market share, *e.g.*, 90 percent or more, may be in a position to exercise undue market power acting alone.[44]

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[41] *Compare* Comments of Viacom at 29-30 (describing view that networks no longer dominate prime time as a "myth") *and* Comments of INTV at 27 ("[T]he networks continue to dominate prime time programming.") *and* LECG Study at 11-20 (arguing that market share analysis reveals that the networks continue to dominate prime time) *with* Comments of NBC at 7-12 (maintaining that networks do not dominate any relevant market) *and* EI Study at 5-28 (analyzing production, distribution, and advertising markets and concluding that the networks, neither singly nor jointly, dominate today).

[42] We note that the court in *Schurz Communications*, 982 F.2d at 1052, in reviewing the Commission's *Report and Order* in MM Docket No. 90-162, 6 FCC Rcd 3094 (1991), observed that "[m]arket power is a matter of degree. Some firms have a lot of it, some a little, some none." We here define market power consistent with our discussion of market power in our fin/syn decision. *See Fin/Syn Second R&O*, 8 FCC Rcd at 3302-08. There, we assessed whether the degree of influence of the networks was sufficient to justify our fin/syn regulations. In referring to undue market power in this proceeding, we mean the exercise of market power, *i.e.*, undue market power, that imposes sufficiently large costs on society to justify regulatory or antitrust action to ameliorate those costs.

[43] Acting together is sometimes referred to as collusion or coordination. Collusion or coordination can be explicit, *e.g.*, meetings of business executives to strike bargains face-to-face, or implicit, *e.g.*, a firm, without explicitly communicating with other firms, increases its price in line with a price increase above the competitive level announced by the market leader.

[44] There is no hard and fast rule about the threshold market share for a single firm below which one can rule out the possibility that the company may be able to exercise market power. *See United States v. Aluminum Co. of America*, 148 F. 2d 416, 424 (2d Cir. 1945) (A 90 percent market share "is enough to constitute a monopoly; it is doubtful whether sixty or sixty-four percent would be enough; and certainly thirty-three percent is not.") (Hand, J.). Even a firm with a very large market share

Alternatively, an entity may be able to exercise undue market power with other businesses if together their market shares form a large part of the market, *i.e.*, the market is concentrated, and other factors such as barriers to entry are present.[45] When a firm or group of firms dominate a market, the market will not operate efficiently.[46] Regardless of whether the firms dominate as buyers or sellers of the product, the quantity of the product produced will be less than that which would be produced by a competitive market.

25. We will assess whether the three networks or their affiliates have undue market power in video programming distribution and the relevant video programming production and national television advertising markets by employing a two-step market power analysis:

> (1) Defining the Relevant Market -- First, we must identify both the product and geographic markets relevant to the operation of the rule. The relevant product market can be defined by determining the willingness and ability of consumers to switch from a product directly affected by the rule to another in response to a price increase, with all other product attributes (such as quality) being equal. To the extent consumers will

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cannot automatically be presumed to have market power; more research would be needed regarding whether there are competitive factors such as ease of entry, excess capacity held by competitors, etc., that would defeat any attempt by the firm to exercise market power despite its very large market share. *See* U.S. Department of Justice and Federal Trade Commission, *1992 Horizontal Merger Guidelines* at 28-32 ("1992 DOJ/FTC Merger Guidelines") (*reprinted in* 4 Trade Reg. Rep. (CCH) ¶ 13,104); *United States v. Baker Hughes, Inc.*, 908 F.2d 981, 986 (D.C. Cir. 1990); *United States v. Syufy Enter.*, 903 F.2d 659, 664-67 (9th Cir. 1990); *Ball Memorial Hosp., Inc. v. Mutual Hosp. Ins., Inc.*, 784 F.2d 1325, 1335-36 (7th Cir. 1986); *see generally* William M. Landes & Richard A. Posner, *Market Power in Antitrust Cases*, 94 Harv. L. Rev. 937 (1981).

[45] All else being equal, a rise in market concentration will facilitate the exercise of market power. Market power is easier to exercise when there are few firms involved in explicit or tacit agreement to collude. The fewer the firms, the lower are the transaction costs of securing initial agreement and the lower are the costs of policing the agreement to spot cheaters, *i.e.*, firms that do not abide by the terms of the collusive agreement. *See* Landes & Posner, 94 Harv. L. Rev. at 946-52.

[46] A market economy relies on competition among rival suppliers and buyers to produce goods and services efficiently. By efficient, we mean that the market produces the quantity and quality of goods and services that society desires and prices the goods and services at the costs to society of producing them. Efficiency is lost however when a firm or group of firms "dominate" a market, *i.e.*, exercise market power. When a *seller* has market power, consumers have to pay more for and receive less of its product, because they have insufficient numbers of alternative sellers offering the product on comparable terms or insufficient quantities of alternatives available within a reasonable amount of time. A *buyer* with market power can lead to similar misallocation of resources by reducing the price being paid for a product to a level below the competitive price, thereby depressing output.

switch between products based on such a price increase,[47] the products are deemed substitutable, *i.e.*, "reasonably interchangeable by consumers for the same purposes,"[48] and hence make up the product market. The relevant geographic market refers to the alternative and economic sources of supply to which buyers of these substitutable products can turn in the event of such a price increase.[49]

(2) Examining Evidence of Undue Market Power -- Second, we estimate and analyze the market's structure and its concentration, as an indication of the absence of undue market power. By market concentration, we refer to the extent to which one or more large firms may have significant shares of the relevant market. If the market is unconcentrated, we presume that the exercise of undue market power is not possible. If the market is concentrated, other market conditions, including barriers to entry, must be examined to determine if one or more firms can exercise undue market power.

We have used this two-step market power analysis in reporting on the status of cable competition,[50] in reconsidering the radio ownership rules,[51] and more recently in seeking comment on revising our broadcast television ownership rules.[52] A similar framework is also used in antitrust analysis.[53]

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[47] The 1992 DOJ/FTC Merger Guidelines, at 10-14, call for the use of a small but significant and nontransitory increase of price to test for substitutability.

[48] *United States v. E.I. du Pont de Nemours & Co.*, 351 U.S. 377, 395 (1956).

[49] *Tampa Elec. Co. v. Nashville Coal Co.*, 365 U.S. 320, 330-33 (1961).

[50] *Cable Competition Report*, 75 RR2d 1415, 1425-26 (1994); *Report* in MM Docket No. 89-600, 5 FCC Rcd 4962, 4994 (1990).

[51] *Second Memorandum Opinion and Order* in MM Docket No. 91-140, 9 FCC Rcd 7183, 7184-87 (1994).

[52] *See TV Ownership Notice*, 10 FCC Rcd at 3534 n.37.

[53] *See, e.g.*, 1992 DOJ/FTC Merger Guidelines.

A. Video Programming Distribution[54]

26. PTAR applies to ABC, CBS, and NBC affiliates in the Top 50 PTAR Markets. These networks and their affiliates display or "distribute" television programming to viewers and sell air time to customers seeking to advertise. In program distribution, networks and their affiliates compete with programs broadcast by independent stations. The list of economic substitutes for network broadcasts may also include cable programs, programs over satellite television systems, videocassette rentals, and other alternatives. For purposes of our review of PTAR, we will focus on program distribution comprising only broadcast television station operators and their networks. This is a conservative, perhaps overly narrow, approach given that a good case can be made that, from the viewers' perspectives, cable system operators *inter alia* are economically relevant alternative distributors of video programming.[55] Since PTAR constrains the market activities of affiliates of the three major networks in the Top 50 PTAR Markets, our primary focus in this section is whether these network affiliates would be able to exercise undue market power in the delivery of video programming in their respective local markets.

27. Even with this narrow description of video programming distribution that is limited to the video programming offered by local broadcast stations, there are substantially more distribution outlets today than in 1970. The total number of commercial and non-commercial television stations has increased 78 percent, from 862 stations in 1970 to 1,532 stations as of January 1, 1995.[56] The number of commercial independent stations (which rely mostly on syndicated programming, including for their prime-time schedules) has grown by almost 450 percent, from 82 in 1970, to over 450 in February 1994.[57] Moreover, in 1970, the Top 50 PTAR Markets had 70 independent stations, or, on average, 1.4 per market. In 1994,

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[54] Since broadcast television is perceived as "free" to viewers, it might seem inappropriate to suggest that broadcast television networks or stations might be able to exercise market power by "raising" prices or "restricting" output. However, an examination of audience shares and measures of concentration generally are taken as an indicator of possible market power in other markets. *See, e.g.*, LECG Study at 11-25. LECG uses network prime-time audience shares as an indicator of possible network market power in a prime-time advertising market. *See also* Bruce M. Owen and Steven S. Wildman, *Video Economics* 196-199 (Harvard Univ. Press 1992); EI Study at 18-20; *Fin/Syn MO&O*, 8 FCC Rcd at 8289 (rejecting the notion that the networks's declining audience share is irrelevant to the networks' power in the program acquisition market).

[55] *See TV Ownership Notice*, 10 FCC Rcd at 3538 (tentatively defining delivered video programming market to include broadcast stations and cable operators).

[56] Television & Cable Factbook, Stations Volume 63, 1995, page iv.

[57] *See Notice*, 9 FCC Rcd at 6337 n. 21 (citing the INTV Census, February 24, 1994). The number of independent stations in 1994 in that Census includes independent stations affiliated with Fox.

the Top 50 PTAR Markets had 278 independent stations, or, on average, 5.6 per market.[58] In short, in 1970, television viewers in the Top 50 PTAR Markets had access, on average, to 4.4 commercial VHF and UHF stations. By 1994, that number had more than doubled to 8.9. (Including noncommercial stations, the per market average again more than doubled from 5.7 to 11.6.[59]) Hence, even without considering other potentially competitive media outlets, the number of competing stations in the markets subject to PTAR has increased very substantially.

28. The recent increases in the number of broadcast stations now provide more program outlets and a larger station base to support the development of new networks. In 1970 there were three national television networks. Today, Fox has developed as a fourth network. Two incipient networks -- UPN and WB -- were launched earlier this year.[60]

29. It is thus clear that, in the Top 50 PTAR Markets, the three original networks and their affiliates face more competition for viewers than they did in 1970 or even in 1980. The effects of this competition are readily apparent in examining the networks' audience shares over the years. Looking at prime time alone, the time period when the networks' viewing shares are the highest, each network's average share of the prime time audience declined from a 31.1 viewing share during the 1971/72 season to a 20.2 share during the 1993/94 season, a loss of almost one-third of each network's audience.[61] ABC, CBS, NBC, and Fox had individual 1993/94 prime-time audience shares of 20.1, 22.7, 17.8 and 11.4 percent, respectively.[62] The Commission's calculation of affiliate audience shares in each of the Top 50 PTAR Markets is consistent with network audience shares nationally. No single network or network affiliate would seem to have the ability to dominate video programming distribution in any of these local markets.[63]

30. Nor is it likely that affiliates in a local Top 50 PTAR Market would dominate as

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[58] *See* 1971 Broadcasting Yearbook; *Investing in Television: 1995 Market Report* (BIA, 1st Ed.). Totals are from Commission calculations based on these sources. Note that the Top 50 PTAR Markets are ranked by the number of prime time television households in the market rather than being ranked by total television households in the market.

[59] The totals and per market averages are Commission calculations based on the 1971 Broadcasting Yearbook and *Investing in Television: 1995 Market Report.*

[60] *See supra* pp. 3-4.

[61] Comments of NBC at 10-11; EI Study at 18-19.

[62] *See* EI Study, Appendix A, Table A-1 at 66.

[63] *See supra* note 44.

a group since video programming distribution is only moderately concentrated.[64] In its 1993 decision setting a timetable for repeal of the fin/syn rules, the Commission stated that "inter-network competition for programming is 'intense.'"[65] Nothing in the record before us calls this conclusion into doubt, as the networks continue to wage a ratings war that has only been heightened with the emergence of the Fox network.[66]

31. We thus conclude that, even focussing narrowly on local broadcast video programming distribution, the three networks and their affiliates cannot singly or jointly dominate video program distribution in the Top 50 PTAR Markets. This is a strong conclusion because the inclusion of additional television alternatives such as cable, satellite systems, video dialtone, etc. would serve to make domination by the networks and their affiliates even less likely.

B. The Video Programming Production Market

32. We begin to define the relevant video programming production market by focussing on the products produced by beneficiaries of PTAR. Entertainment series, news magazine shows, and game shows are examples of the programs sold by independent producers and syndicators of prime-time programs to network affiliates and independents.

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[64] Economists use a measure known as the Herfindahl-Hirschman Index ("HHI") to measure market concentration. In simple terms, the HHI is the sum of the squared market shares of each company in the market. For example, if a market has four equal-sized companies, then each company's market share is 25 percent; the HHI would be: $25^2 + 25^2 + 25^2 + 25^2 = 2500$. The U.S. Department of Justice ("DOJ") and the Federal Trade Commission ("FTC"), based upon extensive study of different industries, generally regard a market with an HHI below 1000 as "unconcentrated," a market between 1000-1800 as "moderately concentrated," and a market above 1800 as "highly concentrated." *See* the 1992 DOJ/FTC Merger Guidelines at § 1.51. In the last instance, more research into ease of entry and other competitive factors is required before concluding that one or more businesses will be able to exercise market power.

Using the prime time audience shares set forth in the EI Study (Appendix A, Table A-1 at 66), the HHI for national prime-time broadcast television program distribution is 1366. This level of concentration has been dropping steadily since 1980. Calculations based on Table A-1 of the EI Study show that concentration first dropped below 1800 in 1987/88, the second year of Fox's existence.

We have also reviewed HHIs for each of the Top 50 PTAR Markets based on prime time and all-daypart ratings reported in *Investing in Television: 1995 Market Report*. These HHIs also indicate that video programming distribution in the Top 50 PTAR Markets is only moderately concentrated. *See* Appendix D for a full listing of the HHIs for each market.

[65] *Fin/Syn Second R&O*, 8 FCC Rcd at 3307.

[66] *See* EI Study at 6-7 (describing competition between the networks). During the 1994-95 season, Fox in fact drew more viewers than CBS among adults aged 18-34 and 18-49. ABC Comments at 6.

The list can be extended to include movies (whether for television, theatrical presentation, or cassette rental), sports programs, talk shows, news programming (local and national), musical variety, dramas, arts presentations, etc. Suppliers of these programs include not only those suppliers that actually are employed in a given year to produce programming for network prime time but also those producers willing and able to produce such programming in the event that market price increased above the competitive level. The list of suppliers will include television networks, independent syndicators, Hollywood movie studios, and international video producers. Buyers of such programming are not limited to television broadcasters but will include other purchasers of video programming such as cable networks and operators,[67] direct broadcast satellite operators, videocassette distributers and, most recently, video programming affiliates of local telephone companies, which propose to offer video dialtone service.[68] This market is "clearly national and perhaps international in scope, because television broadcasters obtain a large portion of their programs from national providers."[69]

33. In looking for evidence of undue market power in the video programming production market, we first consider the demand side. Given the lack of concentration in video programming distribution, it should not be surprising to find that the demand side of the video programming production market shows no evidence that any single buyer or group of buyers exercises undue market power. Indeed, this is what we found in our fin/syn proceeding two years ago:

> We believe that the . . . evidence of purchasing patterns by Fox, cable networks, independent stations, and the three original broadcast networks themselves, demonstrates that the video marketplace has become more competitive with respect to the demand for programming. Moreover, as the number of program distributors, broadcast stations and cable services increases, the demand for programming will continue to grow, thereby providing producers with additional alternative buyers for their programming. Non-

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[67] We did not include cable networks in our narrow examination of broadcast program distribution. However, as we noted, a case can be made for such inclusion. In examining market power on the demand side of the video programming production market, we used a broad market definition, as we did in our fin/syn decision. *See Fin/Syn Second R&O*, 8 FCC Rcd at 3303-04. Our list of buyers includes cable networks and operators since various cable channels are devoted to showing exactly the same fare shown on network prime time, *e.g.*, situation comedies, movies, etc.

[68] *See Notice of Inquiry* in CS Docket No. 95-61, FCC 95-186, released May 24, 1995, at ¶¶ 47-55 (describing local exchange carrier entry into video programming market); *First Report* in CS Docket No. 94-48, 75 RR 2d 1415, 1439-43 (1994) (same). For a discussion of telephone company efforts to purchase video programming, *see* Mike Mills, "In Hollywood, Bells are Ringing," *Washington Post*, Nov. 1, 1994, at D1.

[69] *TV Ownership Notice*, 10 FCC Rcd at 3545.

> network program distributors already are beginning to purchase the quality programming previously sold only to the national networks. In this respect, we find that the market power of the networks *vis-a-vis* other purchasers of programming is limited. Moreover, inter-network competition serves as an additional constraint on any one network's ability to dictate terms in its overall dealings with the production community. Thus, we believe that a program producer that is not satisfied with the arrangement offered by a network has alternative purchasers for the product, and that the current market of alternative purchasers is sufficient to limit network market power over entertainment program acquisitions.[70]

34. There is no evidence that since we issued our fin/syn decision market conditions have changed such that the networks exercise monopsony or oligopsony power in the video programming production market, *i.e.*, that one (monopsony) or several firms (oligopsony) artificially restrict the consumption of programming and depress the market price paid for programming.[71] Aside from the growth in the broadcast industry described above, there are nearly 150 national and regional cable networks,[72] most of which transmit original, non-network programming. Also, other nonbroadcast video program distributors -- such as cable, wireless cable, and satellite services -- have grown.[73] Finally, first-run syndicators are quite active as buyers (and sellers).[74] According to the EI Study, in 1994 the video entertainment programming purchased by each of the three networks accounted for approximately 9.4 percent of aggregate expenditures on video programming in the United States, after taking into account distribution fees associated with syndicated programming and home videos.[75] These market shares indicate that demand for video programming is not concentrated, and that the networks clearly cannot be said to exercise market power in the video programming

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[70] *Fin/Syn Second R&O*, 8 FCC Rcd at 3308.

[71] The Commission, in its *Fin/Syn MO&O*, 8 FCC Rcd at 8286-89, employed a broad measure of the demand side of the video programming production market and rejected the notion the three networks could exercise market power here.

[72] *See* Comments of NBC at 10.

[73] *See Notice of Inquiry* in CS Docket No. 95-61, FCC 95-186, released May 24, 1995 (discussing status of cable industry, wireless cable, satellite master antenna systems, direct-to-home satellite services, video dialtone); *First Report* in CS Docket No. 94-48, 75 RR 2d 1415 (1994) (same).

[74] In 1994, there were 259 different programs in broadcast syndication, 75 percent of which were first-run. Comments of NBC at 10; EI Study at 17-18.

[75] EI Study at 25.

production market, either individually or together.[76]

35. The supply side of the video programming production market is no more concentrated than the demand side. The Staff of the Bureau of Economics of the Federal Trade Commission ("FTC Staff") presents data showing the market shares of leading network suppliers for the prime time of Fall, 1994, 1977, and 1970, respectively.[77] In each year, they listed twenty suppliers. No single supplier in any of those years had a market share of as much as 20 percent. The markets were essentially unconcentrated.[78] None of the suppliers, either acting alone or together, could exercise undue market power. Data provided by the EI Study and the LECG Study essentially confirm this conclusion.[79] Moreover, comments filed

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[76] The Commission calculated HHIs to measure concentration among market buyers in the video programming production market. We relied upon data in the EI Study, Appendix G, Table G-2. Each network's market share of 9.4 percent contributes 88 points to the market's HHI. The three network's shares together contribute 265 points. Fox's share of 5.6 percent contributes 31 points. It is unlikely that any single market share held by a basic cable network, pay cable network, syndicator, or home video distributor would be as large as one of the four networks. No shares for these buyers are reported in Table G-2. Our hypothesis is that the market shares of the remaining buyers are each quite small and therefore are unlikely to increase the market's HHI very much at all. Under these assumptions, the HHI for this market is at least 296 and probably no more than 500, depending on the size of the market shares of non-network buyers. The HHI is almost certainly less than 1000, *i.e.*, the market is unconcentrated by the standards of the 1992 DOJ/FTC Merger Guidelines.

[77] *See* Comments of FTC Staff at 15-17, Tables 3-5.

[78] The HHIs reported by the FTC Staff ranged from 430 to 1063.

[79] The EI Study at Appendix A, Table A-11, shows that ABC, CBS, and NBC together have not produced in any given year more than 8 percent of the hours aired as prime-time entertainment series during the period from 1969/70 through 1993/94. Until the 1990s, they had not aired more than 3 percent. In Appendix E, the EI Study lists the names of suppliers (or packagers) of prime-time entertainment series to the three networks for the period 1969/70 through 1993/94; in no year was that list shorter than 26 names. Two facts about these "suppliers" should be noted. First, they may or may not be individual producers. Second, these are the suppliers with programs on the air in prime time. The actual list of potential suppliers willing to provide prime time series would no doubt be much larger. Thus, it is likely that EI's list of suppliers understates the actual number of producers in the market to provide prime time series.

More generally, the EI Study identified 1399 production companies producing shows that were either broadcast or carried on cable in 1994. The networks were three of many producers, whether one considers network prime-time only or the entire programming day.

The LECG Study also calculates HHIs for broadcast programming. LECG's 1993 HHIs for various dayparts were: prime time broadcasts (all days) -- 1540; prime time broadcasts (weekdays) -- 1347; and total day broadcasts -- 854. Based on Commission calculations of LECG data, the HHI for prime time access period broadcasts (weekdays) was 1705. *See* LECG Study, Tables II.1 through II.4. In short, LECG's HHIs also indicated that the supply side of the video programming production market was either moderately concentrated or unconcentrated.

by the Staff of the FTC's Bureau of Economics ("FTC Staff"), at 13, note that the minimum efficient scale of production in this market is low.[80] Therefore, entry is not impeded by significantly high production costs. The FTC Staff also states that there are no other obvious impediments to entry and growth by new suppliers of programming.[81]

36. We therefore conclude that no buyers or sellers, acting alone or together, are likely to be able to exercise undue market power in the video programming production market. In addition, entry barriers are low. In particular, it is unlikely that the three networks will be able to exercise market power in the video programming production market, either on the demand or supply side, if PTAR is repealed.

37. The WW Study argues that there is evidence of a trend towards increasing vertical integration by ABC, CBS, and NBC. It states that these three networks may be increasing their financial interests in program production and distribution.[82] The WW Study points to the possibility that vertical integration is being driven by a "land rush" for the fixed supply of programming resources (*e.g.*, film archives, experienced programming talent). According to WW, this poses the danger of foreclosing unintegrated producers from the program production market and deterring new entrants into the market.[83]

38. We are not persuaded by this argument. The WW Study itself seems to cast doubt on the prospect that the vertical integration "trend" is actually deterring new entrants into the program production market: "At the moment, given the many alternative sources of programming and the many outlets for broadcasts, it is unlikely that any one firm will be able to amass such market power."[84] In addition, our measures of market concentration in video programming distribution and production do not suggest that firms can exercise undue market

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[80] In its filing the FTC Staff shows, in Tables 3, 4, and 5, that the smallest companies in video programming production in 1994, 1977, and 1970, respectively, had market shares of network programming hours ranging from 0.9 to 1.6 percent. The FTC Staff Comments at 13 conclude therefore that the minimum efficient scale of production in this market was low. Thus, entry is not limited to very large companies. As the FTC Staff documents, small companies can enter and successfully sell prime-time programs. This ease of entry on a small scale adds to the difficulty of large firms attempting to exercise market power.

[81] Satellite technology significantly reduced the average costs of program distribution, thereby facilitating entry into this market. Previously, networks had leased AT&T microwave facilities. *See Network Inquiry Study* at I-113-14 & n.254. *See* also Joel B. Dirlam and Alfred E. Kahn, "The Merits of Reserving the Cost-Savings from Domestic Communications Satellites for Support of Educational Television," 77 Yale L. J. 494 (1968).

[82] WW Study at 7-9.

[83] WW Study at 38-42.

[84] WW Study at 39-40.

power there.[85] Entry also appears likely to be a constraint on firms attempting to dominate those markets. We also note greater integration is not in itself contrary to the public interest.[86] Indeed, vertical integration can provide greater efficiencies and better service to the consumer.

C. The National Television Advertising Market

37. LECG argues that "advertising rate dynamics [are] a superior indicator of the networks' market position" because the television industry is "the business of producing audiences for advertisers."[87] The LECG Study asserts that the three networks dominate the advertising market, noting that the networks raised their *nominal* prime time advertising rates from 1980 through 1991 even though their prime time network audience share steadily declined throughout this period.[88] An examination of nominal (*i.e.*, unadjusted for the effects of inflation) advertising rates over time, however, tells little if anything about undue market power without controlling for a number of variables, especially inflation and increases in demand for advertising. In fact, the increases in rates LECG points to would appear to be readily explained by these two factors, rather than undue network market power.[89] Furthermore, the record before us indicates that ABC, CBS, and NBC each has an average share of national television advertising revenues that has fallen by one-quarter from 19.1 percent in 1970 to 14.6 percent in 1993. The record further shows that even if the market is defined more narrowly as national television advertising *less* national spot sales, each

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[85] In *Fruehauf Corp. v. FTC*, 603 F.2d 345 (2d Cir. 1979), the court rejected the foreclosure theory absent very high market concentration in one stage of production. The 1992 DOJ/FTC Merger Guidelines reflect the notion that vertical mergers often generate important efficiencies and cannot present a competitive problem unless one stage is highly concentrated, *i.e.*, exhibit an HHI above 1800. *See also* Comanor, "Vertical Mergers, Market Power, and the Antitrust Laws," 57 Amer. Econ. Rev. 254, 265 (1967); Robert Bork, *The Antitrust Paradox* (Basic Books 1978); Peltzman, "Public Policy Toward Vertical Mergers," in J.F. Weston and S. Peltzman, eds., *Public Policy toward Mergers* (Goodyear Publishing Company 1969); Perry, "Vertical Integration: Determinants and Effects," in Richard Schmalensee and Robert Willig, eds, *Handbook of Industrial Organization*, Vol 1, Ch. 4, at 183-255 (Elsevier Science Publishers B.V. 1989).

[86] Antitrust authorities generally consider vertical integration to be competitively neutral or benign in the absence of evidence of market power at some relevant stage of the vertical ownership chain. *See* P. Areeda & D. Turner, *Antitrust Law*, Vol. III, ¶ 724 at 195 (1978). The record indicates that the networks do not dominate at any of these stages.

[87] LECG Study at 11, 21. *See also* INTV Comments at 39-40.

[88] LECG Study at 22.

[89] *See* EI Supplementary Study at 43-45.

network's share is less than 23 percent.[90] Under the current record, then, LECG has not made a case that the networks' market shares in either market are sufficiently large to suggest that they could exercise undue market power either individually or acting together.[91]

38. In any event, as the EI Supplementary Study, at 40-41, points out, PTAR was not adopted to address the structure or performance of the advertising industry. This is why the *Notice* did not explicitly seek information on television advertising markets. The Commission adopted PTAR due to concerns that the three networks dominated the production and delivery of television programming. Examination of video programming distribution and the video programming production market is thus directly relevant to whether PTAR is necessary under today's market conditions. We cannot say the same for the television advertising market, nor are we persuaded that PTAR is the appropriate mechanism for addressing the networks' role in these markets.[92]

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[90] *See* EI Study at 20, App. A, Table A-10.

[91] The national television advertising market examined in the EI Study includes network television advertising revenue, national spot television advertising revenue, national cable television advertising revenue, and national syndication television advertising revenue. *See* EI Study, Table A-10. Commission calculations suggest that this large market would be unconcentrated, with an HHI of less than 1000, assuming that all non-network advertisers are sufficiently small that they contribute little or nothing to market concentration. We believe this to be a reasonable assumption.

The narrower market, measured by national television advertising revenues less national spot sales, would be moderately concentrated with an HHI of approximately 1600-1700. This is a Commission estimate based on market shares for each network of 23 percent with an estimated additional increment to the HHI of no more 100 points from all other national television advertising outlets. Our hypothesis is, again, that no single advertising outlet other than a broadcast network is likely to have a significant market share in this narrower advertising market.

[92] The Commission is examining the television advertising market in its pending proceeding concerning its television ownership rules. *TV Ownership Notice*, 10 FCC Rcd at 3541. It is also examining this market in its review of two of its network rules concerning network control of station advertising rates and network representation of affiliates in selling non-network advertising. *Notice of Proposed Rule Making* in MM Docket No. 95-90, FCC 95-226, released June 14, 1995. These two proceedings may shed greater light on the structure of the television advertising market than the limited record presented to us by LECG in the instant proceeding. A more complete record developed in these proceedings conceivably could lead us to alter the conclusion we reach here about network power in this market and warrant modifying our ownership rules and the two network rules accordingly. This, however, would not provide a basis for continuing PTAR. As we have noted, we do not believe PTAR is an appropriate regulatory vehicle for addressing concerns about network power in the television advertising market.

V. THE COSTS OF PTAR

39. In assessing the continuing need for PTAR, we must take into account the costs the rule imposes on the networks, their affiliates, producers of network programming, television viewers, and the efficient functioning of the market. One obvious cost of the rule is that it restricts the programming choices of Top 50 Market Affiliates. They cannot air either network or off-network programming during the access period. While these affiliates urge the retention of the network restriction, they call for repeal of the off-network provision because it "now actually serves to frustrate the accomplishment of one of the rule's central objectives: namely, the maximization of programming choices for local licensees."[93] The WW Study describes how the off-network restriction interferes with the smooth functioning of the network-affiliate relationship by raising the overall costs of network broadcasting.[94] With PTAR in place, the affiliate must either make investments to produce programs itself, or it must purchase first-run programs from syndicators. In the latter case, the affiliate bears the transaction costs of establishing relationships with syndicators and independent programmers. In either case, the affiliate bears the added risk of how first-run programming will perform relative to known-to-be-popular network reruns. As a result of these higher costs, the total of net revenues to be shared among networks and affiliates is made smaller by PTAR.

40. PTAR harms not only networks and affiliates, but the producers of network programming. The off-network restriction has had the unintended effect of discouraging investment in prime-time programming. Producers rely to a great extent on their ability to sell reruns of their programs -- *i.e.*, off-network programs -- to recoup their costs and to earn a profit. The license fee the networks pay for the right to air prime-time entertainment programs often does not cover the costs of producing these programs. According to the Coalition, in fact, the network license fee usually covers only 70 percent of the producer's costs, resulting in production deficits for network programming.[95] The off-network restriction, however, diminishes producers' ability to recoup costs by artificially restraining the prices of off-network programming. It does so by eliminating the Top 50 Market Affiliates from the range of potential purchasers of this programming. By reducing demand, the prices for off-network shows are reduced.[96] PTAR provides a corresponding subsidy to producers of first-

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[93] NASA Comments at 13.

[94] WW Study at 25-6. For a brief summary of the efficiencies of television networks, *see* Owen and Wildman, *Video Economics* at 206-10. *See also* Comments of FTC Staff at 7-10.

[95] Coalition Comments at 9.

[96] The Coalition argues that the impact of the off-network restriction can be seen by comparing a Fox program, which is not subject to PTAR, and an ABC program: "In 1991, . . . Fox's *Married ... With Children* garnered syndication fees of approximately $2.4 million per episode. In contrast, ABC's *Roseanne*, a similar program in terms of demographics and ratings earned $1.8 million per episode just one year later." Coalition Comments at iv.

run syndicated programs in the form of higher prices and to certain independent stations in the form of higher ratings. The Commission believes that PTAR produces costs and inefficiencies to viewers that are larger than the benefits, if any, of PTAR to viewers.

41. Reduced prices for off-network shows will naturally have the effect of lowering the return on network programming, thus reducing the quantity and quality of such programming that a non-PTAR market would otherwise produce. In this respect, television programs can be likened to durable goods. Like any durable good, restrictions on future availability and uses will reduce the value of the good. Program producers will be induced to reduce the quantity of programming they sell because PTAR reduces the size of the secondary market for those programs. This may result, as the WW Study says, in fewer episodes of each series. In some cases, there may be sufficiently few episodes that the series does not qualify for syndication.

42. We are persuaded by WW that by reducing the prices of off-network programming, PTAR's off-network restriction also tends to reduce the quality of prime-time series.[97] WW assumes, as is conventional among economists, that the per-episode production cost of a series may be one measure of program quality.[98] Focussing therefore on this single (and quantitative) measure of quality and not on program content *per se* for a given quantity of prime-time programming, an increase in quality will increase the series' incremental advertising revenue when the quality improvement increases the size of the series' audience.[99] WW assumes also that the incremental cost of that quality increase remains unchanged. In these circumstances, programmers will spend more on program quality when PTAR's off-network restriction is eliminated because programmers can use that quality increase to expand audiences and advertising revenues.

43. In addition to the costs described above, PTAR as a whole prevents the networks and their affiliates from taking advantage of network efficiencies during the access hour. Networks can deliver large audiences to advertisers, which in turn allows the networks and their affiliates to provide higher cost programming that is quite popular among audiences during prime time. The EI Study argues that the loss of these efficiencies due to PTAR

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[97] *See* WW Study at 26; Comments of FTC Staff at 23-26; *see also* EI Study at 45.

[98] *See* Owen and Wildman, *Video Economics* at 144-145: "One would expect that viewers will find programs with large budgets more appealing than programs with small budgets, because program producers will spend the additional production dollars on things that viewers like. Spending more to get more popular actors, better script writers and directors, and more sophisticated special effects will generally result in a more popular program or film. If it were not possible to increase a program's audience appeal by increasing its budget, profit-maximizing producers would never produce the large budget productions ($1,000,000 per hour and more) we see on prime-time network television. If, say, a $700,000 program would be just as popular, networks would demand the latter."

[99] *See id.* at 145-146.