

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

AUG - 3 1998

In the Matter of )  
)  
Fees for Ancillary or Supplementary )  
Use of Digital Television Spectrum )  
Pursuant to Section 336(e)(1) )  
of the Telecommunications Act of 1996 )

MM Docket No. 97-247

**REPLY COMMENTS OF  
THE NATIONAL CABLE TELEVISION ASSOCIATION**

The National Cable Television Association, Inc. ("NCTA") hereby submits its reply comments in the above-captioned proceeding.

**INTRODUCTION**

The purpose of this proceeding is to establish the fees to be paid by broadcasters if they use any portion of their newly allocated digital television spectrum to provide ancillary and supplemental services in addition to free, over-the-air television programming. In enacting Section 201 of the Telecommunications Act of 1996, Congress determined that broadcasters should not be required to pay for any spectrum that was allocated to them by the Commission for the purpose of providing digital television, so long as (1) they used such spectrum only to provide services that were free to viewers and (2) they received no compensation (other than advertising revenues) from a third party for transmitting that party's information. But if a broadcaster uses its digital spectrum to provide services for which a subscriber fee is required, or if the broadcaster receives revenues from third parties for the transmission of those parties' information, then a fee will be required.

Nothing in the Act suggests that Congress intended to subsidize any portion of the digital spectrum used to provide feeable services. Nothing suggests that Congress intended to

encourage the use of digital spectrum to provide such ancillary and supplemental services, especially in lieu of free high definition or multiple standard definition television channels. And nothing suggests that Congress intended to free broadcasters from any risks associated with the provision of such services -- risks that are, of course, borne by any other providers of similar services. Nevertheless, the broadcasters uniformly urge that rates be set at minimal levels for these very reasons.

As demonstrated below, broadcasters should not be shielded in the early years from the competitive risks borne by other providers of such services, nor should the Commission set the fee artificially low to protect broadcasters from these risks and unfairly subsidize their provision of ancillary and supplementary services.

**I. BROADCASTERS SHOULD BEAR THE SAME MARKETPLACE COSTS AND RISKS AS OTHER PROVIDERS OF COMPETITIVE SERVICES.**

National Association of Broadcasters and the Association for Maximum Service Television, Inc. ("NAB/MSTV") remarkably assert that "[b]ecause a simple gross revenue based fee would impose costs on licensees before any new service is likely to become profitable, the disadvantage of a fee on gross revenues is that it may discourage broadcasters from offering certain services where the prospects of ultimate success are uncertain."<sup>1</sup> Apparently, the broadcasters believe that they should not be required to pay for spectrum that is used to provide ancillary and supplemental services unless and until such services are certain to succeed.

Accordingly, NAB/MSTV propose that broadcasters be required to pay no fee at all for spectrum used to provide a feeable service until two years after first receiving revenues from that service. This free testing period should, in their view, be adequate to allow a broadcaster to "determine if a new service will obtain marketplace acceptance and to at least begin recovery of

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<sup>1</sup> NAB/MSTV Comments at 12 (emphasis added).

its costs.”<sup>2</sup> The Association of Local Television Stations (“ALTV”) similarly contends that “the Commission should waive fees entirely for unprofitable services.”<sup>3</sup>

Congress specifically mandated that the fee requirements established by the Commission for spectrum used for ancillary and supplemental services be designed “to avoid unjust enrichment.”<sup>4</sup> It would be the height of unjust enrichment to give broadcasters free use of a necessary and valuable input of production -- *i.e.*, scarce spectrum -- merely because it might not be clear whether or not that use would turn out to be profitable. Although broadcasters have always been given free use of the spectrum, most firms, including those with whom broadcasters will compete in offering ancillary and supplemental services, have to invest in and commit to pay for their plants and facilities whether or not they are earning profits, and whether or not the ultimate success of their products and services is assured.

Allowing broadcasters to use valuable spectrum at no charge unless and until they figure out how to use it successfully and profitably is fundamentally unfair to other competitors and potential competitors who are not allowed the luxury of such cost-free, trial-and-error experimentation. And it encourages competitive inefficiency by subsidizing unsuccessful and unprofitable uses of a valuable resource that would, in the absence of such subsidies, be quickly corrected or punished by market forces.

Giving broadcasters a free ride for a fixed period of time even if their ancillary and supplemental services are profitable or success is assured during that time period is especially unfair. For such established and successful services, the only effect of such a subsidy is to give

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<sup>2</sup> *Id.* at 13.

<sup>3</sup> ALTV Comments at 2.

<sup>4</sup> 47 U.S.C. § 336(e)(2)(A).

broadcasters a boost vis-à-vis their competitors that has nothing to do with any superior competitive skills or efficiencies on the part of the broadcasters.

**II. THE COMMISSION SHOULD NOT PURPOSELY ENCOURAGE BROADCASTERS TO PROVIDE ANCILLARY AND SUPPLEMENTARY SERVICES INSTEAD OF HDTV AND OTHER FREE TELEVISION CHANNELS.**

The broadcasters also argue that any fees imposed for their use of spectrum to provide ancillary and supplemental services should be minimal. Thus, NAB/MSTV contend not only that there should be no fees during the first two years after revenue is first received for a service, but that fees should not exceed two percent of gross revenues after those first two years -- when, presumably, the broadcaster has already had an opportunity to determine whether or not the service will succeed.<sup>5</sup> ALTV proposes an even lower fee of one percent or less of gross revenues.<sup>6</sup>

NAB/MSTV acknowledge that even a two percent fee is at “the lower range” of “private sector licensing fees.”<sup>7</sup> But they suggest that establishing especially low fees is appropriate in order to “encourag[e] the development of new technologies and services.”<sup>8</sup>

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<sup>5</sup> NAB/MSTV Comments at 17. NAB/MSTV also argue that a service should not be regarded as feeable if a broadcaster receives additional revenue from an advertiser in exchange for downloading data about its product. It also seeks to exclude revenues from advertising sold on subscription services from the fee calculation. NAB/MSTV Comments at 6-7. But the statutory language and legislative history are clear that Congress intended to require broadcasters to pay a fee to the government when they use the spectrum for any add-on services other than free television. 47 U.S.C. section 336(e)(1); H.R. Conf. Rep. No. 458, 104<sup>th</sup> Cong. 2<sup>nd</sup> Sess. 160 (1996). In the above situations, where the broadcaster receives additional revenues from the advertiser by using the spectrum to download data or charges a customer a subscription fee to receive a service which contains advertisements, all of the compensation received should be included in the calculation of the fee on gross revenues. *See also* UCC Comments at 12.

<sup>6</sup> ALTV Comments at 17.

<sup>7</sup> NAB/MSTV Comments at 17.

<sup>8</sup> *Id.* at 18; *see also* iii (“high risks associated with untried ancillary and supplementary services dictate that the Commission set a low fee to encourage innovation.”)

ALTV argues that the risks of setting fees too low are greater than the risks of setting fees too high:

If fees are too high, they will create a disincentive to provide new services, leading to losses in consumer welfare. . . . On the other hand, if fees are too low, the social costs are smaller. The primary effect would be a wealth transfer with little effect on consumer welfare.<sup>9</sup>

But Congress struck precisely the opposite balance. The one thing that Congress specifically directed the Commission to avoid was “unjust enrichment” -- *i.e.*, unfair “wealth transfers” to broadcasters. On the other hand, as UCC, *et al.* correctly point out, “nothing in the plain language or legislative history of the 1996 Act manifests any Congressional intent to incentives broadcasters to provide these [ancillary and supplementary] services.”<sup>10</sup>

The broadcasters talk as if the choice that they will face once fees are established will be simply whether or not to provide “new technologies and services” that consumers supposedly demand. In reality, what they must decide is whether to use the spectrum that has been allocated to them to provide feeable or non-feeable services. The choice is between providing (1) a single channel of high definition television, (2) multiple channels of free, standard definition television, or (3) some combination of free, standard definition television and ancillary and supplementary services, most of which are likely to be provided competitively by others. To the extent that HDTV uses all of a broadcaster’s spectrum, provision of any ancillary and supplementary services precludes the provision of HDTV and vice versa.

NAB/MSTV warn the Commission to “proceed with caution in order to avoid making a decision that -- even unintentionally -- would alter the amount and mix of services that

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<sup>9</sup> ALTV Comments at 3-4.

<sup>10</sup> UCC, *et al.* Comments at 2.

broadcasters might develop in the future.”<sup>11</sup> But any decision that the Commission makes in this proceeding will inevitably affect the amount and mix of services to be provided by broadcasters -- because some services will be subject to spectrum fees and some will not. The higher the fee, the greater the incentive to provide non-feeable services; the lower the fee, the greater the incentive to provide feeable services.

Why is it better to err on the side of encouraging broadcasters to provide ancillary and supplementary services instead of high-definition or free standard definition television? Nothing in the Act or legislative history favors striking such a balance. Nor does anything in the Commission’s digital television policies. Indeed, in light of the Commission’s plans to require television viewers to buy new digital television sets and/or converters for all their existing sets in order to watch any television at all, it would seem more appropriate to attempt to encourage the use of digital spectrum for HDTV and other non-feeable services.

### **III. FEES SHOULD BE SET AT THE HIGH END OF THE RANGE PROPOSED BY THE COMMISSION.**

Most parties (including NCTA) agree that setting fees as a percentage of gross revenues from the provision of ancillary and supplementary services is the best approach. As shown above, the broadcasters’ rationales for adopting a low percentage do not hold water. Rates should not be set artificially low to protect broadcasters from marketplace costs and risks. Nor should they be set artificially low to encourage broadcasters to use their spectrum to provide feeable services.

They should, instead, be set -- as the Act requires -- at a level that prevents unjust enrichment and compensates the public for the value of the spectrum. As UCC shows, even the

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<sup>11</sup> NAB/MSTV Comments at 3.

high end of the range proposed by the Commission -- *i.e.* ten percent -- is on the low end of what is paid for other valuable government concessions:

Ten percent would be less than the 12.5% to nearly 17% of gross revenues that mining and oil companies pay the government for onshore and offshore mineral leases on federal public lands. . . . It would also be on par with the 9% gross revenue fee that concessionaires pay certain federal agencies (such as NASA and the Department of Veterans Affairs) for the right to operate concessions on federal lands.<sup>12</sup>

Moreover, as we pointed out in our initial comments, the Commission should take into account the fact that, for all of the broadcasters' talk about the risks and up-front costs associated with providing ancillary and supplementary services, most of those costs will be "sunk" or fixed costs that have already been incurred in connection with the provision of the one channel of free television service that each broadcaster is required to provide. In other words, once the towers and transmitters are in place to transmit digital signals, the incremental cost of providing feeable services will be small -- and most of the revenues generated by such services will, thus, constitute profits.<sup>13</sup> Where gross revenues do not significantly exceed profits, a much higher percentage fee is appropriate than would be the case if marginal costs were high and gross revenues did significantly exceed profits.<sup>14</sup>

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<sup>12</sup> UCC Comments at 9.

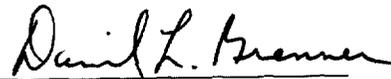
<sup>13</sup> See NCTA Comments at 11.

<sup>14</sup> We also showed in our initial comments that setting the fee at a significant percentage of gross revenues would be desirable to prevent broadcasters from unfairly cross-subsidizing feeable services, to the detriment of their competitors, with revenues from the non-feeable services for which they have received free spectrum. See *id.* at 12.

## CONCLUSION

For the foregoing reasons, and for the reasons set forth in our initial comments, the Commission should set fees that are sufficient to prevent unjust enrichment of broadcasters and to ensure that broadcasters do not compete unfairly in the provision of ancillary and supplementary services. A gross revenues fee, where the percentage is at least on the high end of the range proposed by the Commission, would be most appropriate in light of all the circumstances surrounding the allocation of spectrum to broadcasters for feeable and nonfeeable uses. Such a fee would be consistent with the Commission's statutory mandate.

Respectfully submitted,



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