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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 Protection	)	MM Docket No. 92-264
And Competition Act of 1992	)	
	)	
	)	
Horizontal Ownership Limits	)	

COMMENTS OF THE NATIONAL CABLE TELEVISION ASSOCIATION

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The National Cable Television Association ("NCTA"), by its attorneys, submits the following comments in response to the Commission's Notice of Proposed Rulemaking in the above-captioned proceeding.

INTRODUCTION AND SUMMARY

This proceeding is being undertaken at a time when the cable industry--and the communications industry more generally--is undergoing sweeping changes. Fundamental assumptions regarding the competitiveness of markets, the direction and pace of changing technology, and role of regulation are being challenged almost daily.

The horizontal concentration rule in its present form is a regulation from a prior era. It was established at a time when cable companies faced no significant multichannel video service competition. Most cable companies offered a limited number of channels and significant growth in channel capacity was not anticipated. As a result of the limited capacity, it was argued, programmers with ideas for new cable channels found it difficult to reach the multichannel audience.

Congress did not prescribe a fixed horizontal ownership limit, but instead directed the Commission to establish "reasonable limits on the number of cable subscribers a person is authorized to reach,"[1] either through ownership or on an attributed basis. Under the statute's terms, the Commission has broad discretion to establish a horizontal ownership limit.

The horizontal ownership rule is intended to prevent an MSO that controls too many subscribers from impeding the competitive flow of programming and, by extension, from restricting the programming options available to consumers. At the same time, the Commission is directed to consider the efficiencies that large-scale operations can achieve.

The conditions that animated the Commission's 1993 rule are no longer present. Cable companies are subject to significant and growing competition from DBS and other multichannel services that offer programmers many new outlets. Technology has expanded the number of available channels on cable systems--and with it the opportunities for new programmers to reach cable audiences. And, the Commission effectively applies regulatory tools other than the horizontal concentration rule--which has been stayed by judicial order during this entire period--to achieve the policy purposes that the horizontal rule was intended to accomplish. Collectively, these developments significantly reduce the chances that a large MSO will improperly exercise monopsony power or engage in vertical foreclosure.

Based on the statutory factors and evaluation of current conditions, the Commission should emphasize antitrust analysis in its evaluation of horizontal ownership. The rule should, moreover, focus upon "efficiencies" over generalized concerns regarding the flow of programming. These emphases are justified because there is no evidence that increased

1 47 U.S.C. § 533(f)(1)(A).

ownership levels will result in impeding the flow of programming and the addition of distribution outlets increases a programmer's opportunities to reach customers.

This review must address the mechanism for assessing horizontal concentration and the level of ownership permitted individual MSOs. As to the mechanism, it should be changed from homes passed to subscribers. The horizontal ownership rule is intended to protect programmers and consumers against the exercise of monopsony power or vertical foreclosure by cable MSOs. The homes passed measurement was appropriate when MVPD homes were nearly synonymous with cable homes. Now that more 12 million MVPD homes are served by alternative distributors, a measurement based on cable homes passed will not properly account for the relationship between cable MSO subscribers and non-cable subscribers. In today's competitive environment, a subscriber-based measurement is a more effective tool with which to assess a cable MSO's relative position in the marketplace.

Finally, the Commission should permit cable MSOs to grow internally beyond the cap. Any other approach would penalize operators that successfully attract customers by offering competitively attractive services.

I. EXISTING COMPETITIVE, TECHNOLOGICAL AND REGULATORY CONDITIONS JUSTIFY RELAXATION OF THE HORIZONTAL CONCENTRATION RULE FOR THE CABLE INDUSTRY

A. Growing Competition in Multichannel Services is Significantly Reducing the Risk of Vertical Foreclosure or the Improper Exercise of Any Monopsony Power

1. State Of Multichannel Video Competition: 1993

Competition faced by cable systems has increased dramatically since the Commission's adoption of the horizontal ownership rule. In 1993, C-band satellite dishes were the principal multichannel service alternative to cable. The effectiveness of C-band devices as a competitor to cable service was viewed as limited, however, because C-band customers were required to bear significant up-front costs. The cumbersome nature of C-band equipment also created practical limitations that constrained its effectiveness as a competitor to cable companies. C-band was often viewed as a desirable option mostly in remote rural areas where cable service was not offered.

Cable companies also faced sporadic competition during this period from other multichannel sources. Apartment buildings in urban centers selectively opted for Satellite Master Antenna Television ("SMATV") service and Multipoint Distribution Service. And, in selected areas, a second cable system entered to challenge the incumbent. By late 1993, incumbent cable operators held a multichannel video share of just below 95 percent.[2]

The C-band and other scattered non-cable multichannel audiences were not large enough, in the Commission's view, to fully ameliorate Congress's concern that a large MSO could exercise monopsony power or engage in vertical foreclosure; i.e., disadvantaging an unaffiliated programming rival by refusing to carry it or otherwise impeding its offering to cable customers on the cable system. The Commission adopted the horizontal concentration rule, and took other steps, to promote the competitiveness of multichannel programming services.

2. Multichannel Video Competition Today and Horizontal Concentration

The competitive circumstances now faced by cable companies are very different from 1993. Virtually all of the 77 million multichannel service customers (and the tens of millions who elect not to purchase multichannel service) have at least two multichannel services from which to choose: cable and DBS. Slightly more than 12 million multichannel subscribers, or

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2 Annual Assessment of the Status of Competition in Markets for the Delivery of Video Programming, 13 FCC Rcd 1034 (1998), at Appendix E (Fourth Annual Competition Report).

more than 15 percent, obtain their services from one of cable's multichannel competitors. This growth of multichannel competition has profound implications for the horizontal concentration rule. Rather than being in a position to foreclose the launch of new program services, MSOs faced increased pressures to expand service choices and deliver the programming subscribers most want to receive.

a. Growth of Direct Broadcast Satellite

The development of DBS is the most significant competitive event in the multichannel marketplace since 1993. DBS has experienced unusually quick consumer acceptance. The rapid increase in DBS subscribership, and the marketplace response by cable operators that it has engendered, evidences an effectively competitive multichannel marketplace.

DBS industry data show that there are now 7.25 million DBS subscribers, which equates to a national share of more than nine percent of multichannel homes.[3] When combined with the 2 million C-band subscribers, the DTH (Direct-to-Home) satellite services account for nearly 12 percent of the multichannel universe. In other words, nearly one in eight multichannel customers is a satellite customer.

The national numbers do not tell the whole story. Last year, NCTA's comments to the Cable Competition Report showed that in more than 24 states the DTH penetration exceeded 10%. The number has now grown to 35 states.[4] Consumers clearly view DBS and cable as similar and substitutable. The Department of Justice recently confirmed this development, finding that DBS and cable compete for the same subscribers at comparable prices:

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3 Comments of the National Cable Television Association, Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming, CS Docket No. 98-102, Jul. 31, 1998.

4 Media Business Corp., SkyTRENDS, July 1998.

> Cable and DBS are both MVPD products. While the programming services are delivered via different technologies, consumers view the services as similar and to a large degree substitutable. Indeed, most new DBS subscribers in recent years are former cable subscribers who either stopped buying cable or downgraded their cable service once they purchased a DBS system.[5]

This contrasts with the less competitive circumstances of only a few years ago.

b. Growth of Other Alternative Multichannel Distribution Media

SMATVs, MMDS and telcos also provide significant competition to incumbent cable operators. Combined, they offer service to nearly three million customers. And, they offer cable's competitors access to many million more.

SMATVs provide an important competitive alternative to cable systems in urban markets where large numbers of persons reside in multi-dwelling units (MDUs). Nearly one million customers receive multichannel service via SMATVs. But the potential SMATV market is as large as the 28 million residents of MDUs.

The Commission's actions over the past year have tilted the regulatory balance further in favor of SMATV operators in the lucrative MDU segment. The decision in Cable Home Wiring[6] increases the ability of a SMATV operator to take advantage of a cable operator's investment in inside wiring. In a similar vein, the Commission's recent declaratory ruling in Entertainment Connections, Inc. ("ECI") gives a SMATV operator an additional competitive advantage by allowing it to operate as a full-fledged cable operator.[7]

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5 United States v. Primestar, No.1: 98CVO1193, Complaint, ¶63 (D.D.C. May 12, 1998).

6 Telecommunications Service Inside Wiring, 13 FCC Rcd 3659 (1998).

6 Entertainment Connections, Inc., FCC 96-111, rel. Jun. 30, 1998. The FCC ruled that if a SMATV operator uses telephone company facilities to cross public rights-of-way, it does not qualify as a "cable system." A SMATV is not obliged to comply with many of the legal requirements imposed upon cable systems by Title VI of the Communications Act including the

Repeal of the telco/cable cross-ownership prohibition in the 1996 Act has enabled several major telephone companies to enter the cable television business as full-fledged competitors to incumbent cable operators. Ameritech, among the large telephone companies, has been the most active in seeking cable franchises and constructing systems. Ameritech apparently intends to offer wire-based video service throughout its telephone service area. It has obtained at least 78 franchises and is offering service in 61 communities.[8] When all of these franchises become operational, Ameritech will be able to serve more than one million subscribers.

SNET has received a franchise to provide cable service throughout Connecticut. It has announced plans to construct video facilities over a several year period. The actual number of subscribers served by SNET is not reported.

Bell Atlantic is operating a single cable system in Dover Township, New Jersey. But its video operations are actually coextensive with its telephone service area. It has announced a partnership with DirecTV and USSB to sell those services throughout its telephone service area. SBC also has announced plans to market the services of DirecTV and USSB to its residential customers in MDUs.[9]

Multichannel Multipoint Distribution Service (MMDS) is another significant actual and potential cable competitor. The most recent data indicate that nearly 1.6 million subscribers

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payment of franchise fees and the provision of PEG channels. The Commission's action may also enable SMATV's to avoid the prohibition against cream-skimming (and red-lining) contained in most franchises. The Commission has authorized ECI to function like a wireline cable operator without accepting the vast majority of a cable operator's regulatory responsibilities.

8 Ameritech Press Release, "Ameritech Wins Chicago Cable TV Franchise," Aug. 5, 1998 (http/www.ameritech.com/media/releases/Release-1588.html).

9 "DBS Finally Rings Up the Bells," Multichannel News, Mar. 9, 1998, at 1.

obtain service through MMDS. As with the other distribution media, MMDS is available as a competitive alternative to many more customers than actually purchase the service.

The vitality of MMDS as a competitive alternative is demonstrated by the commitment of BellSouth to construct new, state-of-the-art systems. BellSouth began offering MMDS video service in New Orleans in 1997. It commenced service to Atlanta this year. It has plans to offer MMDS service to other major sections of its region.

And, of course, a large percentage of all Americans continue to rely on broadcast television for their video entertainment needs. With Congress's giveaway of free additional spectrum to broadcasters and to provide one or more channels of digital video, the competitiveness of broadcast television will become even stronger.

3. Consequences of Increasing Competition for the Horizontal Concentration Rule

In its previous evaluation of horizontal concentration, the Commission identified the purpose for establishing ownership limits. It found that if a single entity served too great a number of subscribers, it might be able "to preclude the launch of new video programming services"[10] in which it was not interested. At the same time, the Commission recognized potential "efficiencies" that could result from horizontal concentration.[11] It was on the basis of the balancing of these concerns that the Commission decided in 1993 to set the horizontal ownership limitation at 30 per cent of all homes passed by cable systems.

The quantum increase in multichannel competition since 1993, by itself, justifies a substantial relaxation of the horizontal concentration rule. Programmers have growing numbers

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10 Implementation of Sections 11 and 13 of the Cable Television Consumer Protection and Competition Act of 1992, 8 FCC Rcd 8565, 8576 (1993).

11 Id.

of choices among distribution outlets. For example, DBS, because it generally has more channels than cable, offers more choices of programming--affiliated and non-affiliated--than cable systems. DBS has often been the first major provider of new program services because conventional cable systems are channel-locked. Being available on DBS then creates demand for more capacity on cable, so as to match the DBS offering. As a result, cable companies are given increased incentives to build greater capacity, add services to their channel line-ups and expand viewer choice. Thus, DBS and other MVPD competitors – such as BellSouth's 120 channel wireless systems – not only give programmers more early distribution but also create a competitive spur for cable carriage.

B. Technological Change is Significantly Reducing the Risk of Vertical Foreclosure and the Exercise of Monopsony Power by Large MSOs

Cable's fiber-based platform is providing the technological basis for dramatic changes in the services cable systems offer. Since 1993, cable companies have invested billions of dollars to upgrade their distribution facilities, extending fiber capacity deeper into the network. These investments have resulted in a significant increase in the number of deployed video channels. These changes have major consequences for horizontal concentration.

A comparison of 1993 and 1998 data demonstrate the change in raw terms. The average cable system's channel capacity has increased by 22 in just five years.[12] This means that most cable systems are carrying at least 22 additional national program networks since the rules were first adopted. The presence of more channels on the vast majority of systems increases the opportunities for new services to reach subscribers.

Cable companies are in the process of implementing digital compression. By compressing the size of the bandwidth required to receive video transmissions, digital

[12] Supra n.3, at 37.

technology enables cable companies to deliver many more channels over the same bandwidth. Compression ratios of twelve digital channels in exchange for one analog channel are already common. It is believed, however, that digital video compression is in the early stages of development. More advanced compression techniques available in the coming years are expected to result in systems offering many times the number of existing compressed digital video channels without requiring additional investment in bandwidth. Moreover, cable companies are not alone as providers of digitally compressed video. DBS, for example, has been using digital compression to deliver an expanded array of services, as discussed supra.

Digital compression has significant consequences for regulatory concerns about horizontal concentration. The possibility of vertical foreclosure was much greater where the average cable system capacity was 30 channels, and many of these channels were committed to the satisfaction of must carry/retransmission consent and PEG requirements. As capacity reaches into the hundreds, the competitive incentives of the operator to fill channels will overwhelm any theoretical motives to restrict access to unaffiliated programmers.

In another important development, the pattern of clustering systems that the cable industry has pursued over the past five years is producing operational efficiencies that benefit consumers. The 1997 Competition Report acknowledged the potential benefits of clustering by cable systems. According to the Report,

> Clustering systems provides mechanisms to reduce costs and to improve operating and management efficiencies, to eliminate system redundancies and to attract more advertising. The importance of advertising revenues for cable systems has emerged as a major factor promoting regional consolidation. By consolidating systems in major markets, MSOs can serve entire regions comprised of numerous local franchise areas. This assures advertisers that they will get extensive regional market coverage. Finally, regional clustering may also enhance MSOs' ability to

> compete successfully with LECs and major electric utilities as providers of data transmission and local telephone services.[13]

To achieve these benefits, major cable MSOs have moved to cluster their systems over the past five years. The increasing trend toward clustering reflects a sea change in the cable industry. The legal jurisdiction of local governments to franchise cable systems means that systems were built according to political boundaries.[14] Frequently, the size of local franchises made it difficult for cable systems to realize the economies of scale available to existing and potential competitors. When cable systems were almost exclusively a video service competing with local broadcasters, they were disadvantaged relative to broadcasters by the broadcasters' ability to offer advertisers reach throughout a regional market area. As cable systems evolve to offer Internet access and eventually to deliver residential telephone service, those systems that are part of regional clusters will be able to take advantage of the associated economies of scale.

By affording cable MSOs increased flexibility in the implementation of the horizontal concentration rule, the Commission will facilitate clustering. And, by accommodating larger clusters that are contiguous with regional markets, cable operators will be able to serve the same areas and the same customers as their multichannel video, broadcast, wireless and telephone competitors.

Moreover, the convergence of telecommunications media discussed for most of this decade is on the verge of becoming a reality. Convergence will break down lines that have

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13 Annual Assessment of the Status of Competition in Markets for the Delivery of Video Programming, 13 FCC Rcd 1034, 1115 (1998) (citation omitted).

14 For example, the different franchising authorities of Alexandria and Arlington has resulted in different cable systems serve these jurisdictions. They are served, however, by the same broadcasters, DBS, cellular and PCS systems, and telephone company.

divided providers of video and telecommunications. This change has profound implications for the Commission's policies, including horizontal concentration.

Since the advent of Commission regulation in the 1930's, a bright line has separated video and telephone policies. The technology used to deliver each service has ensured that the provider of one could not readily deliver the other over integrated facilities. The technological mismatch translated into economic circumstances in which entities attempting to bridge the divide discovered that there were limited economies in the joint offering of video and telecommunications services.

Technological developments are altering this dynamic. Cable companies are now using cable plant to provide video, broadband Internet access and telecommunications. The recently announced transaction between AT&T and Tele-Communications, Inc. demonstrates an endorsement of this strategy by the nation's largest domestic long distance carrier.

The Commission should incorporate consideration of the convergence of video and telecommunications into its review of horizontal concentration. Since MSOs must now devote resources to the implementation of one-stop shopping strategies, they will have even less theoretical ability or inclination to engage in vertical foreclosure strategies: since MSOs will have to compete with alternative video providers <u>and</u> telephone companies, they will have strong incentives to market unaffiliated programming to match the offerings of competitors. And, since MSOs offering telecommunications services must comply with numerous federal and state telecommunications regulations, as well as cable regulations, they will be subject to continuing regulatory oversight of their business operations. All of these factors argue strongly in favor of increased flexibility in the enforcement of the horizontal concentration rule.

Over the long run, cable-delivered broadband Internet access holds out the prospect of further alleviating concerns over vertical foreclosure. If broadband Internet access service succeeds as expected, it may eventually redefine the Internet and television by providing consumers with the variety available on the Internet over what is now conceived of as television. If this occurs, cable-provided broadband Internet access may eliminate the capacity constraints that limit the access of programmers to cable systems.

It may be argued that clustering and convergence do not require larger horizontal ownership, i.e., an MSO can accomplish these pro-competitive results without exceeding the current bar. This conclusion, however, ignores several market realities. First, as mentioned, the diminution in vertical foreclosure that one-stop shopping involves itself reduces the case for tighter horizontal limits. Second, to be efficient, cable system clustering may need to involve larger and larger geographic areas. Bell Atlantic's "cluster" covers the entire East Coast and the GTE merger proposes even greater expansion. Statewide and region wide telephone competitors are in place already. An artificial cap on cable's horizontal ownership (unrelated to traditional antitrust analysis) in this competitive environment makes little sense, especially where clusters would grow incrementally but for the artificial cap.

C. Commission Regulations Separate and Apart From the Horizontal Rule Protect Against the Possibility of Vertical Foreclosure and the Exercise of Monopsony Power by a Large MSO

Regulatory constraints on cable operators' control over the selection of the programs on their systems provide further grounds for the Commission to relax the horizontal concentration rule. The program access, program carriage, channel occupancy and must carry/retransmission consent regulations, in particular, implement legal constraints on a cable system's selection of programming. These regulations serve the same purposes as the horizontal ownership rule, making a restrictive implementation of the horizontal rule potentially duplicative.

The Commission has recognized that these regulatory steps have been effective in serving purposes similar to the horizontal rule. It observed that "Statutes and rules such as the program access, program carriage, channel occupancy limits, and must carry requirements all affect the way the cable television industry currently operates and have a profound effect on current industry structure and performance."[15] Citing the 1994 Competition Report, the Commission further noted that "[t]o the extent that large MSOs use their power over vertically-integrated programmers to obtain exclusive distribution rights to satellite-delivered programming, and those exclusive rights disadvantaged competitors of those large MSOs, the 1992 Cable Act's program access provisions and the Commission's program access rules appear to have largely addressed the problem."[16] It described the program access rules as a "necessary factor" in the development of the DBS and MMDS industries. And, it concluded that "[b]ecause these provisions have real and substantive impact on the market, the Commission, in setting the horizontal ownership limit, may properly consider the impact of these provisions in alleviating some of the public interest and anticompetitive concerns about horizontal concentration."[17]

The program carriage rules provide critical protection to programmers against the possibility that an MVPD will engage in discriminatory practices, including vertical foreclosure and the exercise of monopsony power. Under the rule, an MVPD is prohibited from engaging

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15 Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992, Memorandum Opinion and Order on Reconsideration and Further Notice of Proposed Rulemaking, FCC 98-138, rel. Jun. 26, 1998, at para. 50. ("Further Notice")

16 Id.

17 Id.

> … in conduct the effect of which is to unreasonably restrain the ability of an unaffiliated video programming vendor to compete unfairly by discriminating in video programming distribution on the basis of affiliation or nonaffiliation of vendors in the selection, terms, or conditions for carriage for video programming provided by such vendors.[18]

This provision, by its terms, protects unaffiliated programmers against discriminatory practices by MVPDs. The effectiveness of the program carriage rule is evidenced by the fact that only one program carriage complaint has been submitted in the five years that the rules have been in effect, and this case was settled by the parties.[19]

The channel occupancy limitations provide further protection against vertical foreclosure and the exercise of monopsony power. The channel occupancy rules generally provide that "…no cable operator shall devote more than 40 percent of its activated channels to the carriage of national video programming services owned by the cable operator or in which the cable operator has an attributable interest."[20] The channel occupancy limits, like the other regulations, have major implications for the horizontal ownership rule. As a result of the rule at least 60 percent of a cable system's capacity will be filled by must carry/retransmission consent stations, PEG access and leased access programmers, and satellite-delivered national programming offered by unaffiliated programmers. The channel occupancy rule is a more precise regulation than the horizontal rule to constrain an MSO's ability to engage in vertical foreclosure and to exercise monopsony power.

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18 47 C.F.R. § 76.1301(c).

19 Classic Sports Network v. Cablevision Systems Corp., CS Docket No. 97-171 Order, 12 FCC Rcd 22100 (1997).

20 47 C.F.R. § 76.504(a).

Must carry/retransmission consent arrangements further constrain the flexibility of cable operators in the selection of programming. At the time the horizontal ownership rule was implemented, the constitutionality of must carry was in serious doubt. Two appeals courts had previously struck down Commission efforts to impose must carry on cable systems. But the constitutionality of the must carry/retransmission consent scheme subsequently was affirmed by the Supreme Court. The result has been retransmission consent agreements by cable operators throughout the country to carry broadcast-network affiliated cable networks in return for retransmission consent. The leverage demonstrated by these agreements results in carriage of a significant number of additional unaffiliated channels.

The program access, program carriage, channel occupancy and must carry/retransmission consent regulations have been in force for a sufficient period to conclude that they provide whatever check may be needed against vertical foreclosure in today's competitive marketplace. These regulations in important ways duplicate the purposes of the horizontal rule. The existence of these other rules gives the Commission discretion to implement a more flexible, competitive horizontal concentration rule.

II. AS A RESULT OF CHANGED CONDITIONS, HORIZONTAL CONCENTRATION SHOULD BE REVIEWED BASED ON A FLEXIBLE AND PRO-COMPETITIVE STANDARD

When it adopted the horizontal ownership provision in 1992, Congress recognized that cable television would operate in a changing environment. It directed the Commission to adopt horizontal ownership rules that "reflect the dynamic nature of the communications marketplace."[21] In doing so, Congress recognized that a static, fixed approach would fail to take account of changing marketplace circumstances.

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21 47 U.S.C. § 533 (f)(2)(E).

The Commission has discretion, within the bounds of the statutory guidelines, to establish the horizontal ownership limit. The discretion is bounded on one end by the need to protect against vertical foreclosure and the undue exercise of monopsony power, and at the other by the recognition of prospective efficiencies that may result from a large MSO's service to an expanded subscriber base. The horizontal ownership provision sets forth guidelines for assessing the benefits and the risks, but leaves the actual assessment mechanism and determination of permitted and prohibited ownership up to the Commission.

Three principal tasks are assigned to the Commission. It must decide upon a tool for evaluating horizontal concentration. It must then use that tool to establish the maximum level. And, finally, it must consider whether an MSO should be afforded flexibility, in defined circumstances, to grow beyond the cap.

Changed conditions justify revised regulation in each of these areas. First, the mechanism for evaluating horizontal concentration should be changed from homes passed to subscribers. Second, horizontal concentration should be assessed based on a flexible, competitive standard. The Commission should emphasize antitrust analysis in its development of a horizontal ownership standard. Third, cable companies should be permitted to grow internally beyond the cap without requiring divestiture.

A. Because of Changed Conditions, the Horizontal Limit Should Be Based Upon the Number of Subscribers

The Act directs the Commission "to prescribe rules and regulations establishing reasonable limits on the number of cable subscribers a person is authorized to reach,"[22] either directly or as a holder of an attributable interest. In establishing the horizontal rule in 1993, the Commission chose to restrict the number of homes passed by a single operator instead of

[22] Id., § 533 (f)(1)(A).

limiting the number of subscribers. Under the rule, no single operator is permitted to pass more than 30 percent of homes. The rule's rationale is that if a single entity passes too many homes, it may unfairly impede the flow of programming to subscribers and to other video distributors.

Despite changed conditions, the goal of the ownership limit should remain the same. The Commission should establish reasonable limits on the number of subscribers that a single entity is authorized to reach in order to deter the entity from exercising monopsony power over programming or engaging in vertical foreclosure of the programming market.

In the Further Notice, the Commission proposes two steps to take account of the new circumstances. First, it would consider all MVPDs, not just cable, in the calculation. And second, the Commission would base its calculation on the number of subscribers, not the number of homes passed. Under the Commission's proposal, "in calculating a cable MSO's market share, the numerator would consist of the MSO's cable subscribers, and the denominator would consist of the total number of cable subscribers plus non-cable MVPDs nationwide."[23]

In support of the proposal, the Further Notice observes that the Commission has previously acknowledged "the growth of MVPDs other than cable operators and suggested that a true measure of horizontal concentration ought to take into account all MVPDs and MVPD subscribers, rather than cable operators and cable subscribers alone."[24] The test would work as follows. The numerator would consist of an MSO's subscribers. The denominator would be composed of cable subscribers and all other multichannel video subscribers. The relationship of the numerator to the denominator would result in percentages attributable to particular MSOs.

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23 Further Notice at para.79.

24 Id. at para. 80.

This calculation will enable the Commission to more effectively assess the market power of a single MSO over the entire programming market.

NCTA supports the Commission's proposed calculation. The homes passed standard was formerly an effective measure of horizontal concentration because the concentration levels of the cable industry were substantially coincident with the concentration levels associated with the overall multichannel marketplace. But now the homes passed test cannot account for actual subscribers, instead counting homes whether or not a customer subscribes to multichannel service. If the Commission were to maintain the homes passed test, it would not properly account for the presence of multichannel competition in its evaluation of horizontal concentration.

Changes in the competitive landscape anticipated in the near future should also be considered. One recent study, for example, predicted "DBS will continue strong growth and secure 22% of the multichannel video market by 2003."[25] The expected trend toward increased multichannel video competition confirms the need to measure horizontal concentration based on subscribers instead of homes passed

B. The Commission's Evaluation of Horizontal Limits Should Emphasize Antitrust Analysis

In 1993, the Commission perceived its adoption of the 30 percent horizontal ownership limitation as part of a package of protections intended to prevent cable operators from "exercising undue power vis-à-vis programmers and consumers."[26] It noted that cable operators were subject to program access, program carriage, channel occupancy, must carry and other

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25 "Promise of Local Channels Will Not Significantly Impact Industry Growth," Press Release, Jul. 21, 1998, www.strategisgroup.com/press/DBS2.html.

26 Supra n. 16, at 8577.

requirements. "The cumulative effect of these regulations coupled with a horizontal ownership limit of 30% should protect against any one cable system exerting undue power that could prevent the success of new programming services or 'unfairly impede the flow of video programming to the consumer.'"[27]

The 1993 decision on horizontal ownership, coupled with these other regulations, was too tight a limit. At 30 percent homes passed, and even at a significantly higher level of attributed horizontal ownership, a single cable MSO is not in a position to economically constrain the efficient workings of the competitive programming marketplace. Indeed, the Commission's decision considered comments by cable parties that argued on the basis of antitrust principles, that "MSOs must have at least a 50% market share to be regarded as having market power."[28]

The Commission committed in 1993 when it adopted the regulations to revisit them every five years. The Commission understood that changed conditions could warrant a reexamination of the limits. After five years, the Commission has had sufficient experience to reach a more realistic judgment that takes account of the changed conditions.

The horizontal ownership provision is intended to prevent an MSO controlling too many subscribers from restricting the flow of video programming to other distributors[29] or from impeding the flow of video programming to consumers.[30] In addition, the horizontal rule must

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27 Id.

28 Id. at 8575.

29 47 U.S.C. § 533(f)(2)(B).

30 Id., § 533(f)(2)(A).

take account of ownership patterns in the industry, the nature and market power of the local franchise and the various types of non-equity controlling interests.[31]

Congress also directed the Commission to consider *the benefits* of large holdings of subscribers by an MSO. As part of its rules the Commission must take account of "efficiencies and other benefits"[32] that might result from increased ownership or control. Congress also required that the regulations "reflect the dynamic nature of the communications marketplace."[33] Finally, the regulations must not "impair the development of diverse and high quality video programming."[34]

This balancing of potential pro- and anticompetitive factors need not lead to the immediate elimination of the requirement for some limit of ownership by a single MSO. But even if the Commission was to conclude that some limit is needed, it must be recognized that the horizontal ownership rule does not operate in isolation from other rules designed to achieve analogous purposes. As noted, the channel occupancy rule limits an MSO to carriage of affiliated programming on 40 percent of each system's channels. The retransmission consent and PEG access rules further constrain a cable's operator's freedom to select programming, as noted earlier.

Irrespective of these behavioral rules, the marketplace provides an effective and compelling constraint on potential anticompetitive behavior by a large MSO. Cable companies are in the business of persuading their customers to purchase subscriptions based upon the

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31 Id., § 533(f)(2)(C).

32 Id., § 533(f)(2)(D).

33 Id., § 533(f)(2)(F).

34 Id., § 533(f)(2)(G).

programming offered on their systems. It would be economically counterproductive--and, carried to its logical extreme, suicidal--for an MSO to deny its customers desirable programming. By doing so, the MSO would deny itself subscriber and advertising revenues. And, it would encourage customers to shift to alternative distribution media.

Indeed, cable operators have compelling incentives to bring desirable programming to the multichannel marketplace. By offering desirable programming, they increase the likelihood that existing customers will be satisfied and new customers will sign up for service.

In the event that the accumulation of horizontal ownership by a single MSO develops into a competitive problem, the Commission should emphasize the application of an antitrust-type approach. Indeed, the legislative history to the 1992 Act acknowledges that antitrust analysis is one method for evaluating horizontal ownership.[35] In light of the increasing level of multichannel competition, the Commission should emphasize antitrust analysis in its evaluation of horizontal limits.

The factors affecting network launches are more complicated in today's network-rich environment. Larger MSO size has not been shown to be a constraint and may be helpful in some cases. Placement of overly stringent restrictions on horizontal ownership may actually impede the development of new networks. Large MSOs are at the forefront of developments that hold the potential of transforming the communications marketplace.[36] The larger the MSO, the

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35 See Cable Television Consumer Protection and Competition Act of 1992, H.R. Rep. 628, 102 Cong., 2d Sess. 42 (notes traditional antitrust analysis should not be sole method of Commission analysis of horizontal concentration, plainly affording Commission discretion to apply antitrust analysis as one of factors).

36 There has been no evidence to demonstrate that large MSOs foreclose, rather than help launch new networks, despite the occasional "bigness is badness" rhetoric. Nor is the launch phenomenon limited to vertically integrated programmers. History Channel, Sci-Fi and Home and Garden are examples of unaffiliated, relatively new networks that have thrived under the current environment.

more likely it is that a new network can sign sufficiently large affiliation agreements to make launch more likely, even if the large MSO cannot and does not commit 100% of its subscribers. In short, there is no evidence that shows that smaller MSO size is correlated with more launches or that larger MSO size is correlated with fewer launches.

Apart from program-related concerns, size does matter, positively, in terms of efficiencies. As explained in Section I, by deploying digital compression techniques cable systems substantially expand capacity and increase their ability to deliver more services to consumers. Reorganizing cable franchises into large regional clusters increases scale economies and provides incentives for cable systems to establish technologically advanced operations. Convergence will offer consumers the benefits of one-stop shopping, and achieve the long-awaited goal of telecommunications competition.

To realize these goals, and to achieve these benefits, large MSOs must be freed from artificial, duplicative and overly restrictive regulatory constraints. Emphasizing antitrust analysis in the establishment of the horizontal limit is a critical step in that process. Therefore, the Commission, employing antitrust analysis, should raise the cap substantially beyond existing limits.

C. MSOs Should Be Allowed to Grow Beyond the Cap Without Requiring Divestiture

In addition to establishing a new mechanism for assessing horizontal concentration, and a new level of authorized ownership by a single MSO, the Commission should also adopt its proposal authorizing an MSO to grow internally beyond the limit. Requiring divestiture once a cap is reached because of internal growth penalizes an MSO for successfully marketing an improved service desired by consumers.