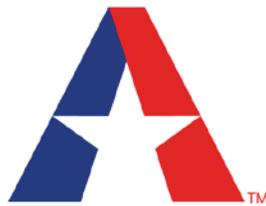


**Before the  
Federal Communications Commission  
Washington, D.C. 20554**

In the Matter of )  
 )  
Promoting the Availability of Diverse and ) MB Docket No. 16-41  
Independent Sources of Video )  
Programming )  
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 )

**COMMENTS**



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## SUMMARY

Imagine a small cable operator in a rural, small town in the Midwest offering broadband and video service. SmallTown Cable (a member of the American Cable Association) invests heavily in its broadband network. Its prices for broadband service have remained stable, and its broadband subscriber base grows year over year. Video service, however, has proven more challenging. SmallTown Cable has had to raise video prices because its programming costs have increased significantly (and remain much higher than those of its competitors). It has lost video subscribers in recent years, especially since customers can now obtain video service from sources other than MVPDs.

SmallTown Cable has two business imperatives that, as it turns out, align considerably with the Commission's program-diversity goals in this proceeding. First, like all MVPDs, SmallTown Cable wants to offer subscribers the most attractive programming it can at affordable prices. For example, SmallTown Cable wants to offer only three of MegaProgrammer's channels rather than having to carry multiple additional channels as the "price" for the three it wants—as MegaProgrammer requires it to do today. In fact, SmallTown Cable would like to replace one of MegaProgrammer's less desirable channels with the Hunting and Fishing Channel, an independent channel it is confident that its subscribers would prefer. Replacing MegaProgrammer's offering with that of an independent programmer obviously serves diversity interests.

Second, SmallTown Cable wants to emphasize its broadband business even at the expense of its traditional cable offering. (Some other small cable operators agree

with SmallTown Cable in this regard, but not all of them do.) Given the increases in its programming costs, SmallTown Cable has concluded that its best chance at long-term viability is tied to success as a broadband service provider. SmallTown Cable would thus like to continue to grow its broadband access business, and is increasingly indifferent to whether its customers obtain video online directly from programmers or aggregators like Netflix. At least in the long run, this imperative also serves diversity interests. An online video model potentially makes it easier both for subscribers to access independent programming and for independent programmers to gain a toehold in the market.

As things stand, however, the business imperatives of larger programmers and distributors are much less aligned with the Commission's diversity goals. To the contrary, these entities engage in a variety of activities that make it much harder for SmallTown Cable to provide its customers with diverse programming.

1. **Forced Bundling.** Large programmers require SmallTown Cable to take all of their programming as a package, rather than allowing SmallTown Cable to choose the programming its subscribers will want. If SmallTown Cable wants to carry the Awesome Channel because its subscribers want to see *The Awesome Monster Show*, for example, it must also take the Slightly Less Awesome Channel, the Not Really Awesome Channel, and the Downright Unpopular Channel. No questions, no exceptions. When SmallTown Cable (or its buying group) tells AwesomeCorp. that its subscribers only really care about *The Awesome Monster Show*, AwesomeCorp. says, in effect, "too bad." (This, of

course, is very different than what programmers tell *the Commission* on this subject.)

Such bundling by large programmers naturally harms SmallTown Cable's subscribers. It also harms diversity in at least three ways. First, it leaves less room on SmallTown Cable's limited-capacity system for diverse programming. Second, it prevents SmallTown Cable from transitioning system capacity from video to broadband, which makes it harder for subscribers to access diverse programming online. Third, as the Commission has repeatedly found, forced bundling of "must have" programming assets results in higher prices and more onerous terms and conditions. This, in turn, makes it more difficult for SmallTown Cable to find the resources necessary to acquire additional independent programming.

2. **Penetration Requirements.** Large programmers require SmallTown Cable to offer most of their networks to the overwhelming majority of its subscribers. Thus, not only must SmallTown Cable *buy* the Downright Unpopular Channel in order to get the Awesome Channel, but it must also offer the Downright Unpopular Channel to the vast majority of its subscribers. As a result, SmallTown Cable's "Expanded Basic" tier might more accurately be characterized as "Super Expanded Basic," a bloated, overly expensive tier full of channels of marginal interest.

Penetration and other similar distribution requirements—and the resulting Super Expanded Basic tier—also harm diversity. If subscribers have to spend more money to purchase the expanded basic tier, they are less likely to then also

purchase additional tiers where independent programmers can be found. Super Expanded Basic also prevents SmallTown Cable from attracting “cord shavers,” who would like to subscribe to some over-the-top video services while retaining a slim bundle of key broadcast and cable programming.

3. **Most-Favored Nation Clauses (“MFNs”).** Some large MVPDs have entered into exceptionally detailed MFNs with independent programmers that prevent these programmers from reaching agreement with SmallTown Cable. For example, one diverse programmer received broad distribution with BigMVPD Co. along with a distribution-specific MFN provision. This provision precluded the diverse programmer from allowing SmallTown Cable to carry it on a specialty tier, which was the only place where SmallTown Cable could affordably do so.

4. **Imposing Programming Costs on Broadband Access.** Some SmallTown Cable broadband subscribers enjoy “Sports3,” the online-only streaming service offered by SportsNet, a popular cable sports network. Sports3 offers live sporting events not available on SportsNet itself or any other outlet. SmallTown Cable broadband subscribers receive Sports3 only because SmallTown Cable pays SportsNet an access fee, which it does only because Sports3 occasionally carries games of local interest. So every SmallTown Cable broadband subscriber pays for Sports3—even though only some of them want or actually watch it. If SmallTown Cable stopped paying the fee, however, *none* of its broadband subscribers could access Sports3—no matter how much they wanted or would pay for it. This is the cable model transposed onto the Internet, which ACA has referred to as “cablization of the Internet.”

More recently, another large programmer proposed that SmallTown Cable pay for broadcast stations and other traditional cable programming based on the number of its broadband subscribers, rather than based on the number of its video subscribers. SmallTown Cable has successfully resisted such proposals so far, but does not know whether it can continue to do so.

If widely adopted, both cablization of the Internet and the more recent cable-programming accounting gimmicks threaten to impose programming costs on broadband access. Rather than purchasing broadband access and then having flexibility to subscribe to the broadband video content of their choice, SmallTown Cable's subscribers would have to pay programming fees in order to receive broadband at all. The broadband future, in other words, would become much like the cable present—with all of its flaws. Such a regime, were it to materialize, would make it harder and more expensive for SmallTown Cable's customers to access diverse and independent programming online.

SmallTown Cable is fictitious, as are the Awesome Channel, MegaProgrammer, or Sports3. Yet SmallTown Cable's story reflects the experience of ACA members who see increasing threats to diverse programming. If the Commission hopes to encourage program diversity in a meaningful way, it will have to address these issues—beginning with forced bundling and penetration requirements.

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**COMMENTS**



The American Cable Association (“ACA”)<sup>1</sup> submits these comments in response to the Notice of Inquiry issued by the Commission in the above-captioned proceeding.<sup>2</sup>

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<sup>1</sup> ACA represents nearly 750 small and medium-sized cable operators, incumbent telephone companies, and municipal utilities. ACA members offer video, broadband, and voice services. These providers offer service to homes and businesses in smaller communities and rural areas, as well as in urban and suburban areas by overbuilding other providers. These providers pass nearly 19 million homes in all 50 states and many U.S. territories, and serve about 7 million of them. More than half of ACA’s members serve fewer than 1,000 subscribers each.

<sup>2</sup> *Promoting the Availability of Diverse and Independent Sources of Video Programming*, Notice of Inquiry, FCC No. 16-19, MB Docket No. 16-41 (rel. Feb. 18, 2016) (“*Notice*”). Throughout these comments, we refer to facts as “reported” by ACA members or others. The programming agreements entered into between ACA members and large programmers invariably contain stringent confidentiality provisions. See *CBS Corp. v. F.C.C.*, 785 F.3d 699 (D.C. Cir. 2015). ACA’s small cable operator members also understandably fear retaliation from large programmers. That said, ACA members can document each of the

As discussed below, the actions of large players in the video market—including the biggest programming conglomerates and the largest multichannel video programming distributors (“MVPDs”)—threaten the diversity interests at the heart of this proceeding.

More specifically, these comments describe the following:

- How small cable operators obtain programming, and how their business imperatives align with the Commission’s program-diversity goals.
- How “forced bundling” by large programmers harms program diversity.
- How penetration and similar distribution requirements by large programmers harm program diversity.
- How most-favored nation clauses (“MFNs”) entered into by large MVPDs can hinder program diversity.
- How imposing programming costs on broadband access threatens program diversity.

If the Commission truly wishes to advance the diversity goals set forth in the *Notice*, it should address these practices—beginning with forced bundling and penetration requirements.

## **I. SMALL CABLE OPERATORS CAN CONTRIBUTE POWERFULLY TO PROGRAMMING DIVERSITY.**

The Commission states that “[a] central objective of multichannel video programming regulation is to foster a diverse, robust, and competitive marketplace for the delivery of multichannel video programming.”<sup>3</sup> Specifically, the Commission seeks

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factual claims made in these comments, and would be pleased to do so if ordered by the Commission and under an appropriate protective order. Also, ACA has worked with the National Cable Television Cooperative (“NCTC”) in the preparation of these comments, as ACA members are also members of NCTC. Accordingly, when we refer to factual assertions from “ACA members” herein, we intend to include NCTC even though NCTC itself is not an ACA member.

<sup>3</sup> *Notice* ¶ 2 (citing statutory provisions).

to enhance diversity by “eliminating or reducing any barriers faced by independent programmers in reaching viewers.”<sup>4</sup> Of course, ACA’s independent small and mid-sized cable operators<sup>5</sup> themselves add substantially to “diversity in the evolving video marketplace.” They can also promote the diversity provided by independent programmers, if allowed to do so. To explain how, we first describe how small cable operators typically obtain programming, and then show how their business imperatives align with the diversity interests advanced in this proceeding.

**A. Small Cable Operators Obtain Programming Directly and Through Buying Groups.**

Larger cable operators, satellite carriers, and large telco providers obtain the rights to offer programming by dealing directly with cable networks and broadcast stations. That is, they enter into programming contracts allowing them to carry national cable networks such as ESPN and TNT and regional sports networks like Comcast SportsNet,<sup>6</sup> they enter into retransmission consent agreements to carry popular local

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<sup>4</sup> *Id.* The Commission defines an “independent video programmer” or “independent programmer” for purposes of this proceeding as “one that is not vertically integrated with a [multichannel video programming distributor or] MVPD.” *Id.* ¶ 1 n.44. ACA suspects, however, that the Commission may not have intended to treat large media conglomerates like Disney and Fox as “independent” or “diverse” programmers. While “diversity” and “independence” may mean different things to different observers, such enterprises do not need the Commission’s protection. In any event, for these purposes, we use the terms “independent programmer” and “diverse programmer” interchangeably.

<sup>5</sup> *About Us*, AMERICAN CABLE ASSOCIATION, [http://www.americancable.org/about\\_us](http://www.americancable.org/about_us) (last visited Mar. 24, 2016).

<sup>6</sup> See 17 U.S.C. § 106(4) (providing holders of copyright in “motion pictures and other audiovisual works” with the exclusive right to publicly perform such works).

broadcast stations,<sup>7</sup> and they receive must-carry elections from other local broadcast stations.<sup>8</sup>

ACA's small and mid-sized cable operators obtain most of their national cable programming, however, through the National Cable Television Cooperative ("NCTC").<sup>9</sup> NCTC negotiates standardized master agreements with programmers and allows its members to opt into them. Because NCTC acts as an interface between programmers and its members, it allows the programmer to deal with a single entity for purposes of negotiating contracts, determining technical standards, billing for payments, and collecting payments, along with other matters. Programmers benefit from working with NCTC because it reduces their transaction costs of dealing with small and medium-sized MVPDs so that they are comparable to the transaction costs of dealing with a single large MVPD. NCTC members benefit because they receive lower rates (sometimes significantly lower) than they would receive through direct deals, although the rates even NCTC can negotiate remain higher than those negotiated by the largest MVPDs in the market.<sup>10</sup>

Two aspects of NCTC's activities are particularly relevant to this proceeding. First, in order to opt into an NCTC master agreement, a small cable operator must

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<sup>7</sup> See 47 U.S.C. § 325(b)(1)(A) (prohibiting an MVPD from retransmitting a broadcast signal without the originating station's consent).

<sup>8</sup> See *id.* §§ 534 (cable carriage of commercial stations); 535 (cable carriage of noncommercial educational stations); 338 (satellite carriage).

<sup>9</sup> See generally *Revision of the Commission's Program Access Rules*, 27 FCC Rcd. 12605, ¶¶ 85 *et seq.* (2012) (describing NCTC's and ACA's advocacy with respect to how the program access rules treat buying groups).

<sup>10</sup> Comments of the American Cable Association, MB Docket No. 12-68, at 2-3 (filed Dec. 17, 2012).

accept the agreement in its entirety—generally including bundling and penetration requirements.<sup>11</sup> Thus, if NCTC’s master agreement with Fox contemplates carriage of multiple networks on the expanded basic tier, a small cable operator must generally agree to carry all of those networks on expanded basic in order to opt in. And it will almost certainly opt in, as it is highly unlikely to negotiate a better deal on its own.<sup>12</sup>

Second, NCTC for a variety of reasons has not negotiated master agreements for some of the most valuable local and regional programming, including broadcast stations and regional sports networks. Small cable operators that wish to carry such programming must arrange to do so directly. This, in turn, can give large programmers considerable additional leverage over small cable operators and NCTC alike.<sup>13</sup>

**B. Small Cable Operators’ Business Imperatives Align with the Diversity Objectives in This Proceeding.**

Small cable operators exist in an increasingly difficult video marketplace.<sup>14</sup> They all compete against well-capitalized entities such as AT&T/DIRECTV and DISH, and in

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<sup>11</sup> For more details with respect to penetration requirements for the lowest-bandwidth cable systems, please see discussion *infra* Part II.B.

<sup>12</sup> An individual small cable operator, of course, has essentially zero leverage against a large programmer. Its carriage or non-carriage of a large programmer’s channels represents no more than a rounding error for the large programmer.

<sup>13</sup> Most NCTC members do not operate in areas served by broadcast stations owned and operated by Disney, Fox, or NBCU. Some of the largest NCTC members do. And most NCTC members do operate in markets served by RSNs owned by Fox or NBCU. As a condition of obtaining programming directly, some programmers will require small cable operators to “extend” their NCTC master agreements to a date after that agreement actually expires with large, pre-set rate increases. This reduces what small amount of leverage NCTC might have in subsequent negotiations with that programmer because, if the programmer fails to reach an agreement with NCTC, it will maintain carriage on those systems with which it has negotiated such an extension. When a large programmer thereby gains additional leverage against NCTC, the programmer may use this leverage to extract higher fees and more onerous carriage and penetration requirements.

<sup>14</sup> See, e.g., Comments of the American Cable Association, MB Docket No. 15-158 (filed Aug. 21, 2015) (“ACA 2015 Video Competition Comments”); American Cable Association, “High

some cases other terrestrial broadband and video providers as well. They pay an increasing amount for programming, often significantly more than their larger competitors. This is reducing their video margins toward zero—or worse.<sup>15</sup> In part because of these difficulties, however, they face two business imperatives that align considerably with the Commission’s diversity interests in this proceeding.<sup>16</sup>

**1. ACA Members Seek to Carry Independent and Diverse Programmers.**

ACA members seek to provide the widest range of the most attractive programming to their subscribers (consistent with any capacity constraints they face) at affordable prices. This, of course, can mean many things; indeed, it means different things to different small cable operators, each of which serves a unique subscriber base.<sup>17</sup> ACA members overwhelmingly believe, however, that they serve their subscribers better when they can choose programming independently of ownership considerations. In many cases, they would choose channels offered by independent programmers over secondary channels offered by large ones. In nearly *all* cases, they would choose higher rated or lower cost independent programming over the lowest-rated large-programmer offering.

Independent programmers offer several advantages to ACA members. To begin with, they often offer a better price-to-value ratio for their programming than the

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and Increasing Video Programming Fees Threaten Broadband Deployment” (Apr. 2015), *attached to ACA 2015 Video Competition Comments* (“ACA Video Study”).

<sup>15</sup> ACA Video Study at 6-8.

<sup>16</sup> *Notice* ¶ 3 (seeking comment on the state of the marketplace for independent programmers).

<sup>17</sup> See *infra* Part II.A (describing the particular interests of rural small cable operators).

secondary and tertiary channels of large programmers. They can also help ACA members serve important demographic audiences. This, in turn, can help ACA members differentiate themselves to their subscribers from larger national MVPDs. More broadly, diverse and independent programmers provide an important competitive alternative to programming owned by the largest media conglomerates. Their mere existence can help regulate the prices charged by large programmers, and can provide alternatives in the event the large programmer withdraws its programming. As an “institutional” matter, therefore, an ACA member might favor independent programming over large-programmer channels of equal cost, if allowed to do so.

For these reasons, ACA members and NCTC have long championed independent programming. NCTC has entered into agreements with numerous independent video programmers. Many of these agreements are popular with NCTC’s members—to the extent they are able to opt into them (as discussed in more detail below). Indeed, NCTC and ACA members represent a significant source of distribution for independent programmers. Taking into account small independent video programmers that have been acquired by large programmers over the years, the number of independent networks that have been supported by NCTC and ACA members is even greater.

For example, smaller MVPDs strongly support the Outdoor Channel, which carries content that is virtually tailor-made for the subscribers of many of ACA’s small rural operator members. The independent station is carried by over 770 NCTC members, which represents more than 90 percent of all its members. Moreover, NCTC

members in the aggregate represent about 15 percent of Outdoor Channel's total subscribers—making NCTC one of the network's largest channels of distribution today.

## **2. ACA Members Seek to Transition to Broadband Video, Which in the Long Term Will Promote Independent Programming.**

Small cable operators' business imperatives align with the Commission's diversity interests in another way: Economic challenges in the *video* marketplace have led many of them to prioritize their *broadband* service.<sup>18</sup> As part of their increasing focus on broadband, such providers seek to serve those who want online video services as a supplement to or replacement for their cable service. In other words, many small cable operators have increasingly focused on growing their broadband business even when doing so comes at the expense of their traditional cable offerings.

Small cable operators will have even stronger incentives to continue this change in emphasis over time. In a study prepared with the assistance of Cartesian<sup>19</sup> and filed with the Commission last summer, ACA showed that increases in video programming costs have made the video business less profitable—or even unprofitable—for small cable operators.<sup>20</sup> That study suggested that, given current conditions, video margins for the average smaller cable operators generally would become negative by 2020.<sup>21</sup>

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<sup>18</sup> Of course, promoting broadband deployment generally is one of the Commission's most important goals. See, e.g., *Protecting and Promoting the Open Internet*, 30 FCC Rcd. 5601, ¶ 2 (2015) (describing the “virtuous cycle” that drives innovation and investment on the Internet—both at the ‘edges’ of the network, as well as in the network itself”).

<sup>19</sup> See *Our Story*, CARTESIAN, <http://www.cartesian.com/about-us/our-story/> (last visited Mar. 24, 2016).

<sup>20</sup> ACA Video Study at 3, 4-8.

<sup>21</sup> *Id.* at 7 (“If we assume that the current market trends for programming costs and multichannel video revenues continue, video margins for smaller-scale MVPDs will become negative by 2020.”).

The number of small, video-only cable systems that have ceased providing service in recent years corroborates this evidence.<sup>22</sup>

That study also looked at the effect of these declining margins on broadband deployment. Under the current trajectory, “the business case for broadband deployment for all use cases<sup>23</sup> would be expected to decline and eventually become unprofitable in the coming decade,”<sup>24</sup> with rural expansion being “the most vulnerable due to the high cost of building out new broadband.”<sup>25</sup>

The only scenario the study found consistent with expanded broadband deployment—and, correspondingly, the scenario that appears most likely to lead to long-term viability—is a “broadband-centric” strategy. Under such a strategy, “broadband becomes the central product for consumers in the triple play bundle in place of multichannel video.”<sup>26</sup> While providers would continue to provide some MVPD packages, subscribers would primarily receive their programming online. They would, in other words, pay their Internet Service Provider (“ISP”) for connectivity, and then purchase the bulk of their video programming directly from programmers or program aggregators, such as Netflix.

A growing number of small cable operators have begun to transition to a broadband-centric model. Indeed, a handful have abandoned video altogether. The

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<sup>22</sup> ACA 2015 Video Competition Comments at 2-3.

<sup>23</sup> “Use cases” include “rural expansion,” “new fiber overbuild,” “telco fiber overbuild,” and “suburban incumbent expansion.” ACA Video Study at 9.

<sup>24</sup> *Id.* at 13.

<sup>25</sup> *Id.*

<sup>26</sup> *Id.* at 15.

executive of one such operator explained his choice simply: “[T]he TV model is broken.”<sup>27</sup> Others have taken more measured steps. As Wave Broadband’s CEO put it, while the company continues to sell traditional cable packages, it now focuses on “what [it] can do to help customers get online, go get content directly from the content owner and pay that content owner directly.”<sup>28</sup> Indeed, Wave has reported that one of its most popular offerings today is “a broadband connection and a Roku box.” Wave and other ACA members have also worked with TiVo in order to offer their customers a set-top box that integrates their traditional MVPD service with online video services.<sup>29</sup> Another group of ACA members now makes available local broadcast stations and some other independent stations to its customers via an app on a Roku box.<sup>30</sup>

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<sup>27</sup> Shalini Ramachandran, *More Cable Companies Take TV Off Menu*, WALL ST. J. (Oct. 3, 2014), <http://www.wsj.com/articles/more-cable-companies-take-tv-off-menu-1412120310> (quoting BTC President Scott Floyd) (“Ramachandran”).

<sup>28</sup> Tony Lenoir, *Q2 Steady, but Red Flags in Future Outlook for Video Margins*, SNL KAGAN (Aug. 8, 2014), [www.snl.com/interactivex/article.aspx?id=28833656&KPLT=6](http://www.snl.com/interactivex/article.aspx?id=28833656&KPLT=6). Tom Might, chief executive of CableOne, explained his company’s own move to focus on broadband: The “trends are kind of hard to fight. . . . Better to join them and make your profit where the business is growing.” Ramachandran, *supra* note 32.

<sup>29</sup> See Letter from Ross Lieberman to Marlene Dortch, MB Docket No. 15-64, at 2-3 (filed Feb. 11, 2016) (describing Suddenlink, RCN, Grande Communications, Atlantic Broadband, General Communications Inc., Astound, CableOne, Blue Ridge Communication, Mediacom, Midcontinent, Vyve Communications, Wave Broadband, Entouch, Armstrong, Frontier Communications, WOW!, and NCTC as having entered into deals with TiVo). Grande Communications’ president described these steps as “enabl[ing] our viewers to easily navigate, search and discover content from across traditional television channels, the Internet and our own VOD library in a simple, intuitive fashion that is unlike anything else available on the market.” *Id.* at 2.

<sup>30</sup> See, e.g., *EZVideo*, CANBY TELCOM, <https://www.canbytel.com/television/ezvideo/> (last visited Mar. 24, 2016); *TV Services*, POLAR COMMUNICATIONS, <http://www.polarcomm.com/residential/television/> (last visited Mar. 24, 2016); *Rainbow MyTV*, RAINBOW COMMUNICATIONS, <http://rainbowtel.net/services/rainbow-mytv> (last visited Mar. 24, 2016); *GMA Video*, WAITSFIELD AND CHAMPLAIN VALLEY TELECOM, <http://www.wcvt.com/services/internet/gma-video/> (last visited Mar. 24, 2016).

To be sure, no ACA member seeks to emphasize broadband service over cable service in order to serve diversity interests. Those who have started the transition from cable-centric to broadband-centric service have done so because they believe in the business case for such a transition.<sup>31</sup> In addition to its advantages for ACA members, however, this transition also offers great potential for independent programmers and for the diversity interests identified by the Commission.<sup>32</sup>

To begin with, broadband video provides subscribers with access to a vast universe of programming, as opposed to the programming chosen by the MVPD. This alone serves diversity interests. Moreover, such a model promises to make it easier for independent and niche programmers to gain a toehold, at least in the long run. No longer would a niche channel need to secure carriage from large MVPD before it could reach an audience and start building a critical mass of subscribers. Rather, immediately upon launch, it would have a potential audience of everyone with a broadband connection. As Chairman Wheeler explained only last week:

Diversity of voices is [an] area where our digital networks have been a game changer. Our open broadband ecosystem has democratized the media landscape and given innovative new content creators a way to find their audiences outside of the established distribution systems.<sup>33</sup>

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<sup>31</sup> As a Cincinnati Bell executive put it earlier this month, “[w]e would rather go to broadband, a much higher-margin product [than video].” *ACA Summit: Cincinnati Bell Sounds ‘Skinny’ Gong*, MULTICHANNEL NEWS (Mar. 2, 2016), [www.multichannel.com/news/distribution/aca-summit-cincinnati-bell-sounds-skinny-gong/403008](http://www.multichannel.com/news/distribution/aca-summit-cincinnati-bell-sounds-skinny-gong/403008).

<sup>32</sup> *Notice* ¶ 3.

<sup>33</sup> Tom Wheeler, *Empowering Small Businesses to Innovate in Today’s Digital Economy*, FCC (Mar. 25, 2016), <https://www.fcc.gov/news-events/blog/2016/03/25/empowering-small-businesses-innovate-today%E2%80%99s-digital-economy>.

Chairman Wheeler also echoed Commissioner Clyburn, who pointed to the importance of expanded broadband in the Commission’s most recent Section 257 Triennial Report to Congress, stating “the Internet is the great equalizer for minorities and women who have struggled for a foothold in the traditional media and other businesses.”<sup>34</sup> The Writers Guild put it similarly:

The online video market has been a necessary competitive development, increasing choice and flexibility for consumers. For writers, it has brought forth new buyers for their content and ideas, as well as the opportunity to distribute content directly to the public. This has had a positive effect on the diversity of information available to the public because the traditional entertainment industry is controlled by a handful of companies, which has limited diverse and independent content.<sup>35</sup>

The Writers Guild cited the growth of online distributors such as Netflix—and the amount those entities can spend on “independent sources in direct competition with television networks”—as positive aspects of online video.<sup>36</sup>

Independent programmers have already shown the promise of an online video distribution model. For example, Crunchyroll, a San Francisco-based startup, enters licensing agreements with television networks and studios in Japan to provide translated versions of Japanese anime.<sup>37</sup> In most American cable markets, this niche programming is unlikely to appeal to a broad enough audience to make carriage of this

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<sup>34</sup> *Id.* (quoting Statement of Commissioner Mignon L. Clyburn, *Section 257 Triennial Report to Congress Identifying and Eliminating Market Entry Barriers For Entrepreneurs and Other Small Businesses*, 26 FCC Rcd. 2909, 2970 (2011)).

<sup>35</sup> Petition to Deny of Writers Guild of America, West, MB Docket No. 15-149, at 23 (filed Oct. 13, 2015).

<sup>36</sup> *Id.*

<sup>37</sup> *About Crunchyroll*, CRUNCHYROLL, <http://www.crunchyroll.com/en/about> (last visited Mar. 14, 2016).

content worthwhile. Yet Crunchyroll currently has 750,000 paid subscribers worldwide, streams 1.5 billion minutes of video every month, and is now branching out to provide programming to underserved audiences, such as the global audience for Korean drama.<sup>38</sup>

Of course, there are limits to the relationship between online video and diversity interests. ACA also understands that, in today's environment, many independent programmers may still want, or even need, "linear" carriage on traditional video platforms.<sup>39</sup> We do not suggest otherwise. We do, however, suggest that this may decreasingly be the case as online video continues to supplement, or even replace, traditional video.

## **II. FORCED BUNDLING HINDERS SMALL CABLE OPERATORS FROM OFFERING DIVERSE PROGRAMMING.**

From ACA's perspective, the forced bundling requirements imposed by large programmers present perhaps the biggest impediment to program diversity. Concerns about the pernicious effects of forced bundling are not new: As ACA noted as early as 2008, "[w]hen dealing with small and medium-sized cable companies, owners of 'must have' satellite channels almost invariably tie or bundle those channels with less desired (or *undesired*) channels."<sup>40</sup> More recently, ACA's advocacy has focused on the

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<sup>38</sup> Lauren Orsini, *Crunchyroll Leads by Example: The Future of Streaming Video is Niche*, FORBES (Jan. 13, 2016), <http://www.forbes.com/sites/laurenorsini/2016/01/13/crunchyroll-leads-by-example-the-future-of-streaming-video-is-niche/#7787b76a7d9c>; Janko Roettgers, *Crunchyroll launches new Korean Drama site KDrama.com*, GIGAOM (Feb. 20, 2014), <https://gigaom.com/2014/02/20/crunchyroll-launches-new-korean-drama-site-kdrama-com>.

<sup>39</sup> See *Notice* ¶ 14 (seeking comment on whether online carriage is a viable business model).

<sup>40</sup> See, e.g., Comments of the American Cable Association, MB Docket No. 07-198, at 5-6 (filed Jan. 3, 2008) ("ACA Tying Comments").

bundling of two *desired* channels, such as a network-affiliated broadcast station with a regional sports network or a suite of national cable networks.<sup>41</sup> In each case, ACA has cited the harmful effects of forced bundling on consumers and its members.<sup>42</sup> Forced bundling, however, also harms the diversity interests at issue in this proceeding—especially when applied against smaller cable operators. Below, we first describe the prevalence of forced bundling, and then explain the various ways in which forced bundling harms program diversity.

**A. Large Programmers Impose Increasingly Stringent Forced Bundling Requirements.**

Eight years ago, ACA described a world in which a handful of large programmers “tied” their popular programming to undesired programming.<sup>43</sup> Back then, “the rights to distribute 13 of the most powerful channels [were] tied to or bundled with obligations to distribute at least 60 other channels.”<sup>44</sup> Claims of standalone offers from programmers were “illusory.”<sup>45</sup>

Bundling remains just as problematic today. NCTC reports that it has negotiated master agreements with nine of the largest media groups, namely Disney/ESPN, Fox, Comcast/NBCU, Turner, Viacom, AETN, AMC, Discovery, and Scripps. These agreements cover a total of 115 different individual networks. Of them, 65—or 57

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<sup>41</sup> See, e.g., Comments of the American Cable Association, MB Docket No. 15-216, at 15-33 (filed Dec. 1, 2015) (“ACA Good Faith Comments”).

<sup>42</sup> *Id.* at 14 *et seq.*, citing Michael H. Riordan, “Higher Prices from Bundling of ‘Must Have’ Programming Are Not Based on Competitive Marketplace Considerations” (Dec. 1, 2015) (“Riordan Bundling Paper”), *attached* thereto.

<sup>43</sup> ACA Tying Comments at iv-v, 8.

<sup>44</sup> *Id.* at iv (emphasis omitted).

<sup>45</sup> *Id.* at v, 13.

percent—must be bundled. Thus, an NCTC member that opts into deals with each of these large programmers must carry 65 networks at a minimum. Of course, few, if any, small cable operators actually *want* to carry all of these networks. Indeed, as one ACA member explained, a programmer can sometimes leverage a single very popular *show* (*The Walking Dead*) into carriage of multiple *networks* of varying subscriber interest (AMC, WE tv, BBC World News, BBC America, SundanceTV, and IFC).<sup>46</sup> Once a small cable operator agrees to put a bundled network on a system, moreover, it is almost impossible for the operator to enter into a subsequent deal that does not require continued carriage of the bundled network—no matter how few people watch it.

In the aggregate, forced bundling results in cable operators carrying more programming by large programmers than by independent and diverse programmers. NCTC members collectively provide bundled programming to 310 million subscribers (counting each of the 65 bundled network’s subscribers separately) and independent programming to only 56 million subscribers (again, counting each of the 72 independent

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<sup>46</sup> This member’s explanation corresponds with concerns raised by more than 200 small and medium-sized cable operators during NCTC’s negotiations with AMC in 2015. See Letter of Small Operators to FCC Chairman Wheeler, MB Docket No. 15-158, at 1 (filed Dec. 17, 2015) (“AMCN insists all cable operators distribute five services (IFC, WEtv, Sundance, BBC World News, and BBC America) in order to carry their single network with meaningful ratings”) (emphasis omitted). It is also consistent with press reports about the final AMC/NCTC agreement. See Mike Farrell, *AMC, NCTC Reach Agreement*, MULTICHANNEL NEWS (Jan. 4, 2016), <http://www.multichannel.com/news/networks/amc-nctc-reach-agreement/396228> (“AMC said the NCTC deal includes all six of its networks – AMC, IFC, WeTV, Sundance, BBC America and BBC World News.); see also Dow Jones Business News, *Small Cable Firms Go Without AMC’s Channels as ‘Walking Dead’ Returns*, NASDAQ (Feb. 23, 2016), <http://www.nasdaq.com/article/small-cable-firms-go-without-amcs-channels-as-walking-dead-returns-20160223-01035#ixzz44HkTNzN2> (“Though the flagship AMC channel’s distribution declined due to the drops, its smaller sister networks WE tv, IFC, SundanceTV and BBC America, will add subscribers thanks to new channel-distribution requirements AMC won as part of the deal.”).

network's subscribers separately). On a network-by-network basis, the difference is just as stark. To take just one example, the bundled SEC Network has more than three times the number of NCTC subscribers than does the independent Pac-12 Network.

Merely comparing NCTC's figures, however, does not tell the entire story. Those figures do not, for example, reflect multicast bundling, where network-owned and affiliated broadcast stations force small cable operators to carry largely valueless secondary channels, such as rerun-focused MeTV,<sup>47</sup> Heroes & Icons,<sup>48</sup> and Decades.<sup>49</sup> Nor do they reflect "first on" requirements, under which a cable operator does not have to bundle now, but cannot launch any new programming without first launching additional networks from the large programmer.

Programmers, for their part, assure the Commission that they never force distributors to accept bundles. Rather, they claim that they always provide standalone offers for must-have channels that reflect those channels' real market value.<sup>50</sup> Bundles,

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<sup>47</sup> *MeTV Shows*, METV, <http://www.metv.com/shows/> (last visited Mar. 24, 2016).

<sup>48</sup> *Heroes & Icons Shows*, HEROES & ICONS, <http://www.heroesandiconstv.com/shows/> (last visited Mar. 24, 2016).

<sup>49</sup> *Decades Schedule*, DECADES, <http://www.decades.com/#schedule-section> (last visited Mar. 24, 2016).

<sup>50</sup> See, e.g., Reply Comments of Fox Entertainment Group, Inc. and Fox Television Stations, Inc., MB Docket No. 10-71, at 13 (filed June 3, 2010) ("Fox makes all of its programming services available for purchase to all MVPDs—both large and small—on a stand-alone basis, and always offers MVPDs reasonable rates, terms and conditions in exchange for carriage."); Comments of NBC Universal, Inc. and NBC Telemundo License Co., MB Docket No. 07-198, at 39 (filed Jan. 4, 2008) ("NBCU is also willing to offer its non-broadcast networks on a standalone basis (except with respect to the HD simulcast versions of its SD networks) if requested by the operator at a rate that reflects the market value of those networks on a standalone basis."); Comments of the ABC Television Affiliates Association *et al.*, MB Docket No. 15-216, at 42 (filed Dec. 1, 2015) ("ABC Affiliates Comments") ("Proposals for carriage of additional programming are bargaining proposals which an MVPD is free to accept, reject or counter with a proposal of its own. No MVPD is forced to accept a 'bundle' of programming.") (internal quotations and emphasis omitted).

they assert, are merely more efficient alternatives to standalone offers.<sup>51</sup> That comes as news to ACA members, which report that the vast majority of programmers refuse to provide standalone offers at all.

On the rare occasions that programmers do set out their purported standalone rates, moreover, ACA members report that all such rates were the same as or even higher than the price of the programmer's entire bundle. Such offers were invariably made, moreover, with essentially no substantiation of the economics involved from the programmer's perspective. Such offers were, in other words, intended not to be accepted—and, as far as ACA is aware, none of them were accepted. The bundle was the only real option provided. To use a parallel standard from labor law,<sup>52</sup> those offers forced the cable operator to “choose between acceptance of [the bundle] and an alternative that the [programmer] knows the [cable operator] cannot live with.”<sup>53</sup>

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<sup>51</sup> See *Notice* ¶ 16 (“[Programmers] maintain that, through the bundling of programming, MVPDs have the option of obtaining valuable programming at discounted prices.”). For the most recent version of this argument, see, for example, Comments of 21st Century Fox, Inc., MB Docket No. 15-216, at 12 (filed Dec. 1, 2015); Comments of the Walt Disney Company, MB Docket No. 15-216, at 19 (filed Dec. 1, 2015).

<sup>52</sup> *N.L.R.B. v. Borg-Warner Corp., Wooster Div. of Borg-Warner Corp.*, 356 U.S. 342, 349 (1958) (“[G]ood faith does not license the employer to refuse to enter into agreements on the ground that they do not include some proposal which is not a mandatory subject of bargaining . . . . [S]uch conduct is, in substance, a refusal to bargain about the subjects that are within the scope of mandatory bargaining.”).

<sup>53</sup> *Lathers Local No. 42 of the Wood Wire & Metal Lathers Int’l Union*, 223 N.L.R.B. 37, 42 (1976); see also *S. California Pipe Trades Dist. Council No. 16 of the United Ass’n*, 167 N.L.R.B. 1004, 1009 (1967) (where “the counterproposals advanced by [the party that had been insisting on a non-mandatory subject] were so extreme as to preclude a reasonable expectation of acceptance [such] that the ostensible choice they offered was illusory,” the party was in effect continuing to insist on the non-mandatory subject even though it had been removed from the counterproposal, and the party thus failed to bargain in good faith).

In sum, forced bundling involves exactly the same techniques as it did eight years ago when ACA most extensively reported on it and remains as prevalent as it has ever been. As discussed below, this harms independent programmers for many of the same reasons it harms ACA member subscribers.

**B. Forced Bundling Harms Program Diversity.**

Forced bundling obviously harms ACA members and their subscribers, which is why ACA has fought against it for so long. It also, however, threatens the diversity interests at issue here. As described in more detail below, forced bundling takes up valuable “shelf space” on capacity-constrained systems that might be used for independent programming or broadband. It also raises the price of programming generally, making it more expensive for subscribers to obtain diverse programming.

**1. Forced Bundling Takes Up Valuable Capacity on Capacity-Constrained Systems.**

As ACA has demonstrated over the years, many small cable operators have limited capacity. Forced bundling, however, occurs for all but the most capacity-constrained systems. More specifically, NCTC reports that some (but not all) of its agreements with large programmers provide some limited relief for the very lowest-bandwidth systems. These exemptions do not apply to many other systems that are “capacity constrained” by any reasonable definition of the term. Indeed, as ACA members explain, any moderate-bandwidth system that has not yet gone all digital, and that offers both a competitive number of HD channels and high speed broadband

service, quickly becomes “capacity constrained”—but most such systems do not qualify for the relief cited by NCTC.<sup>54</sup>

Forced bundling, then, causes an obvious diversity problem for such systems: Bundled channels take up a large portion of the cable operator’s limited “shelf-space” and prevent it from carrying other, diverse programming. One ACA member, for example, reports that essentially all of its capacity for television programming is devoted to bundled offerings. Another member, who has already converted a 550 MHz system entirely to digital, reports that it is at capacity and now is being forced to make expensive upgrades just to find space for bundled channels it does not even want.

ACA members unanimously report that this limits their ability to carry diverse and independent programmers. One member, for example, tells independent programmers “all the time” that, because of the space taken by large programmer bundles, there is “no room left” for them. Others describe having been compelled to drop diverse channels that had loyal viewers and fit well with the particular demographics of the subscriber base. Diverse networks that have paid the price for the bundling demands of large programmers include Outside Television, UP, MAV TV, The Blaze TV, ONE World Sports, Entertainment Studios, and beIN Sports.<sup>55</sup> Independent programmer ONE World Sports, for its part, confirms these reports: Small cable operators routinely tell it

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<sup>54</sup> Some of this limited capacity, moreover, is often devoted to analog service. Since an analog channel takes up as much as twelve times the bandwidth as a digital standard-definition channel, and as much as four times the bandwidth of a digital high-definition channel, analog or hybrid-analog systems face particularly difficult capacity challenges.

<sup>55</sup> ACA members report having dropped the following independent networks for a variety of different reasons, including but not limited to forced bundling: Blue Highways, Family Net, Retirement Living, GSN, Weatherscan, WFN, Go!TV, Sportsman Channel, AXS TV, ION, ION Life, qubo, Pivot (formerly Halogen).

that they cannot carry the channel because bundled programming has taken up all of their shelf space.

The loss of diversity caused by forced bundling sometimes cuts especially deep for two reasons. First, the bundled channels sometimes duplicate one another. For example, Viacom's Teen-Nick is largely composed of re-aired shows from Viacom's Nickelodeon.<sup>56</sup> Second, the bundled programming often fails to serve the particular needs of the communities served by the small cable operator. Many ACA members, for example, serve rural areas. They thus tend to seek programming tailored to rural needs and interests. Forced bundling, however, requires them to offer the same homogenized programming offerings in rural areas as do urban cable systems. The more space these members must give begrudgingly to offerings such as the Esquire Network, which targets the "more upscale, affluent, urban-dwelling guy,"<sup>57</sup> the less is available for channels like the World Fishing Network that subscribers actually want to watch.<sup>58</sup> Similar disconnects arise with sports programming, with several ACA members pointing to ESPN's nationwide forced bundling of its SEC Network in this regard. The SEC Network devotes its programming to the athletic exploits of the Universities of Alabama,

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<sup>56</sup> On March 24, 2016, for example, TeenNick was dominated by long blocks of reruns of *Ned's Declassified School Survival Guide*, *Big Time Rush*, *iCarly*, and *Victorious*, all shows that originally aired on Nickelodeon. See *TeenNick Schedule*, TEENNICK, <http://www.teenick.com/shows/tvschedule/> (last visited Mar. 24, 2016).

<sup>57</sup> Brian Steinberg, *Esquire Network Seems Out of Style on TV Scene*, VARIETY (June 7, 2013), <http://variety.com/2013/tv/news/esquire-network-seems-out-of-style-on-tv-scene-1200493866/>.

<sup>58</sup> See WORLD FISHING NETWORK, <http://www.worldfishingnetwork.com/> (last visited Mar. 30, 2016).

Kentucky, Tennessee, and other Southeastern Conference member institutions.<sup>59</sup>

Many viewers in other parts of the country—such as those in the footprints of the Big 10 or Pac-12 conferences—do not want to pay for the SEC Network. They certainly do not want to lose hometown programming in order to make room for the SEC Network.

Small cable operators could, theoretically, increase their capacity in order to make room for more video programming. It makes little economic sense, however, for small cable operators to make such significant investments in video upgrades when their margins for video programming are small, or even negative.<sup>60</sup> Rather, it makes more sense for them to invest in broadband<sup>61</sup>—but, as discussed in more detail below, penetration requirements can make *that* more difficult as well.<sup>62</sup>

Just as forced bundling takes up shelf space that might be used to provide independent programming directly, it also takes up shelf space that might be used to provide higher performance broadband service.<sup>63</sup> As discussed above, many small cable operators seek to gradually increase the amount of system capacity devoted to broadband in order to offer faster speeds and remain viable in the long term.<sup>64</sup> One

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<sup>59</sup> *About the Southeastern Conference*, SEC SPORTS, <http://secsports.go.com/article/11067695/about-the-sec-conference> (last visited Mar. 29, 2016).

<sup>60</sup> ACA 2015 Video Competition Comments at 3-4 (reporting that ACA members continue to close systems and face severely eroding video margins).

<sup>61</sup> ACA Video Study at 28 Table 4.

<sup>62</sup> See *infra* Part III.B.2.

<sup>63</sup> See *Shentel will lose AMC Networks*. SHENTEL (Dec. 22, 2015) <https://www.shentel.com/news/2015/december/amc%20channel%20drops> (noting that adding unwanted AMC networks “to our lineup would not benefit our customers and it could impact our ability to enhance broadband capacity.”).

<sup>64</sup> See *supra* Part I.B.

ACA member reports, for example, that bandwidth allocated to high-speed broadband has quadrupled over the past three years, because consumer behavior has evolved rapidly. The move to such a model, moreover, promises to increase subscribers' access to diverse programming.<sup>65</sup> To the extent ACA members must devote capacity to carrying large programmers' third, fourth, and fifth channels, they cannot repurpose this capacity for broadband.

## **2. Forced Bundling Raises Prices, Making It Harder for Even High-Capacity Systems to Offer Diverse Programming.**

The problems described above relate principally to limited-capacity systems. Even with respect to systems with capacity to spare, however, the economics of forced bundling harms diversity interests. As the Commission has repeatedly found, bundling of two sets of desirable programming raises programming costs by increasing the cost to the distributor of failing to reach agreement.<sup>66</sup> In the *Comcast-NBCU* proceeding, for example, ACA argued that Comcast could extract higher prices by bundling its regional sports networks with NBC's broadcast stations or NBCU's suite of national cable networks. In support of this claim, it demonstrated that the joint negotiation of separately owned, same-market big four network-affiliated broadcast stations increased the price that the broadcasters could have obtained in separate negotiations by at least 20 percent.<sup>67</sup> In light of evidence presented by ACA and others, as well as its own

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<sup>65</sup> *Id.*

<sup>66</sup> ACA has made such a showing most recently in the good-faith negotiation proceeding. See generally ACA Good Faith Comments; see also Riordan Bundling Paper at 11-16.

<sup>67</sup> *Comcast Corp., Gen. Elec. Co., and NBC Universal, Inc.*, 26 FCC Rcd. 4238, ¶ 137 (2011) ("*Comcast-NBCU Order*"); William Rogerson, "Economic Analysis of the Competitive Harms of the Proposed Comcast-NBCU Transaction," at 14-17 (June 21, 2010), *attached to* Comments of the American Cable Association, MB Docket No. 10-56 (filed June 21, 2010);

independent findings,<sup>68</sup> the Commission allowed MVPDs to elect arbitration for individual “must have” programming assets rather than the bundle.<sup>69</sup>

Again citing ACA’s submissions, the Commission reached a similar determination more recently in prohibiting same-market “top four” stations from jointly negotiating retransmission consent. There, the Commission found:

Analyses in the record draw on basic economic principles to explain why coordinated conduct such as joint negotiation results in higher retransmission consent fees: [I]f two broadcasters can collectively threaten to withdraw their signals unless they are each satisfied, then they will be able to negotiate higher fees for everyone than if each broadcaster can only threaten to withdraw its own signal unless the broadcaster is satisfied.... [I]t is the ability to threaten collective withdrawal that creates the power to raise retransmission consent fees.”<sup>70</sup>

This proposition had “been validated in other economic contexts” and was “also reflected” in Federal Trade Commission and Department of Justice merger and collaboration guidelines, the Commission noted.<sup>71</sup> Nothing about this insight is specific to broadcasters, RSNs, or any particular genre of programming. Rather, it applies more

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*see also* William Rogerson, “A Further Economic Analysis of the Proposed Comcast-NBCU Transaction,” at 23-27 (Aug. 19, 2010), *attached to* Reply Comments of the American Cable Association, MB Docket No. 10-56 (filed Aug. 19, 2010).

<sup>68</sup> *Comcast-NBCU* Order, App. B. ¶¶ 54-55 (“We test ACA’s claim that the combination of RSNs and local affiliates of major broadcast networks leads to higher programming charges by analyzing the change in affiliate fees following the integration of a Fox O&O broadcast station and a Fox RSN in the same local market under the joint ownership of News Corp relative to a control group of RSNs not under joint ownership with a broadcast station... The results generally support the conclusion that joint ownership of these two types of programming assets in the same region allowed the joint venture to charge a higher price for the RSN relative to what would be observed if the RSN and the local broadcast affiliate were separately owned.”).

<sup>69</sup> *Id.* ¶ 57.

<sup>70</sup> *Amendment of the Commission’s Rules Related to Retransmission Consent*, 29 FCC Rcd. 3351, ¶ 14 (2014).

<sup>71</sup> *Id.* (“DoJ has recognized that collaboration by competing broadcast stations could ‘harm competition by increasing the potential for firms to coordinate over price or other strategic dimensions, and/or by reducing incentives of firms to compete with one another.’”).

broadly: when programmers force the bundling of two popular blocks of programming, they can raise prices.

When large programmers raise prices through bundling, they harm diversity by making it harder for small cable operators to purchase independent programming. Several ACA members have suggested that there are only “so many dollars in the system” for programming. From an economic perspective, this means that the carriage of the bundled programming raises the marginal cost of carrying the independent programming. Thus, to take one example, suppose an ACA member located in the Pacific Northwest values the SEC Network at \$1.50 per subscriber and values the Pac-12 Network at \$3.00. If forced to carry the SEC Network, however, it may value the Pac-12 Network at only \$0.50, either because it believes subscribers will not want to pay for two specialized sports channels, or because carrying both channels reduces the profits from the cable operator’s broadband service by reallocating bandwidth. In such a scenario, the ACA member might well choose not to carry the Pac-12 Network at all. This, in fact, is how ACA members tell us they actually behave. One ACA member put it succinctly: “We have not launched channels because there is only so much cost I can pass on to customers.”

“Budgets,” of course, work the other way as well. ACA members report that, when they find themselves with additional room in their budgets—such as when they fail to reach agreement with a large programmer for bundles—they are able to carry more independent programmers. For example, when CableOne was forced to remove Viacom channels last year, it announced that it expected to add channels such as The

Blaze, Hallmark Channel, TV One, “and more.”<sup>72</sup> CableOne’s channel lineups suggest that it indeed did so.

Exacerbating this “budget” problem—and making it more difficult yet for small cable operators to afford independent programming—are the incentives for vertically integrated programmers to charge artificially high prices to ACA members. As the Commission has repeatedly found,<sup>73</sup> vertically integrated programmers tend to negotiate more aggressively with rivals<sup>74</sup> of their distribution affiliates. This is because the integrated firm takes into account the possibility that any harm from failure or delay in reaching agreement would be offset to some extent by a benefit to the affiliated distributor. Likewise, negotiating a higher price raises the costs of its distribution rivals. “The higher opportunity cost for selling its programming due [to vertical integration] gives [the vertically integrated programmer] a greater incentive to raise the prices for its programming to rival MVPDs.”<sup>75</sup> Indeed, vertical integration can result in price increases for the entire suite of bundled programming—even if no individual network is considered “must have.”<sup>76</sup> While this is not necessarily a bundling problem in and of itself, the two largest vertically integrated programmers—Comcast/NBCU and

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<sup>72</sup> *Viacom Channels Removed From Cable ONE Lineup*, CABLEONE (Mar. 31, 2014), <http://www.cableone.net/AAU/pressrelease/Pages/ViacomChannelsRemovedfromCableONELine-Up.aspx>.

<sup>73</sup> Comments of the American Cable Association, MB Docket No. 14-57, at 15-16 (filed Aug. 25, 2014) (“ACA Comcast-TWC Comments”); Gary Biglaiser, “The Harms of Comcast-TWC-Transaction,” at 5-24 (Aug. 25, 2014), *attached thereto as Exhibit A* (“Biglaiser”).

<sup>74</sup> See ACA Comcast-TWC Comments at 17-19 (describing competitive overlap of Comcast and Charter systems with ACA member systems).

<sup>75</sup> Biglaiser at 5-6.

<sup>76</sup> *Comcast Corp., Gen. Elec. Co. and NBC Universal, Inc.*, 26 FCC Rcd. 4238, ¶ 47 (2011) (concluding that vertical integration of the suite of NBCU’s national cable networks would “allow Comcast-NBCU to extract higher rents from MVPDs”).

Discovery—sell their networks as a bundle. And vertical integration unquestionably amplifies the harms bundling causes to independent programmers.

### **III. PENETRATION REQUIREMENTS HINDER SMALL CABLE OPERATORS FROM OFFERING DIVERSE PROGRAMMING.**

Large programmers also harm diversity interests by requiring small cable operators to carry channels on more highly penetrated tiers than the interest in those channels would support. By imposing such penetration requirements, programmers have increased the size and cost of the expanded basic tier—which, in turn, makes it difficult for subscribers to purchase independent programming on higher tiers for which expanded basic is a prerequisite. Such requirements also make it more difficult for customers to subscribe to broadband video services as a complement to their cable television service.

#### **A. Large Programmers Impose Increasingly Stringent Penetration Requirements.**

ACA and its members have long objected to the way penetration requirements limit their flexibility to provide the channels their subscribers actually want at an affordable price.<sup>77</sup> Penetration requirements nonetheless remain exceedingly problematic. ACA members report that each of the largest programmers insists on distribution to the vast majority of a small cable operator's subscribers for many, if not all, of its networks. They do so either by naming the tier on which to be carried ("expanded basic" or "the most penetrated tier other than broadcast basic"), by naming

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<sup>77</sup> See, e.g., ACA Tying Comments at 14-17; Letter from Edward Yorkgitis, Jr. to Marlene Dortch, MB Docket No. 14-57, at Attach. (filed Feb. 18, 2015) (describing penetration requirement-related concerns with the proposed Comcast-Time Warner Cable merger).

a minimum percentage of subscribers to receive the programming, or through some similar mechanism.

Some programmers enforce their penetration requirements by insisting on minimum payments. Thus, for example, a programmer may insist that a small cable operator pay as if it offered a channel to 85 percent of its subscribers, even if its expanded basic tier reaches only 80 percent of its subscribers. Others are more draconian, enforcing heavy penalties for noncompliance. Some programmers—particularly regional sports networks—even resist “carving out” the broadcast basic tier from their penetration requirements. In such circumstances, if too many subscribers choose the broadcast basic tier, a small cable operator must move the channel in question into that tier to meet penetration requirements—or pay as if it had done so.<sup>78</sup> More exotic variations on this theme exist as well. One might be called a “penetration MFN”: a requirement that, if an operator moves any competitor’s programming onto a more highly penetrated tier, it must do the same for the large provider’s programming.

These penetration requirements have become pervasive. One ACA member, for example, reported that AMC insisted on carriage of all of its networks, including its lesser watched ones, on the highest non-basic tier. Another ACA member singled out Fox as a particularly egregious offender, remarking that the member is “[u]nable to grow our business in a meaningful way and create choice because of our Fox deal.” And, as with bundling requirements, ACA members report that penetration requirements are presented as *faits accomplis*. That is, programmers do not offer ACA members

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<sup>78</sup> If the small cable operator moves the channel into broadcast basic, moreover, MFNs may require it to move other programmers’ channels into broadcast basic as well, compounding the effect.

additional value in exchange for penetration requirements, or the choice to offer less penetration in exchange for other consideration. Either the cable operator accepts the demanded penetration levels or it does not get the desired programming—period.

ACA members, moreover, report that the problem is getting worse. They describe a uniform strategy by large programmers of “taking less penetrated product and driving it into the expanded basic tier.” Thus, they report, almost every renewal with a large programmer results in new additions to expanded basic—a tier that might more accurately be described as “Super Expanded Basic.”

## **B. Penetration Requirements Harm Diversity.**

Like forced bundling, penetration requirements harm diversity in several ways. First, they can make purchasing independent programming more expensive for subscribers by larding up, and increasing the cost of, the more basic tiers. Second, they discourage broadband video as a supplement to traditional cable service.

### **1. Penetration Requirements Make It More Difficult for Subscribers to Afford Independent Programming.**

Penetration requirements harm diversity by making it more difficult for subscribers to afford independent programming. This, in part, is because of how MVPDs package their programming (and how they are required to do so by large programmers). Generally speaking, subscribers must purchase lower tiers as prerequisites to purchasing higher tiers. Thus, a subscriber must purchase “broadcast basic” in order to receive “expanded basic,” and must purchase “expanded basic” in order to receive a higher, specialty tier. Independent networks, of course, can most often be found on less penetrated tiers because they lack the leverage to command carriage on more highly penetrated tiers.

All things being equal, the more channels required to be in an expanded basic tier, the more expensive the tier will likely be,<sup>79</sup> as MVPDs pass on the higher programming costs to subscribers.<sup>80</sup> The higher price may discourage subscribers from purchasing the Super Expanded Basic tier, thus precluding them from also purchasing independent programming offered on a higher tier. Subscribers will also likely have less demand for higher-tiered independent channels due to what economists call “substitution” and “income” effects. Under the substitution effect, if Super Expanded Basic channels are partial substitutes for the independent programming on a higher tier, the independent programming will be less valuable to subscribers, who therefore will be less inclined to purchase it. Under the income effect, the more expensive Super Expanded Basic tier will reduce consumers’ disposable income. If consumers have to spend more on Super Expanded Basic, they will have less to spend on an additional tier with independent programming.

The income effect, of course, should particularly concern the Commission here. It suggests that subscribers with the least resources face the greatest constraints in their ability to access diverse independent programming. To the extent the Commission

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<sup>79</sup> To the extent programmers can force their channels onto the *broadcast basic* tier, the problem compounds for ACA members and their subscribers. The Copyright Act and implementing regulations requires cable operators to pay statutory copyright royalties on “the full amount of monthly (or other periodic) service fees *for any and all services or tiers of services that include one or more secondary transmissions of television or radio broadcast signals*, for additional set fees, and for converter fees.” FORM SA3, General Instructions, at vii, <http://copyright.gov/forms/sa3.pdf>. Cable operators must, in other words, pay royalties on fees for the broadcast basic tier *even if it includes non-broadcast channels*.

<sup>80</sup> See, e.g., *AT&T Inc. and DIRECTV*, 30 FCC Rcd. 9131, ¶ 290 (2015) (discussing pass through of programming costs).

concludes that independent programmers particularly benefit lower-income populations, this concern becomes even more acute.

Programmers, for their part, have suggested that penetration requirements can reduce the cost of programming because they typically charge less for more widely distributed programming.<sup>81</sup> This may or may not be true.<sup>82</sup> If so, however, this does not address the “Super Expanded Basic” problem, which concerns price of the entire tier, not the price of any individual program on the tier. ACA is unaware that programmers have ever claimed that they would charge more for *expanded-basic* channels if not allowed to place *other* channels on expanded basic—they have suggested only that they would charge more for those other channels. Even if programmers were to charge more for individual channels taken off expanded basic, the result might well be better for subscribers and programmers alike. Subscribers might well prefer a cheaper expanded basic tier and the option to purchase other channels they might want on an a la carte basis or on very limited tiers—even if those other channels were more expensive individually than they would be on the Super Expanded Basic tier. From the perspective of independent programmers, moreover, such a regime would be far preferable for the reasons discussed above.

Certainly, the anecdotal evidence supports the idea that the Super Expanded Basic phenomenon correlates with higher prices. According to the Commission’s data,

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<sup>81</sup> *Report on the Packaging and Sale of Video Programming Services to the Public*, FCC, at 22-23 (Med. Bur. rel. Nov. 18, 2004); Comments of Charter Communications, Inc., MB Docket No. 04-207, at 6-10 (filed July 15, 2004).

<sup>82</sup> Comments of the Walt Disney Company, MB Docket No. 07-198, at 64-67 (filed Jan. 4, 2008).

expanded basic grew from 44 channels in 1995 to 160 channels in 2013.<sup>83</sup> And the average price of expanded basic increased from \$22.35 to \$64.41 over the same period, representing a compound annual growth rate of 6.1 percent.<sup>84</sup> Conversely, those few providers who have managed to offer slimmer basic bundles (Verizon<sup>85</sup> and Cincinnati Bell,<sup>86</sup> for example) have offered lower prices. (One of these providers, however, received a lawsuit for its trouble.<sup>87</sup>)

## 2. Penetration Requirements Discourage Cord Shaving.

Penetration requirements also harm diversity indirectly by preventing small cable operators from attracting subscribers who want to subscribe to broadband video as a complement to their cable television service. Again, small cable operators increasingly seek to emphasize a “broadband-centric” service even at the expense of their traditional

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<sup>83</sup> *Implementation of Section 3 of the Cable Television Consumer Protection and Competition Act of 1992*, 29 FCC Rcd. 5280, ¶ 19 Table 4 (2014) (“2014 Cable Price Report”). Despite this increase in the number of channels on expanded basic, research suggest that consumers actually watch the same number of channels that they always have. *Advertising & Audience: State of the Media*, NIELSEN MEDIA (May 12, 2014), <http://www.nielsen.com/us/en/insights/reports/2014/advertising-and-audiences-state-of-the-media.html>.

<sup>84</sup> *2014 Cable Price Report* ¶ 17 Table 3.

<sup>85</sup> In April 2015, Verizon began offering Custom TV, a \$55 a month package containing 45 base channels and a customer’s choice of two small collections of channels organized by genre. Lucas Shaw, *Verizon Ushers in the Era of ‘Skinny Cable’*, BLOOMBERG BUSINESSWEEK (Apr. 30, 2015), <http://www.bloomberg.com/news/articles/2015-05-01/verizon-ushers-in-the-era-of-skinny-cable->.

<sup>86</sup> Cincinnati Bell is now offering a starter package of thirty-eight core channels, plus one “genre package” selected by the subscriber, for \$29.99. Jeff Baumgartner, *Cincinnati Bell Rings Up Slimmed-Down TV Packages*, MULTICHANNEL NEWS (Feb. 5, 2016), <http://www.multichannel.com/news/content/cincinnati-bell-rings-slimmed-down-tv-packages/397178>.

<sup>87</sup> See, e.g., Eric Gardner, *ESPN, Verizon Make Progress in Settling Lawsuit Over Custom TV*, HOLLYWOOD REPORTER (Feb. 23, 2016), <http://www.hollywoodreporter.com/thr-esq/espn-verizon-make-progress-settling-868908>.

cable service, and such a model promises to add considerably to program diversity.<sup>88</sup> Many subscribers, however, are not yet prepared to make a complete break from traditional cable.<sup>89</sup> For the moment, at least, they would prefer to engage in what has become known as “cord shaving” instead. That is, they want a slim bundle of broadcast and other key linear programming, supplemented by online sources for the rest.<sup>90</sup> When large programmers force small cable operators to offer Super Expanded Basic—and prevent them from providing a slim-bundle alternative—they preclude the most viable bridge between a cable-centric model and a broadband-centric one.<sup>91</sup>

Large programmers seem to understand this, at least when they talk about carriage of *other* programmers. AMC Networks CEO Josh Sapan, for example, recently stated that his company has “in its mindset a belief that there is no free ride in television”—ignoring that penetration requirements give his own networks a “free ride” compared to their independent network competitors.<sup>92</sup> CBS CEO Les Moonves also spoke against Super Expanded Basic when he noted that “people are tired of paying for things they don’t want to watch.”<sup>93</sup> He added:

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<sup>88</sup> See *supra* Part I.B.

<sup>89</sup> ACA Video Study at 3.

<sup>90</sup> *Id.* at 15.

<sup>91</sup> *Id.* at 14. Some subscribers can “cord-shave” by keeping only the broadcast basic tier. Many are unwilling to do so, however, without key cable programming like ESPN.

<sup>92</sup> David Lieberman, *Josh Sapan Q&A: AMC Networks CEO Sees Opportunities Amid TV’s Woes*, DEADLINE HOLLYWOOD (Aug. 24, 2015), <http://deadline.com/2015/08/amc-networks-josh-sapan-tv-challenges-1201502408/>. Sapan went on to damn with faint praise the networks AMC regularly forces cable operators to carry in high-penetration tiers, stating that those channels “are known, respected, if not adored, by the people who watch them.” *Id.*

<sup>93</sup> Jon Lafayette, *Moonves Endorses Streaming Skinny Bundles*, BROADCASTING & CABLE (Mar. 8, 2016), <http://www.broadcastingcable.com/news/currency/moonves-endorses-streaming-skinny-bundles/154424>.

Someone's going to figure out how to do this and how to give people what they want to watch and it's not for \$100 a month, it will be for \$35 or \$39 dollars a month where you'll really get the 12 to 15 or 18 channels that you care about. And not get the karate channel for 25 cents a month.<sup>94</sup>

Programmers, in other words, seem to agree that slim bundles are the future. None, however, wants to be the first mover, or can imagine that its own programming might not have a guaranteed place on any slim bundle.<sup>95</sup> As long as programmers continue to insist on penetration requirements for their own programming, ACA members will find it impossible to offer slim bundles—which, in turn, will make it harder for subscribers to access diverse programming.

#### **IV. MFNS CAN HINDER SMALL CABLE OPERATORS FROM OFFERING DIVERSE PROGRAMMING.**

In some circumstances, MFNs imposed by large MVPDs can also harm diversity. Independent programmers have argued that MFNs forced upon them by large MVPDs can prevent them from entering into agreements with smaller MVPDs, because the programmers cannot give the flexibility that smaller providers need.<sup>96</sup> ACA members

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<sup>94</sup> *Id.*

<sup>95</sup> Richard Greenfield, *TV Bundles Must Shrink or Consumers Will Leave Pay TV Ecosystem Altogether #goodluckbundle*, BTIG (Mar. 9, 2016), <http://www.btigresearch.com/2016/03/09/tv-bundles-must-shrink-or-consumers-will-leave-pay-tv-ecosystem-altogether-goodluckbundle/#ixzz44KKT5slW> (“[I]t’s amazing how all the programming executives are convinced that skinny bundles are going to happen, but are confident their set of key channels will be part of these smaller bundles and that these smaller bundles will be contained to a minority of total MVPD subscribers #goodluckbundle”) (available for registered users and on file with authors).

<sup>96</sup> *Notice* ¶ 7 (“Some parties claim that MVPDs’ insistence on MFN provisions precludes an independent programmer from making unique or innovative arrangements designed to achieve initial carriage of new programming, because those same unique terms could then be required to be extended to all MVPDs. They further argue that, given the proliferation of MFN provisions, an independent programmer that achieves some carriage is likely to have numerous MFN obligations, and that this can initiate a ‘domino effect’ when a single term in an agreement with one MVPD or OTT service triggers the MFN obligations in a programmer’s agreements with other MVPDs.”) (internal citations omitted).

tell a similar story. Several members report that one or more independent programmers have sought carriage on their systems, but have been unable to accept terms they otherwise would have accepted because of an MFN with a large MVPD.

ACA members obviously are not parties to the contracts between independent programmers and large MVPDs. Confidentiality provisions in those contracts, moreover, limit what independent programmers can divulge about them. Yet it is not difficult to see how problems might occur. Imagine that an independent programmer gains carriage with BigMVPD Co. on a highly penetrated tier in exchange for very low affiliation fees. Suppose that (as is often the case) BigMVPD Co. has obtained separate MFN protections in its contract with the independent programmer for a variety of specific provisions, including penetration requirements. Now suppose an ACA member is willing to offer the independent programmer more money but wants to offer the channel on a higher tier. The independent programmer cannot accept the ACA member's offer without risking demotion on the BigMVPD Co.'s system. The MFN, in other words, does not "recognize" the broader bargain that the independent programmer seeks to make with the ACA member. It recognizes solely that the ACA member has offered a better deal *with respect to penetration*, and thereby requires the programmer to offer the large MVPD the same penetration terms. This, of course, is just an example. Other varieties of MFNs can also operate to preclude small cable operators from carrying independent programmers. ACA Members have cited beIN

Sports and the Hallmark Channel as independent programmers that they could not carry because of MFNs.<sup>97</sup>

## **V. IMPOSING PROGRAMING COSTS ON BROADBAND ACCESS CAN HINDER PROGRAMMING DIVERSITY.**

In the longer term, imposing programming fees on retail broadband service can also harm the program-diversity interests at issue in this proceeding. Several years ago, ACA first described what it called the “cablization of the Internet” in the context of ESPN’s online-only offering, now known as ESPN3.<sup>98</sup> ESPN3 does not mirror ESPN’s cable network. Rather, it offers exclusive live sporting events<sup>99</sup> as well as reruns of events previously shown on ESPN itself.<sup>100</sup> For this service, ESPN charges ISPs based on the number of their broadband subscribers rather than charging subscribers directly. In other words, if a subscriber’s ISP has not paid for ESPN3, she cannot access the programming no matter how much she might be willing to pay for it. And if the ISP *has* paid, then she must pay for ESPN3 through her internet bill regardless of her interest.

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<sup>97</sup> ACA members also report that MFNs can bar emerging independent programmers, eager to generate momentum, from offering launch incentives such as initial free periods or reduced fees to smaller operators without offering them to large MVPDs, even though these same large MVPDs benefit from volume discounts not available to smaller operators.

<sup>98</sup> *E.g.*, Comments of the American Cable Association, GN Docket Nos. 09-47, 09-51, and 09-137 at 2-3 (filed Dec. 2, 2009) (“ACA NBP December Comments”).

<sup>99</sup> Most of these are of less interest to viewers, but, over the years, a handful of them have been of particular local interest—such a college football and basketball rivalries. See, *e.g.*, James Pilcher, *UC Fans Upset by Internet Blackout*, CINC. ENQ. at 1A (Jan. 24, 2009).

<sup>100</sup> ESPN3, [http://espn.go.com/watchespn/index/\\_/channel/espn3](http://espn.go.com/watchespn/index/_/channel/espn3) (last visited Mar. 29, 2016).

ACA raised concerns about the broader effects of such a payment model.<sup>101</sup> As ACA pointed out, the Internet has succeeded because of “[u]niversal and unfettered access to Internet content and services by consumers.”<sup>102</sup> Moreover, consumers benefit from having access to the Internet without having to incur costs for access to content that it does not want.<sup>103</sup> ACA worried that the “transposing of [programmers’] current business model to the Internet”<sup>104</sup> could threaten this success in numerous ways.<sup>105</sup>

Other than ESPN3 itself<sup>106</sup> and a handful of less successful services, programmers have so far avoided the “access fee” model. More recently, however, ACA members report that programmers have sought to peg fees for their traditional MVPD programming to the member’s number of broadband subscribers rather than its number of video subscribers. Of course, this does not involve the blocking of Internet content from subscribers of disfavored providers, as does the ESPN3 model.<sup>107</sup> And, as far as ACA is aware, none of its members have agreed to such terms. Were large

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<sup>101</sup> Comments of the American Cable Association, GN Docket No. 09-51 at 2-3 (filed June 8, 2009) (“ACA NBP June Comments”) (“Such a business model increases broadband prices for some, and decreases consumer choice for others.”).

<sup>102</sup> *Id.* at 4.

<sup>103</sup> *Id.*

<sup>104</sup> ACA Video Study at 15.

<sup>105</sup> ACA NBP June Comments at 5.

<sup>106</sup> *ESPN3 Participating Providers*, ESPN3, <http://espn.go.com/watchespn/affList> (providing a list of ESPN’s “participating providers”).

<sup>107</sup> Indeed, programmers have referred to such issues as merely “accounting.” See, e.g., ABC Affiliates Comments at 24 (“[T]he Commission should not prohibit broadcast stations from negotiating for payment based on signals viewed by an MVPD’s subscribers through the MVPD’s internet offering, rather than by means of the MVPD’s traditional video service. Just as with other substantive terms of a retransmission consent agreement, the definition of those ‘subscribers’ on the basis of which retrans fees are determined should be left to the parties to negotiate at arm’s length.”) (internal citations omitted).

programmers to insist on such arrangements, however, ACA members might not be able to hold out. If such arrangements became the norm, moreover, they could lead to many of the same ills associated with cablization of the Internet.

Today, Americans purchase broadband and broadband video separately. That is, they purchase broadband *access* from an ISP. They then purchase broadband *video* either *a la carte* from programmers (HBO GO or CBS All Access, for example) or from an online aggregator of such programming (Netflix or Hulu, for example). If programmers decide to make their online services available only through ISPs that pay “access fees,” programming fees would be “baked in” to broadband access fees. So too if they decide to charge each broadband subscriber for traditional cable programming. Either way, subscribers would have to pay for ABC, NBC, ESPN, and Fox in order to get broadband at all. And either payment model would impose the ills of today’s cable model on the Internet. Of most relevance to this proceeding, such a model would increase the price of broadband service dramatically. This, in turn, could make it more difficult for many subscribers to obtain more diverse programming.

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ACA would like to thank the Commission for opening a proceeding to examine program diversity. We recognize that a Notice of Inquiry, by definition, represents only the beginning of this examination. We cannot state strongly enough, however, that if the Commission seeks to encourage program diversity, it will have to address the issues discussed in these comments—starting with forced bundling and penetration requirements. We look forward to providing specific proposals for action as the record develops further.

Respectfully submitted,

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