W7C

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

In the Matter of	)	
	)	
Amendment of Section 73.658(g)	)	Docket No. 00-108
of the Commission's Rules —	)	
The Dual Network Rule	)	

COMMENTS OF VIACOM INC.

Anne C. Lucey
Vice President for Regulatory Affairs
Viacom Inc.
1501 M Street, N.W.
Suite 1100
Washington, DC 20005
(202) 785-7300

Richard E. Wiley
Lawrence W. Secrest
Marjorie J. Dickman
of
Wiley, Rein & Fielding
1776 K Street, N.W.
Washington, DC 20006
(202) 719-7000
Counsel for Viacom Inc.

September 1, 2000

TABLE OF CONTENTS

Page

I. INTRODUCTION AND SUMMARY 2

II. BACKGROUND: THE ORIGINS OF THE DUAL NETWORK RULE AND ITS ROLE IN TODAY'S HIGHLY COMPETITIVE MARKETPLACE 5

- A. The History Of The Rule 5
- B. The Network Television Business 10
- C. Today's Highly Competitive Video Marketplace 13
- D. The History And Distinctive Role Of UPN 20
  1. Since Its Creation, UPN Has Struggled to Build an Effective National Distribution Chain 21
  2. Notwithstanding Its Distinctive Programming Contributions, UPN Lags Well Behind the Other Networks in Audience Ratings and Is Not Self-Supporting 23
  3. Program Suppliers, Creative Personnel, and Numerous O&O and Affiliated Stations Are Financially Reliant on the UPN Network 24

III. THE PROPOSED RULE CHANGE WILL PROMOTE IMPORTANT PUBLIC INTEREST OBJECTIVES WITH REGARD TO PROGRAMMING 28

- A. Modification of the Rule Will Promote Overall Programming Diversity 29
  1. Economic Studies Are Virtually Unanimous In Recognizing That Common Ownership Creates the Incentive to Counterprogram In Order to Reach the Largest Possible Aggregate Audience 32
  2. The Commission Also Has Recognized the Incentive To Diversify Program Offerings Among Commonly-Owned Outlets 33

B. Modification of the Rule Will Potentially Increase the Total Amount of News and Public Affairs Programming Available to the Public 34

C. Modification of the Rule Will Promote Efficiencies That Strengthen The Programming Services of UPN, WB, and Their Affiliated Stations 36

D. The Combination of UPN and WB With a Major Network Would Not Cause Any Material Reduction In News/Public Affairs "Viewpoint" Diversity 37

IV. THE DUAL NETWORK RULE DISTORTS THE MARKETPLACE BY DIVERTING INVESTMENT AWAY FROM THE EMERGING UPN AND WB BROADCAST NETWORKS 42

V. THE PROPOSED RULE MODIFICATION WILL NOT IMPAIR COMPETITION IN ADVERTISING SALES 47

VI. THE RECORD IN THIS PROCEEDING SUPPORTS REPEAL OF THE DUAL NETWORK RULE IN ITS ENTIRETY, WITHOUT THE NEED FOR IMPOSITION OF SEPARATION REQUIREMENTS OR OTHER OPERATIONAL "SAFEGUARDS" 49

VII. CONCLUSION 51

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

In the Matter of Amendment of Section 73.658(g) of the Commission's Rules – The Dual Network Rule	))))))	MM Docket No. 00-108

COMMENTS OF VIACOM INC.

Viacom Inc. ("Viacom") hereby submits its comments in response to the *Notice of Proposed Rulemaking* ("*NPRM*") released by the Commission on June 20, 2000 in the above-captioned proceeding proposing to relax the dual network rule.[1] For the reasons set forth herein and in its previous comments in the Commission's 1998 Biennial Review proceeding,[2] Viacom strongly supports the Commission's proposal to modify the "dual network" rule, 47 C.F.R. § 73.658(g), by "eliminating the portion of the rule that precludes the ownership of the UPN or WB television networks by the ABC, NBC, CBS, or Fox television networks."[3]

[1] *In the Matter of Amendment of Section 73.658(g) of the Commission's Rules – The Dual Network Rule, Notice of Proposed Rulemaking*, MM Docket No. 00-108, FCC 00-213 (rel. June 20, 2000) ("*NPRM*").

[2] *In the Matter of 1998 Biennial Regulatory Review – Review of the Commission's Broadcast Ownership Rules and Other Rules Adopted Pursuant to Section 202 of the Telecommunications Act of 1996 ("Biennial Review Proceeding"), Comments of Viacom Inc.*, MM Docket No. 98-35 (filed Nov. 19, 1999) ("Viacom Comments"). Those Comments are hereby incorporated by reference.

[3] *NPRM* at ¶ 1. Indeed, the record before the Commission in this and earlier proceedings
(Continued...)

On May 4, 2000, Viacom acquired CBS Corporation ("CBS") pursuant to FCC approval granted May 3, 2000.[4] As a result, Viacom now owns and operates the CBS Television Network and the emerging United Paramount Network ("UPN").[5] In its decision approving Viacom's acquisition of CBS, the Commission granted a twelve-month period from the date of consummation of the transaction to allow Viacom to come into compliance with the dual network rule. However, in its recent *Biennial Review Report*,[6] the FCC subsequently found that the dual network rule (as applied to a combination of one of the four "major" over-the-air television networks and either of the UPN or WB "weblets") may no longer be in the public interest. Accordingly, the agency initiated this rulemaking proceeding to eliminate the portion of the rule that applies to the two emerging networks. For the reasons set forth herein, Viacom urges the Commission to act promptly to modify the dual network rule as proposed.

I. Introduction and Summary

Over the past decade, the Commission has examined the dual network rule on three separate occasions and – in each instance – has proposed that the rule should either be eliminated outright or substantially relaxed. Most recently, in the *NPRM*, the FCC has

---

(...Continued)
supports repeal of the dual network rule in its entirety. *See infra* Section VI.

[4] *In the Matter of Shareholders of CBS Corporation (Transferor) and Viacom Inc. (Transferee), Memorandum Opinion and Order*, FCC 00-155 (rel. May 3, 2000).

[5] Viacom previously held a 50% interest in UPN, but acquired the remaining 50% interest from a subsidiary of Chris-Craft Industries, Inc. on April 3, 2000.

[6] *Biennial Review Proceeding, Biennial Review Report*, MM Docket No. 98-35, FCC 00-191 (rel. June 20, 2000) ("*Biennial Review Report*").

proposed to repeal the aspect of the rule that applies to the emerging UPN and WB networks. In today's fiercely competitive video program marketplace, it is clear – beyond any serious possibility of challenge – that this aspect of the rule is no longer needed and, instead, frustrates important public interest objectives. Indeed, in his separate statement supporting the initiation of this proceeding, Chairman Kennard observed that there are "powerful reasons" in favor of modifying the dual network rule to end its application to UPN and WB.[7]

In particular, repeal of the "weblet" restriction will advance the following public interest goals and objectives:

- Promoting overall programming "diversity." Economics experts have long recognized that common ownership of media outlets promotes overall "diversity" in television programming. Thus, if two networks are owned by a single entity, the owner will have a strong incentive to "counterprogram" the two outlets – thereby increasing service to minority or "niche" programming tastes and interests.

- Increasing news and public affairs programming. A combination of an emerging network and a major network could create the potential that the news gathering and reporting resources of the larger entity might be re-deployed in ways that serve the viewers of the emerging network.

- Creating efficiencies that strengthen the program services of UPN, WB, and their affiliated stations. Viacom's ownership of CBS and UPN illustrates a wide variety of ways in which such combinations can promote efficiencies that strengthen an emerging network – and enhance the program services that can be offered by such entities and their affiliates.

- Enhancing the ability of the emerging broadcast networks to attract financial investment. The existing rule discriminates against UPN and WB and weakens their ability to attract capital investment. In particular, it channels Big Four network investment toward unregulated emerging broadcast networks (*e.g.*, PaxTV and, potentially, a "Fox II" network) – as well as cable networks and other so-called "alternative" media.

[7] *Id.* (Statement of Chairman William E. Kennard) at 3.

This latter point is especially important, given UPN's precarious financial position. The Commission is well aware that this network has experienced accumulated losses of some $800 million, could not be sold to Chris-Craft earlier this year for the incredibly low price of $5 million, and now is in danger of losing a large percentage of its affiliate base (as a result of the recently announced Fox/Chris-Craft deal). Under these circumstances, it is not at all clear that UPN would survive if the Commission failed to adopt the proposed rule change - and, thus, in effect, ordered Viacom to divest its ownership interest in the weblet.

The benefits noted above can be realized without incurring any significant countervailing "downside" - even in the special area of news and public affairs "viewpoint" diversity. This is true for three reasons: (1) the growth of alternative media outlets has diminished the importance of maintaining UPN and WB as independently owned network "voices"; (2) evidence suggests that common ownership of media outlets does not eliminate the editorial independence of those outlets; and (3) viewpoint diversity would not be advanced to any material degree by maintaining the existing restrictions on UPN and WB, because these financially struggling entities do not carry regularly scheduled network news and public affairs programming.

It is also apparent that a network merger involving UPN or WB would not generate significant negative consequences in the sale of advertising. The advertising marketplace in which they compete is extremely competitive. Indeed, in addition to the broadcast networks, this marketplace most assuredly includes advertising-supported cable networks, as well as syndication and local television advertising sales. UPN and WB hold relatively small shares of the advertising sales in this huge marketplace. Moreover, given the fact that these emerging networks serve distinctive audience tastes and demographic groups, there is now (and, in the future, would be) relatively little direct competition in advertising sales between UPN or WB and a commonly owned Big Four partner. Further, if one of these networks were eliminated, there would be an overall decline in the supply of advertising time.

Accordingly, the Commission should move with dispatch to repeal the existing restrictions on UPN and WB. Indeed, the evidence as discussed herein makes clear that the dual network rule *in its entirety* is anachronistic, outdated, and overdue for repeal.

II. Background: The Origins of the Dual Network Rule and Its Role in Today's Highly Competitive Marketplace

A. The History of the Rule

The original dual network rule, first adopted 59 years ago, prohibited a radio station from affiliating with an entity that maintained two or more radio networks. The FCC's policy goals at that time were expressed as "maximizing diversity" and "encouraging competition."[8] The regulation was based on the 1941 Report on Chain Broadcasting, which set forth the Commission's general concern that dual networking would allow the major networks to obtain "too much market power."[9] In 1946, the rule was applied to the infant television broadcasting industry, as the Commission itself has noted, "without additional analysis or comment."[10]

---

[8] *In the Matter of Review of the Commission's Regulations Governing Programming Practices of Broadcast Television Networks and Affiliates*, *Notice of Proposed Rulemaking*, 10 FCC Rcd 11951, 11955 (1995) ("*Review of Network Rules*").

[9] *Id.* at 11967.

[10] *Id.* at 11953 (citing *Amendment of Part 3 of the Commission's Rules,* 11 Fed. Reg. 33 (Jan. 1, 1946)).

The FCC repealed the dual network rule with respect to radio in 1977, due to the tremendous increase in the number of radio stations, the lessening economic importance of networks, and changes in the nature of radio programming.[11] By 1992, when the Commission again took up the subject of the dual network rule, this time for television, there had been substantial growth and tremendous change in the television broadcasting industry.[12] Yet the network regulations had not kept pace with the changing times. Indeed, the Commission observed as much, noting that there had been rapid growth in the number of multichannel service providers, such as cable and satellite network services (which are not subject to the rule). Moreover, the agency recognized that these non-broadcast network operators "enjoy certain economies of scale and marketing advantages."[13] Consequently, "broadcast networks seeking to become multichannel service providers have confronted certain regulatory barriers to doing so, and those barriers appear to have channeled the networks' activities into non-broadcast enterprises."[14]

More specifically, the Commission noted that, because the rule proscribed the maintenance of two *broadcast* networks, broadcasters were funneling their resources into non-off-air media. For example, the agency noted that NBC operated CNBC, and that Capital Cities/ABC (now Disney/ABC) had acquired a substantial interest in the ESPN and A&E cable

---

[11] *In the Matter of Review of the Commission's Regulations Governing Television Broadcasting, Notice of Proposed Rulemaking*, 7 FCC Rcd 4111, 4117 (1992) ("*Review of Television Rules*"); *Review of Network Rules* at 11954.

[12] *See infra* Section II.C.

[13] *Review of Television Rules* at 4117-18.

[14] *Id.* at 4118.

networks.[15] As a result, the dual network rule (which was intended to promote the development of new over-the-air networks) was having precisely the opposite effect, to the detriment of its primary intended beneficiaries — the estimated 30 percent of American households who received their television service exclusively over-the-air. Therefore, out of concern that it not "perpetuate unnecessary regulations that impede the competitive ability" of television stations and networks, the Commission proposed to eliminate the dual network rule in its entirety.[16]

---

[15] *Id.* Since 1992, each of the networks has expanded its cable presence. NBC now has interests in ValueVision, Inc. and A&E Television Networks, which operates A&E and The History Channel. NBC also owns CNBC and now operates MSNBC in partnership with Microsoft. General Electric Capital Corp. Annual Report, SEC Form 10-K (Mar. 17, 2000); Additionally, NBC owns a 25% interest in Rainbow Media Holdings, Inc., whose cable networks include AMC, Bravo, Independent Film Channel, Much Music, Madison Square Garden Network (regional), Fox Sports Net (Rainbow Media owns 50 percent), and Romance Classics. *Rainbow* (visited Aug. 14, 2000) <http://www.rainbow-media.com/philosopy/present.html>.

Disney/ABC now owns the Disney Channel and Toon Disney, as well as 80 percent of ESPN, Inc., which operates ESPN, ESPN2, Classic Sports Network, and ESPNEWS; 37.5 percent of A&E Television Networks, which operates A&E and The History Channel; 50 percent of Lifetime Entertainment Services, which operates Lifetime Television and Lifetime Movie Network; and 39.6 percent of E! Entertainment Television, which also operates Style. The Walt Disney Co. Annual Report, SEC Form 10-K (Dec. 21, 1999).

Similarly, Fox now has investments in ten U.S. cable programming services: Fox News Channel, Fox Sports, The Golf Channel, Speed Vision, Outdoor Life, Fox Family Channel, Fox Kids Network, FX, FXM and The Health Network. Fox's parent, News Corp., has an interest in Rainbow Media as well. Fox Entertainment Group, Inc. Annual Report, SEC Form 10-K (Sept. 27, 1999); *Fox Entertainment Group* (visited Aug. 14, 2000) <http://www.newscorp.com/public/irfox/report99/cover,highlights,chart/orgchart.html>.

Prior to Viacom's acquisition of CBS, CBS had also entered into the cable arena, with The Nashville Network (TNN) and Country Music Television (CMT). CBS Corp. Annual Report, SEC Form 10-K (Mar. 29, 2000).

[16] *Review of Television Rules* at 4113. Significantly, the Commission concluded that repeal of

(Continued...)

Three years later, in a separate 1995 rulemaking proceeding, the FCC again questioned whether network regulations, including the dual network rule, "are necessary to achieve [the twin goals of promoting competition and development of new networks] or, conversely, whether the rules increase the costs of networking without producing any real benefits."[17] As it had in the 1992 proceeding, the Commission observed that some network regulations, including the dual network rule, "now operate to inhibit development of new broadcast networks and discourage innovation."[18] After reiterating its earlier conclusion that the dual network rule was no longer justified, the Commission called for additional comment as to how repeal of the regulation could result in "economies of scale and scope for networks and affiliates and provide independent stations with an alternative programming stream."[19]

Before the FCC acted on either the 1992 or 1995 rulemaking proposals, the 1996 Act directed the agency to relax the rule greatly, while allowing maintenance of two limited exceptions.[20] Under Section 73.658(g), as revised in response to Congress' directive, a station may affiliate with an entity that maintains two or more television networks, unless such networks are comprised of: (a) ABC, NBC, CBS or Fox; or (b) one of these Big Four

---

(...Continued)
the rule would not harm diversity due to the proliferation of over-the-air and non-broadcast outlets that provide a "multiplicity of network and other program sources" for consumers. *Id.* at 4118.

[17] *Review of Network Rules* at 11956.

[18] *Id.* at 11974.

[19] *Id.* at 11969.

[20] Telecommunications Act of 1996, Pub. L. No. 104-104, § 202(e), 110 Stat. 56 (1996).

networks and "an English-language program distribution service that, [on February 8, 1996], provided four or more hours of programming per week on a national basis pursuant to network affiliation agreements with local television broadcast stations in markets reaching more than 75 percent of television homes (as measured by a national ratings service)."[21] In other words, the new dual network rule permitted any combination of broadcast networks *except* those involving the Big Four and the English-language networks in existence on the date of enactment of the 1996 Act and having the specified reach - which were understood to be UPN and WB.[22] Despite this change, Congress directed the FCC to review the new dual network rule — as well as the rest of the Commission's broadcast ownership rules — as part of the required biennial proceedings, and to "repeal or modify any regulation it determines to be no longer in the public interest."[23]

---

[21] 47 C.F.R. § 73.658(g).

[22] The legislative history of the 1996 Act assumes, without factual analysis, that the second prong of the revised rule, which sets forth the criteria for determining which new broadcast networks are subject to the restriction, applies to UPN and the WB network. H.R. Conf. Rep. No. 104-458, at 163 (1996). Similarly, in adopting implementing regulations, the FCC concluded, without citation or review of UPN's audience reach, that the statute "in effect encompasses" UPN. *Implementation of Sections 202(c)(1) and 202(e) of the Telecommunications Act of 1996, Order*, 11 FCC Rcd 12374, 12376 (1996). In fact, as Viacom demonstrated in its Comments in the Biennial Review proceeding, at the time of enactment of the 1996 Act, UPN's distribution by full power primary affiliates fell below the affiliate reach benchmark. Viacom Comments at 39. WB similarly has asserted that, as of February 8, 1996, it delivered four or more hours of programming on a national basis to "less than 71 percent of television homes, well below the 75 percent threshold." *Biennial Review Proceeding*, *Supplemental Comments of The WB Television Network*, MM Docket No. 98-35, at 5 n.10 (filed Jan. 27, 2000) ("WB Supplemental Comments").

[23] Telecommunications Act of 1996, Pub. L. No. 104-104, § 202(h), 110 Stat. 56 (1996).

As noted above, in the 1998 *Biennial Review Report*, the FCC concluded that the dual network rule may no longer be in the public interest and announced the commencement of the instant rulemaking proceeding. Additionally, in the *NPRM* in this proceeding, based on its own economic analysis of network operations and the contemporary marketplace, the Commission stated its belief that "a merger between an emerging network, such as WB or UPN, and a major network may produce net benefits" for advertisers and viewers without compromising the agency's diversity goals.[24] As demonstrated below, the Commission's repeated conclusions regarding the dual network rule have been correct in each instance, and repeal of the rule is long overdue.

B. The Network Television Business

As explained in more detail in the attached Declaration of Dr. Robert W. Crandall, Senior Fellow in Economic Studies at the Brookings Institution, commercial broadcast television networks generally engage in two basic business activities: "program brokerage" and "advertising brokerage."[25] These activities have inherent costs and risks that are exacerbated by the current dual network rule, especially as it is applied to the two "weblets."

Program brokerage involves the development, production, licensing, and scheduling of programs to be distributed over the network's chain of owned and affiliated stations. In this process, a network may enter into short- or long-term licensing agreements with outside

---

[24] *NPRM* at ¶ 26; *see also id.* at ¶ 9.

[25] Declaration of Dr. Robert W. Crandall, Senior Fellow, Economic Studies Program, Brookings Institution, dated August 31, 2000, at ¶¶ 6-10 ("Crandall Declaration").

program suppliers or "packagers" – or it may create shows through its own in-house production facilities or those of an affiliated production entity.

In practice, networks engage in both kinds of program acquisition activities – *i.e.*, licensing shows from outside producers and "in-house" production. But even where an outside producer is involved, the networks typically bear a substantial amount of the risk of program development and production. For example, "they may pay for pilot production, commit for a specified minimum number of episodes, and agree to pay a share of unanticipated cost over-runs of each episode produced."[26] "In return for bearing the risk of financing program series' development, the networks generally obtain renewal rights for subsequent seasons and a share of the profits for non-network exploitation of the programs in reruns [and] foreign exhibitions," as well as the right to participate in ancillary revenues.[27]

The *NPRM* recognizes the extent of the risk assumed by networks in acquiring program rights, and the benefits that would flow from increased efficiencies. The Commission found that vertical integration between program production and network distribution "results in a major efficiency gain, namely, the ability to adapt more readily the (internal) relationship between the program supplier division of the merged enterprise with the network distribution division to unanticipated changes in the economic environment."[28] Thus, the Commission

---

[26] *Id.* at ¶ 7.

[27] *Id.*

[28] *NPRM* at ¶ 19.

found that vertical integration "may result in substantial efficiencies that may benefit network television advertisers and viewers."[29]

Networks also sell advertising time for spots in or adjacent to their programs, thus affording advertisers "the opportunity to diversify their messages across a number of entertainment [programming] vehicles."[30] "Because the popularity of a program and the resulting demand for advertising cannot be known in advance, the networks assume the risk that advertising revenues may not defray the full costs of their programs."[31]

It is also important to recognize that "expertise in program selection and program and advertising brokerage is likely to require fixed costs that could be exploited more economically across a larger number of program hours than are available to a single national network." A single network can only offer about 22 hours of primetime programs each week. Moreover, an individual network obviously cannot expand its programming beyond the number of hours available in a week.

Given these circumstances, networks have a clear incentive to seek additional opportunities to use their accumulated expertise in programming and advertising. As noted above, cable television and other alternative media provide obvious options for such investments. Under the dual network rule as it currently exists, however, the emerging UPN

---

[29] *Id.*

[30] Crandall Declaration at ¶ 8.

[31] *Id. See also infra* Section II.C. (discussing escalating costs and increased risks of program acquisition).

and WB broadcast networks do not represent such an option and, as a result, are at a substantial disadvantage in attracting investments of this kind.

C. Today's Highly Competitive Video Marketplace

In today's intensely competitive media environment, broadcast television networks clearly lack any semblance of marketplace "dominance." On the contrary, over the past 20 years, the traditional networks have faced greatly increased competition from an expanding array of alternative content distributors, resulting in declining audience share for the broadcast networks, rapidly escalating program acquisition and operating costs, and ever-increasing financial risks.

In the 1979-80 TV season, the "Big Three" of ABC, CBS and NBC enjoyed a combined national audience share of 90 percent.[32] In 1985, when the Fox network was launched, the three major national networks still accounted for 74 percent of the national primetime viewing audience.[33] In 1992, however, the three networks' share of the primetime audience had dropped to 59 percent.[34] Moreover, by the 1998-99 broadcast season, the *four* major networks, including Fox, accounted for just 52 percent of the primetime audience.[35] Even with the addition of UPN and WB, the *six* national networks together attracted a smaller

---

[32] *See* Rick Kushman, *Crisis of the Networks*, Sacramento Bee, July 25, 2000, at EN18.

[33] *See* Robert W. Crandall, *The Economic Case Against the FCC's Television Network Financial Interest and Syndication Rules* (1990) (submitted with *Joint Comments of Capital Cities/ABC, Inc., CBS, Inc., and National Broadcasting Company, Inc.*, MM Docket No.90-162 (1990)) ("Crandall Analysis of Fin/Syn Rules").

[34] Edmund L. Andrews, *Networks Gain Program Rights; Producers Lose*, N.Y. Times, Apr. 2, 1993, at A1.

[35] *See* Crandall Analysis of Fin/Syn Rules.

share of primetime viewing in 1998-99 (60 percent) than the Big Three had in 1989 (64 percent).[36]

In contrast, the share of homes viewing cable network programming has skyrocketed. From the 1993-94 season to the 1998-99 season, the share of viewers watching cable networks increased 71 percent, whereas the combined share of viewers tuning in to broadcast networks declined by 29 percent.[37] A recent study found that, in the first week of August 1999, primetime and total-day ratings for basic cable exceeded the ratings for the Big Four networks combined.[38] Even with the good ratings enjoyed by some of the broadcast networks this summer, it is clear that the era of broadcast network "dominance" is over. As the Commission observed in its *NPRM*, "[t]he growth of cable television and DBS have substantially increased the number of viewing options for viewers, resulting in a steady erosion in the size of audiences attracted to conventional, over-the-air network television programming."[39]

Erosion in the audiences of over-the-air networks obviously has repercussions in advertising sales as well. This year, cable's advertising dollars are predicted to surge between

---

[36] *See In the Matter of Annual Assessment of the Status of Competition in Markets for the Delivery of Video Programming*, *Sixth Annual Report*, 15 FCC Rcd 978, 1026 ("*1999 Competition Report*"); Crandall Declaration at ¶ 12.

[37] Nielsen Media Research, Combined Network Shares. Specifically, in 1999, primetime ratings for the broadcast networks continued to fall; the Big Four were down 4% (from a 29.6 to a 28.3), while the six broadcast networks - including UPN and WB - were down 3% (to a 30.7). *See* Multichannel News, Jan. 3, 2000, at 3.

[38] *Cable Consistently Is Beating Big 4 Networks*, Comm. Daily, Aug. 11, 1999, at 8.

[39] *NPRM* at ¶ 14. *See also infra* note 51.

25 percent and 30 percent ahead of last year as advertisers continue to shift their budgets away from broadcasting, leaving the networks with only an estimated 5 percent increase.[40]

This difficult competitive picture for network broadcasting in general is even more challenging for emerging networks such as UPN.[41] These nascent networks face intense rivalry, not just from other over-the-air competitors, but also from a wide range of other media sources, including cable networks and Internet services. Indeed, broadcast market share is shrinking as the number of cable networks "grows exponentially faster than the number of eyeballs watching television."[42] There are now 214 national basic and premium cable networks that select and schedule their own programming – a 146% increase since 1984.[43]

Moreover, within the past five years, the Internet has emerged as an increasingly significant provider of video programming. Noting that an estimated 100 million Americans use the Internet and over 50 million computers operate in American households,[44] the Commission recently determined that "real-time and downloadable video accessible over the

---

[40] Steve McClellan, *Cable Upfront Wins the Battle for Bucks*, Broadcasting & Cable, May 15, 2000, at 7.

[41] Significantly, cable program services and broadcast network services operate on very different economic models. Whereas cable services generally are paid for the right to distribute their programming, broadcast networks must *pay* (either through cash compensation or advertising availabilities) for such distribution. The sale of advertising time generally is a broadcast network's only source of revenue.

[42] *See* Deborah D. McAdams, *Time Keeps Ticking Away*, Broadcasting & Cable, Apr. 24, 2000, at 36.

[43] National Cable Television Association, *Cable Television Industry Overview 2000,* at 4. Specifically, the number of national cable networks has increased since 1984 as follows: 1984 (48 networks); 1992 (87 networks); 1998 (174 networks); and 1999 (214 networks). *Id.* at 5.

[44] *1999 Competition Report* at 983-84.

Internet . . . has become more widely available . . . [as m]edia companies continue to offer increasing amounts of video over their Web sites in the expectation that the pictures will be acceptable for the intended use or eventually improve to broadcasting or VCR quality."[45] Powerful technology players like Apple Computer, Microsoft, and Real Networks, along with an array of smaller innovators, are continuously providing new software for viewing Internet video.[46] In addition, many web pages have arisen specifically designed to offer Internet audio and video, further increasing the Internet outlets for streaming video.[47] With almost 30 million streaming media users,[48] the Internet is another direct competitor to the broadcast networks.

Telecommunications companies have also signaled their dedication to high-speed wireless data as a future competitor to traditional broadcast video. Industry experts believe that consumers will soon access digital video through wireless services.[49] Broadcasters agree;

---

[45] *Id.* at 1030.

[46] *Id.* at 1030-31.

[47] *Id.* at 1031-32. For example, Broadcast.com, which is billed as an "Internet broadcast network," offers live radio and television broadcasts. *Id.* Moreover, Entertaindom.com, one of the original entertainment networks on the Web, offers cutting-edge animation, short films, and webcasts of rock concerts. *See Entertaindom.com* (visited Aug. 25, 2000) <http://www.entertaindom.com>. Similarly, AtomFilms.com, another entertainment website, offers short films, animation, and digital media. *See AtomFilms.com* (visited Aug. 25, 2000) < http://www.atomfilms.com>.

[48] *New Media*, Comm. Daily, June 13, 2000, at 9.

[49] *See* Alan Breznick, *A Wireless Explosion*, Cable World, Dec. 6, 1999, at 1 ("The rapidly developing competition between cable lines and technology may not be confined to data . . . . Although high-speed Web access seems the most promising field for wireless right now, analysts say, digital video service may not be far behind.").

for example, Bob Wright, President/CEO of NBC, has said that "he expects to see 'tremendous development of wireless as a delivery vehicle' for TV programming."[50]

A critical (and inevitable) effect of the rise in competition has been the increasingly fractionalized nature of the electronic media marketplace.[51] The fragmentation of the audience has a corresponding impact on program acquisition, forcing broadcasters to find affordable ways to produce or acquire compelling, quality product to attract and retain viewers. As the Commission noted in the *NPRM* in this proceeding, "the continuing growth in cable . . . provides significant competition to the incumbent television networks as purchasers of television programs . . ., [leaving] the contracting environment . . . both more complicated than before and somewhat more risky for the networks."[52]

---

[50] *Id.*

[51] Today, approximately 67% of all households with television sets subscribe to cable or satellite, giving them a choice of an average of 57 channels of programming, and in some cases, over 170 video channels. *1999 Competition Report* at 983. This compares to the 20% cable penetration rate in 1979. *See* Paul Farhi, *Clap If You Love Mega TV! Without the Conglomerates, You Can Wave Goodbye to Free, High-Quality Shows*, Wash. Post, Sept. 12, 1999, at B1. VCRs are in 82% percent of all homes, allowing viewers to watch what they want, when they want. *1999 Competition Report* at 985. Video stores are located in every neighborhood. *Id.* at 1033-34. Pay-per-view is available at the touch of the remote and video-on-demand is being rolled out by cable operators. *Id.* at 1012, 1002. Further, over 100 million Americans visit and use the Internet, which is now available in over 50 million homes. *Id.* at 985. The Internet offers consumers a one-on-one experience on thousands of websites, many of which stream video programming. *Id.* Soon, with the implementation of digital television service, every broadcast TV station will be capable of transmitting at least 6 channels of video. *Id.* at 1067.

[52] *NPRM* at ¶ 14. This tension between declining revenues and escalating costs highlights the importance to broadcast services of exploring and exploiting all possible economies of scale. Indeed, the Commission has long recognized the efficiencies that can be derived from common ownership, including: joint financial, legal, research, and administrative and support functions; joint purchasing of equipment (especially with the high cost of digital conversion); joint purchasing of services (*e.g.*, programming consultants, ratings services); joint negotiation
(Continued...)

As their viewership has *decreased*, the networks have been facing steadily *increasing* programming costs. For example, the National Football League ("NFL") has locked in over $17 billion in broadcast network license fees for 1998 to 2002 programming packages from three of the Big Four networks – ABC, CBS, and Fox.[53] Major League Baseball ("MLB") has proposed a similarly expensive deal to the broadcast networks, whereby Fox's annual payments for MLB programming would jump from $115 million to $345 million, and NBC's annual payments for MLB's post-season and All-Star Game package would increase from $80 million to $240 million.[54] In addition, the U.S. television rights for the Olympic games from 2000 to 2008 is costing NBC an unprecedented $3.6 billion – $715 million of which is attributed to the 2000 Sydney Summer Olympics alone.[55]

Sports is not the only program source that has been affected by rising costs; entertainment programming costs have been escalating as well. Indeed, the average production cost for a primetime program is now $1.8 million per episode,[56] while the cost of a

---

(...Continued)
for exhibition rights to programming; fluidity in the allocation of scarce human resources, such as on-air talent and specialized management; and sharing of news and program resources among stations. *See, e.g., In the Matter of Review of the Commission's Regulations Governing Television Broadcasting; Television Satellite Stations Review of Policy and Rules*, *Report and Order*, 14 FCC Rcd 12903, 12930 (1999) ("*TV Local Ownership Order*").

[53] *See* Michael Freeman, *NBC, Fox Nix Baseball Hike*, Electronic Media, July 3, 2000, at 3.

[54] *Id.*

[55] *See* Steve McClellan, *NBC Goes for the GOLD*, Broadcasting & Cable, June 26, 2000, at 18.

[56] *See* John Consoli, *Television: Networks Bask In Summer Heat*, Mediaweek, July 24, 2000.

hit show like NBC's "ER" has exploded to an exorbitant $13 million per episode[57] – totaling about $300 million per year and more than $1 billion for the renewal period for a single popular series.[58]

Compounding the riskiness of such an expensive endeavor is the frequency with which new network television shows fail. Specifically, the failure rate for new network programs generally is 80 percent or more and has been reported to be as high as 95 percent.[59] This percentage translates into extremely low renewal rates for new network shows. For example, among the top *five* networks, only nine new shows from the 1998-99 season were renewed for 1999-2000 season.[60] Moreover, even with respect to the extremely small number of shows

---

[57] *See* Gary Levin, *All Reality As Far As the Eye Can See As 'Big Brother' Joins Voyeuristic Mix, Can Anything Else Survive?*, USA Today, July 5, 2000, at 1D. Moreover, NBC has agreed to pay approximately $6 million per episode of "Friends." *See* Cynthia Littleton, *'Friends' Once Again: Cast Getting $750,000 a Show*, Hollywood Reporter, May 15, 2000, at 1. Similarly, Fox's new drama "The $treet," which is scheduled to debut this fall, boasts a per episode production cost of $2.3 million. *See* Sallie Hofmeister, *Company Town; Taking Major Risks, Ovitz Tries for Prime Time Again; TV: His New Firm Has Sold a Record Seven Shows, But He Could Lose Millions If They Don't Become Hits*, L.A. Times, Aug. 9, 2000, at C1.

[58] *See* Steve McClellan, *Can the Big 4 Still Make the Big Bucks?*, Broadcasting & Cable, June 8, 1998, at 24.

[59] *See* Sallie Hofmeister, *Company Town; Taking Major Risks, Ovitz Tries for Prime Time Again; TV: His New Firm Has Sold a Record Seven Shows, But He Could Lose Millions If They Don't Become Hits*, L.A. Times, Aug. 9, 2000, at C1. *See also* Lynette Rice, *Alpha Female; ABC's Pat Fili-Krushel is the Highest-Ranking Woman in TV*, Entertainment Weekly, Dec. 17, 1999, at 21 (reporting an 88% failure rate for new network shows); Stephen Battaglio, *Has Murdoch's Network Been Out-Foxed?*, Fortune, June 12, 2000, at 40 (reporting an 80% failure rate for new network shows).

[60] *See* Alan Permgament, *Fall Preview; The Television Season Heading Into the Year 2000 Offers Some Alarming Trends and Some Thoughtful Shows*, Buffalo News, Sept. 5, 1999, at 24.

that do succeed, "studios must be prepared to finance production for at least four and up to six years. Only then can a hit show [begin to] recoup expenses by selling reruns to TV stations in syndication."[61] Thus, UPN and WB, like their larger competitors, must find ways to deal with the rising costs involved in funding, developing and, in many cases, replacing the programs that make up their network schedules each year.

D. The History and Distinctive Role of UPN

The challenges experienced by over-the-air broadcasters generally are brought into sharp focus by examining the experiences of the two emerging networks and, in particular, by a review of the six-year history of UPN. In the short period of its existence, UPN has struggled – against great odds – to develop a new broadcast television network. In the process, it has introduced program services that are especially responsive to the interests of underserved audiences.[62] However, it has also incurred substantial losses and is not financially self-supporting. As a result, if UPN were required to operate once again on a stand-alone basis (independent of a "Big Four" network), the weblet would face daunting challenges. If it could survive at all, an independently owned UPN presumably would be under intense pressure to shift over time toward an increased reliance on "mass-appeal" programming – as has been the case with the Fox television network – in order to broaden its advertising and revenue base.[63]

---

[61] Sallie Hofmeister, *Company Town; Taking Major Risks, Ovitz Tries for Prime Time Again; TV: His New Firm Has Sold a Record Seven Shows, But He Could Lose Millions If They Don't Become Hits*, L.A. Times, Aug. 9, 2000, at C1.

[62] *See* Viacom Comments at 27-30.

[63] Noting that Viacom has made a "compelling showing" as to how the FCC's ownership rules

(Continued...)

1. Since Its Creation, UPN Has Struggled to Build an Effective National Distribution Chain

UPN was developed in 1994 as a co-venture between movie studio and television station group owner Paramount Pictures and TV group owner United Television, Inc. (a subsidiary of Chris-Craft Industries, Inc.). The network was launched on January 16, 1995, with four hours of programming broadcast on two nights per week.[64] That same year, Viacom acquired Paramount. At the outset, United/Chris-Craft was the sole operator of the new network but, in January 1997, Viacom exercised an option to become a 50 percent owner of the UPN venture. On April 3, 2000, Viacom purchased the remaining 50 percent ownership interest from Chris-Craft's subsidiary, BHC Communications, Inc. Today, UPN is a wholly-owned unit of Viacom.[65] Viacom completed its merger with CBS on May 4, 2000 and was given twelve months in which to comply with the dual network rule.

(...Continued)
"have served to disadvantage UPN's efforts to establish itself as a national television network," the WB states that it "has faced virtually identical hurdles in its quest to provide a competitive over-the-air alternative to the four entrenched broadcast networks." WB Supplemental Comments at 9.

[64] On January 11, 1995, just days before UPN began operations, Time Warner launched its own new entrant into the television programming arena, the WB network. The two fledging networks had already begun their competition for local outlets (*i.e.*, network affiliates), months before their launch dates.

[65] Viacom triggered a buy-sell procedure on February 3, 2000 under the UPN Joint Venture Agreement with Chris-Craft. Under the buy-sell procedure, Chris-Craft was given 45 days to choose either to buy Viacom's interest in UPN or to sell its own interest to Viacom. Although the buy-sell price was only $5 million, Chris-Craft was unwilling to assume sole ownership of UPN – and sole responsibility for the network's continuing losses. Given that Chris-Craft – the most likely buyer of UPN – was unwilling to assume ownership of the network, it is questionable whether anyone would be willing to do so today, at any price. In the absence of a buyer, if the dual network rule is not relaxed as proposed and Viacom/CBS is required to
(Continued...)

Unlike the established networks, UPN does not pay formulated compensation to its affiliates. The revenues received by UPN affiliates are those generated solely by those affiliates themselves. Moreover, because the four established networks had long since entered into relationships with the stations having the most desirable transmission facilities - VHF stations and well-located UHF facilities - UPN had to fight with the other new network, WB, for whatever other outlets might be left in each local market. Thus, UPN was forced to cobble together a national network of affiliates composed largely of UHF stations and, in a number of markets, of LPTV facilities, most of which are at a substantial coverage disadvantage vis-à-vis competing stations affiliated with the established "Big Four" networks.[66] In a few markets, UPN was not able to secure an over-the-air affiliate at all, and instead endeavored to arrange for fill-in cable carriage.[67]

In addition, some of the UPN affiliates agreed to carry the new network's programming only on a secondary basis, reserving their primetime hours to the carriage of

(...Continued)
divest its interest in UPN in order to come into compliance with the rule, the network obviously would not survive.

[66] As a partner in the fledging UPN network, Viacom's Paramount Stations Group was determined to build its own station group as UPN-only affiliates. This decision required the company to dispose of valuable CBS-and NBC-affiliated stations in several Top 50 markets, replacing them in most cases with UHF stations having less desirable transmission facilities. With the sole exception of KSTW, Channel 11, Seattle-Tacoma, every station acquired by Viacom's Paramount Stations Group for its UPN O&O group after the launch of UPN has been a UHF facility.

[67] Of UPN's current total audience reach, 1.754% is through primary affiliation agreements directly or indirectly with local cable operators.