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

In the Matter of:	)	
	)	
Implementation of Section 11 of the Cable Television Consumer Protection and Competition Act of 1992	)	CS Docket No. 98-82
	)	
Implementation of Cable Act Reform Provisions of the Telecommunications Act of 1996	)	CS Docket No. 96-85
	)	
The Commission's Horizontal and Vertical Ownership and Attribution Rules	)	MM Docket No. 92-264
	)	
Review of the Commission's Regulations Governing Attribution of Broadcast and Cable/MDS Interests	)	MM Docket No. 94-150
	)	
Review of the Commission's Regulations and Policies Affecting Investment in the Broadcast Industry	)	MM Docket No. 92-51
	)	
Reexamination of the Commission's Cross-Interest Policy	)	MM Docket No. 87-154

COMMENTS OF COMCAST CORPORATION ON OPP WORKING PAPER No. 35

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Comcast Corporation ("Comcast") hereby responds to the Media Bureau's ("Bureau's") request for comments[1/] on OPP Working Paper No. 35, "Horizontal Concentration in the Cable Television Industry: An Experimental Analysis" by Mark Bykowsky, Anthony M. Kwasnica, and William Sharkey ("Working Paper" or "the paper"), which was released on June 3, 2002 by

1/ *See* Press Release, *Media Bureau Seeks Comment on Experimental Economics Study Examining Horizontal Concentration In The Cable Industry*, DA 02-1304 (June 3, 2002).

the Commission's Office of Plans and Policy ("OPP").[2/] The Bureau has asked, among other things, for "comment on the value of the study in providing empirical evidence relevant to the ownership issues raised in the Commission's pending cable ownership rulemaking proceeding." Comcast regretfully responds that, for the reasons detailed below and in the attached Declaration of Professor Howard Shelanski ("Shelanski Declaration"), the Working Paper's limitations and flaws prevent it from playing any useful role in the Commission's resolution of the issues pertinent to the promulgation of new cable ownership rules.[3/]

Introduction and Summary

Comcast respects the reasons that led OPP to commission the Working Paper. Judicial decisions have imposed tight constraints on agency efforts to limit the ownership interests of cable multiple system operators ("MSOs"). In particular, those decisions have made it clear that (1) cable operators are entitled to the protection of the speech and press provisions of the First Amendment,[4/] (2) horizontal ownership rules "interfere with [cable operators'] speech rights by limiting the number of viewers to whom they can speak,"[5/] (3) any cable ownership rules must

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[2/] *See* Press Release, *FCC Releases Study on Horizontal Concentration in the Cable Television Industry* (June 3, 2002). Subsequently, on July 3, OPP and the Bureau released a "revised data set" that corrects "several computational errors" in the original study and issued a revised version of the Working Paper. *See* Press Release, *Office of Plans And Policy And Media Bureau Release Revised Data Set Involving Experimental Economics Study Examining Horizontal Concentration In The Cable Industry* (July 3, 2002).

[3/] Comcast and AT&T Corp. are filing separate comments pertaining to the Working Paper and its lack of relevance to their pending merger. *See* Comments of Comcast Corporation and AT&T Corp., MB Docket No. 02-70 (July 18, 2002).

[4/] *See, e.g.*, *Leathers v. Medlock*, 499 U.S. 439, 444 (1991); *Turner Broadcasting System, Inc. v. United States*, 512 U.S. 622, 636 (1994) ("*Turner I*").

[5/] *Time Warner Entertainment Co., L.P. v. Federal Communications Commission*, 240 F.3d 1126, 1129 (D.C. Cir. 2001) ("*Time Warner II*").

"not burden substantially more speech than necessary,"[6/] (4) to meet this test, any resulting rules must be addressed to harms that are "real, not merely conjectural,"[7/] and (5) these rules must "in fact alleviate these harms in a direct and material way."[8/] Against the backdrop of several judicial reversals of FCC media ownership rules,[9/] it was entirely appropriate for the Commission to seek to explore whether academic researchers could assist in developing a record that would provide empirical, "non-conjectural" evidence useful in fashioning new ownership limits.

Although the motivations for this exercise are laudable, the results of this particular set of experiments are of no value. Candidly, it is difficult for a merger applicant *not* to attempt to find merit in a study that purports to show that efficiency is high and buyer bargaining power is minimal even in an environment in which one MSO is substantially larger than any that exist today – and even considerably larger than would exist after approval of the pending merger of Comcast and AT&T Broadband.[10/] The simple truth, however, is that the Working Paper does not affect in any way the evidence of record in this proceeding.

For two distinct reasons, the Working Paper provides *no* facts or analysis relevant to *any* issue currently pending in the ownership rules proceeding (or the merger proceeding). *First*, the

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6/ *Id.* at 1130.

7/ *Id.* (citing *Turner I*, 512 U.S. at 664).

8/ *Turner I*, 512 U.S. at 664.

9/ *See, e.g., Time Warner II; Fox TV Stations v. FCC*, 280 F.3d 1027 (D.C. Cir. 2002) (national television station and cable/broadcast ownership rules); *Sinclair Broadcasting Group, Inc. v. FCC*, 284 F.3d 148 (D.C. Cir. 2002) (local television ownership rule).

10/ As the Commission is aware, post-merger AT&T Comcast will comply even with the old 30% limit that the Court of Appeals reversed and remanded. *See Applications for Consent To the Transfer of Control of Licenses of Comcast Corporation and AT&T Corp., Transferors, To AT&T Comcast Corporation, Transferee, Application and Public Interest Statement* at 4, 49, 69 (submitted February 28, 2002).

Working Paper assumes a hypothetical environment that bears no resemblance to the real-world environment in which video programming networks negotiate with cable operators for distribution of programming, and it studies that hypothetical environment in a way that is itself further removed from reality. Consequently, the study yields no insights relevant to describing – or predicting – actual bargaining between cable networks and cable operators. *Second*, the conditions of the experiment – even if the model were reliable and the experimental conditions realistic – were not designed to, and did not, produce results that bear on the issues that must control the outcome of this proceeding. The study measures, at most, the effects of MSO "concentration" on the profits of cable networks and on the efficiency of network-operator bargaining. But the statute that controls this proceeding does not authorize the Commission to impose subscriber limits on cable systems in order to enhance networks' profits or the efficiency of network-operator negotiations. Rather, any cable ownership limits must be justified with reference to their effects on the flow of programming from *program producers* to *consumers*. Remarkably, neither of these two groups is represented in this study.[11/]

Comcast's analysis of the OPP Paper takes each of these points, in order, and explains them in detail. First, Part I explains why the conditions under which the study was conducted make it unreliable as a means of either describing or predicting actual bargaining between cable networks and cable operators. As we show, the experimental model does not even remotely approximate the real-world characteristics of the market for cable network programming. The

[11/] The authors suggest that, in this game, cable networks' profits may act as a proxy for the flow of programming to viewers. *See* Working Paper at 7. However, this cannot be the case since program creators do not need agreements with cable networks to deliver their product to viewers (they can reach consumers by way of other platforms, and they can reach consumers by other means over the cable platform without executing carriage agreements with cable operators). Further, the authors never explain why the flow of extra rents to sellers should imply or represent a greater flow of programming to viewers.

authors report a series of "results" of the "experiment," but both the design and execution of the study are seriously flawed. As a result, none of these results can be taken as evidence, much less as the sort of clear, concrete, and specific evidence required by the *Time Warner II* court.

Part II of these comments draws on Comcast's earlier submissions in this rulemaking to describe the statutorily and judicially prescribed standards that must govern decisions regarding the adoption of new ownership rules. We explain why the goal of any horizontal ownership limit adopted in this rulemaking must be to ensure, based on real evidence of a genuine risk, that the horizontal scale of a cable operator does not jeopardize the ability of consumers to access an abundance of video programming. We further explain why a proper focus, as Congress and the courts dictate, on the flow of video programming from its creators to its consumers means the Commission *must* take account of various pathways by which programming moves from creators to viewers and *must not* confuse the profitability of cable networks or the access of programming networks to cable systems with the welfare of viewers or the flow of programming to consumers.

Against this controlling legal background, one must conclude that the study was not designed to, and did not, produce results that constitute evidence respecting the issues that must control the outcome of this proceeding. The Working Paper reports the outcome of a game, based upon a hypothetical market model, the purpose of which was to illuminate the distribution of profits from cable programming between cable networks and cable operators (the so-called tests of "bargaining power') and the frequency with which those networks and operators are able to conclude contracts where it is in their economic interests to do so (the so-called tests of "efficiency"). Yet the statute that governs this proceeding, as well as the D.C. Circuit's authoritative construction of that statute, make quite clear that any speech-restricting limits on cable ownership must be tailored to address a real risk of market power abuse that could impede the flow of programming to consumers and cannot be justified by abstract predictions about the relative profitability of cable networks or the efficiency of their negotiations with cable operators.

The Commission must focus, as does the statute, on the risk of abuse of buyer market power that "unfairly" impedes the flow of programming from program creators to consumers. But the study was not designed to and does not address the flow of programming to consumers, focusing instead solely on relationships between intermediaries (specifically, networks and MSOs), and, even then, providing no basis to extrapolate from its "efficiency" and "bargaining power" conclusions whether increased concentration would effect the flow of programming even through the cable distribution channel. Of course, the study completely ignores that cable networks are only one pathway by which program producers can reach viewers; there are many other routes – independent of cable operator control – by which an abundance of programming can and does reach viewers.

I. **<u>The Working Paper Cannot Shed Light on the Relationships Between Cable Networks and Cable Operators Because the Conditions Under Which the Game Was Conducted so Greatly Differ from Real-World Circumstances.</u>**

A careful review of the conditions under which the game was conducted can lead to only one view: those conditions are too far divorced from the actual and varied conditions that underlie the real-world process of negotiating cable network carriage agreements, and the absence of necessary variables greatly skews the results. Plainly stated, the model cannot be said to depict or predict the actual bargaining process. No useful evidence emerges from this experiment.[12/]

12/ Professor Shelanski states the matter thusly: "the Study's experiment in no way reflects the structure, incentives, tradeoffs, or economic environment in which cable operators actually bargain with cable networks for programming. For that reason, its results apply to a world quite

Simplification is of course necessary in the design of an experiment. Inherent in the design of a laboratory model is the task of selecting only certain components or conditions of the world it seeks to analyze. The task of the designer, however, is not to select those parameters that render the model practicable. Rather, the conditions underlying the study must reflect key attributes of the world under study.[13/] In this regard, the authors of the Working Paper state that "[a]n attempt was made to include in the experimental market those features of the actual market that have an important impact on the affiliate agreements negotiated between programming networks and MVPDs."[14/] In fact, the game models a market that does not correspond to any actual market and imposes a variety of conditions on the negotiation process that would never be tolerated by network or MSO executives.[15/] Further, the study excluded a wide range of real-world actors and negotiating topics.

As a result of all these omissions, which are discussed in detail below, the study has no probative value in seeking to describe or predict any actual behavior. While Comcast does not object in principle to the use of experimental economics as a credible method for describing and predicting certain economic behavior in the real world, this particular attempt was not successful.

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different from the real one and thus provide no basis upon which any regulatory judgments can be made in this rulemaking or in any other related context." Shelanski Declaration at ¶ 17.

13/ *See* Shelanski Declaration at ¶ 3.

14/ Working Paper at 3.

15/ As footnoted below, many – but by no means all – of the artificial characteristics of the experimental conditions are acknowledged in the Working Paper.

A. <u>Unrealistic market structures and market participants</u>

1. Networks

The number and types of networks designed for the game are both odd and unexplained. They do not in any way resemble the number, types, or complexity of cable networks with which cable operators bargain every day. For example:

Number of firms – The model includes only four experimental networks. These are clearly inadequate to represent the almost 300 national cable networks currently in existence.[16/]

Types of firms – The design of the experiment not only rests on a very small number of networks, but also completely omits many important network types.[17/] None of the model networks bears the particular attributes of differing kinds of networks such as:

- regional or local networks;[18/]
- "must have" networks, those which every MVPD is virtually compelled to carry;[19/]

16/ *See Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming, Eighth Annual Report*, CS Docket No. 01-129 at Tables D-1 and D-2 (rel. Jan. 14, 2002) ("*Eighth Annual Video Competition Report*") (listing national networks). The paper acknowledges that "the experimental market includes far fewer programming networks . . . than there are in the actual market." Working Paper at 50.

17/ *See* Shelanski Declaration at ¶ 12 (discussing different routes from producer to viewer).

18/ The 8th Annual Video Competition Report identified some 80 regional networks. *Eighth Annual Video Competition Report* at Table D-3. The Commission ascribed great significance to these networks in its recent program access report and order. *See Implementation of the Cable Television Consumer Protection And Competition Act of 1992, Development of Competition and Diversity in Video Programming Distribution: Section 628(c)(5) of the Communications Act, Sunset of Exclusive Contract Prohibition, Report And Order*, CS Docket No. 01-290 at ¶ 19 (rel. June 28, 2002) ("*Program Access Order*") ("We note the growing importance of regional video programming services").

19/ These, too, were recognized as a distinct class of programming in the *Program Access Order*. *See id.* at ¶ 34.

- networks that are under common ownership (*e.g.*, owned by a major broadcast network);[20/]

- networks that are owned by a cable system or a cable MSO or a group of cable systems;[21/]

- new networks;[22/] and

- networks that are "bundled," for the purpose of sale to distributors, with "must-have" networks – and the networks that compete with such bundled networks.

Moreover, the sample of theoretical networks is itself selected from a very small sample of real-world networks.[23/] The network sample, in consequence, is so unrepresentative that one cannot have confidence in the model as a means of predicting actual behavior.

Absence of competition – These four networks apparently do not compete with each other for either viewers or channel positioning, since (in the study) a buyer's decision to carry one

20/ *See* Comments of Writers Guild of America, CS Docket No. 98-82, at 10 (filed Jan. 4, 2002) (ownership comments suggest particular problems at the *network* rather than the distribution level).

21/ The Working Paper acknowledges that the "experimental market . . . does not take into account that some large cable operators have attributable interests in programming networks." Working Paper at 50.

22/ The 8th annual video competition report identified 51 new networks that were preparing to launch. *See Eighth Annual Video Competition Report* at Table D-4. That none of the hypothetical networks is a new entrant follows from the fact that each experimental cable network has a perfectly predictable audience rating. *See* Working Paper at 10. No new network comes into being with that characteristic (indeed, audience size changes even for long-established networks, but predictions about audience size are especially uncertain in the case of new networks). We have no way of knowing how the bargaining would have changed had the buyers and sellers been given a range of possible audience ratings, with the actual ratings not becoming known until long after the deal was concluded.

23/ Cost structures for these networks were derived in part from estimates supplied by respected industry analysts. Where analysts' estimates were unavailable, "an estimate of the missing data was generated" by the study's authors using undisclosed means. *See* Working Paper at 10 n.21.

does not affect the viewership of any other.[24/] Further, the experimental networks' relative viewer levels are oddly skewed. Instead of presenting the rather continuous (and shifting) array of viewership levels that the nearly 300 real world networks display, these four carry fixed ratings, respectively, of 1.50, .90, .12, and .10.

2. MVPDs

The number and types of MVPDs/buyers in the experiment likewise do not even remotely replicate real-world circumstances:

Number of firms – The experiment was run with different groupings of buyers (with a minimum of three and a maximum of five buyers), none of which resemble real-world buyers. The size and market shares of these buyers do not correlate with those in the real world, and the number of real-world buyers is of course much larger.[25/]

Type of firms – For reasons that are unexplained in the Working Paper, in every set of experimental transactions one – and only one – buyer is said to represent a DBS provider. Despite the label, nothing about the game conditions replicates the circumstances of a DBS provider. The model did assign the "DBS provider" lower monthly costs than the "MSOs,"[26/] but in no other respect does the model attempt to capture the characteristics of a DBS provider

[24/] As Professor Shelanski discusses, networks compete against each other for a finite pool of viewers and channel slots. *See* Shelanski Declaration at ¶ 4. Particularly when one network is viewed as a substitute for another, a buyer's decisions with respect to network A obviously can affect its decisions with respect to network B.

[25/] The paper acknowledges that "the experimental market includes far fewer . . . MVPDs than there are in the actual market." Working Paper at 50.

[26/] Working Paper at 11 (Table 3). Inexplicably, the study simply assumes that "the vast majority of a buyer's costs were already covered by an existing flow of revenue." Working Paper at 11. This, of course, ignores the need for cable operators to recover the considerable investment in constructing (and operating) the additional channel capacity that makes carriage of additional networks possible.

(including the manner in which it competes with cable companies). In addition, in the real world, there are of course two DBS operators – not one – serving the entire country.[27/]

Absence of Competition – Most tellingly, in this experiment, not only is the DBS firm free from competition – so, too, are the cable operators.[28/] Unlike real-world conditions, nowhere in this experiment can a buyer (whether denominated cable or DBS) gain or lose market share depending on which programming that buyer chooses to carry.[29/] Nor do the programming choices of its rivals (competing MVPDs) enter into the equation. It is difficult to imagine an abstraction that is further from reality than the experimenters' assumption that a cable operator will not gain or lose any subscribers no matter what programs the system carries and no matter what programs are carried by DBS operator(s).[30/] This flaw of the study is especially puzzling given the guidance provided by the Court of Appeals in *Time Warner II.* There, the court admonished the Commission that horizontal ownership rules *must* take into account not just current market shares but also elasticities of demand, "*bearing in mind that if an MVPD refuses*

27/ The paper acknowledges that, in contrast to the conditions of the experiment, "there are multiple DBS providers" in the real world. Working Paper at 50.

28/ Professor Shelanski points out that "the failure to recognize that consumers in each market usually have three separate choices of MVPDs, each with different mixes of programming to offer, is itself a compelling reason why the experiment is of no utility in fashioning horizontal ownership rules." *See* Shelanski Declaration at ¶ 11.

29/ The authors acknowledge this deficiency of the experiment: "In the actual market, MVPDs have an incentive to carry a package of programming networks that maximizes their subscription and local advertising revenues. [As a result], the value MVPDs place on a given programming network depends, in part, on the types of programming networks they decide to carry." Working Paper at 52.

30/ Again, we note that the Commission's recent decision in the program access proceeding rests on a very different premise. The extent to which the Commission's vision of the market for cable network programming as reflected in that decision differs from the Working Paper's vision is quite striking.

to offer new programming, customers with access to an alternative MVPD may switch."[31/] The Working Paper ignores this admonition, and this characteristic of the study alone is sufficient to deprive it of any potential relevance to the Commission's task of meeting the standards of the remand.

B. Unrealistic negotiating conditions

Putting aside all of these contrived and unrealistic characteristics of the buyers and sellers in the hypothetical world of the study, there are other serious flaws in the experiment as well. Even if the hypothetical buyers and sellers possessed real world attributes, the nature and manner of the negotiations were such as to deprive the bargaining results of any value in making predictive judgments about actual business behavior.

Perhaps one or two of these constraints are not sufficiently consequential, by themselves, to call into question the utility of the experiment, but certain flaws are completely disqualifying. Even if any given flaw would not be fatal standing alone, the sheer force of the number and weight of unrealistic negotiating conditions negates the experiment as a basis for decisions in rulemaking or transactional proceedings. The results of the study probably would be significantly different were these flaws "corrected"; however, since each of these flaws has unique and unpredictable implications, it would be impossible to deduce a set of "corrected" results without re-designing and re-administering the game.

1. Lack of bargaining knowledge and experience

The study used persons who had so little experience, and so little knowledge of what they were doing, that what transpired cannot fairly be called "negotiation."

[31/] *Time Warner II*, 240 F.3d at 1134. Accordingly, the court directed that, "in revisiting the horizontal roles the Commission will have to take account of the impact of DBS on that market power." *Id.*

Both buyers and sellers were represented by college undergraduates and graduate students. Each was expected to conduct a full round of bargaining in no more than six minutes.[32/] The buyers and sellers knew very little going in. They had no prior course of dealing, so they did not know who had bought what from whom, or at what approximate prices, in previous periods. The parties gained no cumulative expertise; sellers and buyers had no way of learning how they had performed relative to other participants before they moved on to subsequent rounds. The parties were permitted no face-to-face communications and were able to communicate only by computer and then only to reveal offers and acceptances. Indeed, the buyers and sellers did not even know what product they were buying and selling!

Every one of these conditions and constraints is completely antithetical to real-world bargaining between MVPDs and cable networks. That bargaining is carried out by experienced, informed professionals, over a period of many months (and sometimes years), with tens and hundreds of millions – and sometimes even billions – of dollars at stake. Perhaps ironically, in at least one respect this aspect of the study was a complete success: just as one might expect, given the unrealistic conditions, the subjects bargained in unrealistic ways and regularly failed to reach agreements that would be mutually profitable, regardless of market concentration and regardless of whether the programming at issue was popular. This behavior could not and does not regularly occur in the real world.

2. Unrealistic contract terms and bargaining options

The model also denied the game-players several terms or options that are available to their real-world counterparts. Part of this stems from the parties who were not at the table. For

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[32/] As discussed by Professor Shelanski, the amount of time allowed for bargaining was both unrealistic and significant to the outcome of the game. *See* Shelanski Declaration at ¶¶ 4, 7.

example, we already noted that no networks had common owners, so no bundled offers could be made. No seller had a standing deal with a buyer, so no renewal contracts could be represented. Nor could the negotiations be influenced by the knowledge gained during prior negotiations or the leverage arising from a particular network already being part of the program line-up a given MVPD's customers were already used to receiving.[33/] Further, no network was allowed to account for other potential income sources, such as foreign sales or ancillary rights. This also meant that no buyer could offer to buy or share those rights to induce a sale. Buyers were not told whether they could or could not pass along higher rights fees to subscribers.[34/] No party was allowed to negotiate for anything other than price, such as channel positioning, longer terms, or promotional efforts.

II. <u>The Experiment Was Designed To Measure Network Profitability and Network-Distributor Bargaining Efficiency, Not Effects on the Flow of Programming to Consumers.</u>

When presented with any "experimental results," one asks: What is the question to which these data are the answer? Helpfully, the designers of this game tell us precisely what questions they intended to answer: First, what are the effects of various levels of MSO size on "efficiency" (by which they mean the propensity of network and MSO to reach a deal when it is in the best interests of each to do so)?[35/] Second, what are the effects of various levels of MSO

33/ Such pre-existing relationships, and the concomitant value that viewers assign to existing choices, will often have a determinative effect on subsequent carriage decisions. For example, no MVPD would even consider dropping ESPN for a new, untested all-sports network no matter how much less the new network charged. *See* Shelanski Declaration at ¶ 4.

34/ The paper acknowledges this flaw in the experiment. Working Paper at 52 ("The experiments also impose the restriction that the subscription price charged by the MVPD is independent of . . . the level of the affiliate fee paid by that MVPD").

35/ Working Paper at 3-4.

size on "bargaining power" (by which they mean the amount of profits from the network-operator enterprise that inure to the networks)?[36/] As we show in the remainder of this Part II, however, these are not the right questions for this proceeding.

A. Constraints under which this proceeding must be conducted

The present examination of horizontal ownership is informed by several constraining factors external to the Commission. An understanding of the context in which this proceeding takes place is therefore essential to the outcome. In its previous filings in this docket, Comcast has endeavored to identify the relevant contextual factors by asking three questions:

- What are the objectives (and commands) of the applicable *statutory* provision?
- What constraints have *judicial* decisions placed on the Commission's implementation of the statute?
- What are the current *marketplace* facts that the Commission must consider in deciding what horizontal ownership constraint, if any, is needed?

1. The Statute

While some commenting parties have characterized the Commission's obligation in this proceeding as everything from re-enforcing the program access rules[37/] to encouraging or discouraging particular types of programming,[38/] the central goal of this proceeding is clearly identified in the statute: to ensure that there are no unfair impediments to the flow of video programming to consumers.[39/]

36/ *Id.* at 4.

37/ *See* Comments of The Broadband Service Providers Association at 3; Comments of RCN at 19.

38/ *See* Comments of the U.S. Conference of Catholic Bishops at 2-3.

39/ *See*, *e.g.*, Comments of Comcast at 7.

The object of Congress' concern in passing the 1992 Cable Act was the American consumer, not the executives or shareholders of programming networks or of cable MSOs. The purpose of the Act, as made clear by the legislative history, was to encourage the availability of new and varied choices for consumers while at the same time recognizing the constantly evolving nature of the marketplace and the resulting need for regulatory flexibility. The statute itself therefore requires that the Commission account for "the dynamic nature of the communications marketplace."[40/]

The "Ownership Restrictions" section of the 1992 Cable Act is not a "catch-all" provision that allows the Commission to impose regulations to address to all sorts of real or perceived "harms." To the extent that the Commission might find a market failure in the MVPD marketplace, there are numerous other tools at its disposal. Effects of MSO size on matters other than the flow of video programming to consumers cannot properly be the basis for limits on cable ownership.

2. Judicial Rulings

The courts have removed any doubt that the Commission's sole charge under the ownership statute is to address genuine risks of harm to viewers' interests in accessing an abundance of programming. No other justification can be made for regulation of cable ownership, and any assessment of risk must be grounded in a complete record that reflects an accurate understanding of current marketplace conditions.

Any rules adopted in this proceeding will directly affect cable operators' First Amendment rights, and no court has ever suggested that reallocation of wealth is a sufficiently substantial governmental interest to justify curtailing free speech. Only a risk of harm to viewers

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40/ 47 U.S.C. § 533(f)(2)(G).

that is "real, not merely conjectural"[41/] can justify ownership limits, and even then those limits must "in fact alleviate these harms in a direct and material way."[42/] The court in *Time Warner II*, rejecting the 30% subscriber cap, noted that the Commission's basic charge was to "ensure that a programmer have at least two conduits through which it can reach the number of viewers needed for viability."[43/] Any ownership restriction intended to do more runs the serious risk of "burdening substantially more speech than necessary."[44/]

3. Marketplace Realities

A valid assessment of whether perceived harms are "real, not conjectural" and whether particular solutions "in fact alleviate these harms in a direct and material way" requires a realistic view of the marketplace. And market circumstances in 2002 are fundamentally different than they were in 1992. The number of competing firms, the strong bargaining position of broadcasters and other networks, and the technological advancements of the past decade all combine to make the markets for production, aggregation, and delivery of video programming both vibrant and competitive, where innovation is rewarded and complacency is disciplined.

Conditions have radically changed with respect to competition among multi-channel video programming distributors. Today, the vast majority of viewers nationwide can choose from three facilities-based MVPDs, and many can choose from four or more. Two all-digital DBS providers compete with cable in every market in America, and in many of those markets

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41/ *Turner I*, 512 U.S. at 664.

42/ *Id*.

43/ *Time Warner II*, 240 F.3d at 1131-32.

44/ *Id*. at 1130 (quoting from earlier cases).

OVS or cable overbuilders provide additional competition (not to mention SMATV and MMDS).

The fact that both DBS providers and an ever-increasing number of cable providers offer digital service is important. Through digital technology, almost all consumers can choose to receive 200 or more programming channels in their homes. Given such a massive number of hours to be filled with programming (200 channels means 4,800 one-hour time slots per day), cable firms have little incentive or ability to deny carriage unfairly to any particular programmer.

Additionally, given the bargaining power of "must-have" broadcast and non-broadcast networks as well as the plethora of other ways to reach viewers, cable operators cannot act as "gatekeepers" standing between consumers and programming. Program producers have numerous means available to get their product into viewers' homes. The most effective of these routes, by far, are still the broadcast networks, whose signals are delivered to every cable consumer regardless of the preferences of any given cable operator, provided that the broadcast network either consents to their retransmission or elects must-carry status. In addition to broadcast networks, there are numerous "must-have" networks that no cable operator could realistically exclude.[45/] No single cable operator (or even group of cable operators) could erect a barrier between programmers and consumers since there are so many routes around them.

4. Defining relevant markets

Much of the discussion in this proceeding focuses on the relationship between "programmers" and "distributors." References to "programmers" have generated some confusion, because they blur the line between two distinct sorts of activities. The Commission's

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45/ The Commission noted the importance of such networks in its *Program Access Order*. *See* note 19, *supra*.

NPRM properly identifies three distinct markets in the flow of programming from creator to consumer: (1) the market for the *creation* of programming by producers; (2) the market for the *aggregation* or *packaging* of programming by, *e.g.,* broadcast or other networks; and (3) the market for *distribution* of programming by, *e.g.,* MVPDs. As Comcast has discussed in detail in its previous comments, the relationships among these separate markets are complex.

Many firms do not confine themselves to a single one of these activities but instead compete across these markets, engaging in the production (Market 1), packaging (Market 2), and delivery (Market 3) of content. Local broadcasters, for example, engage in all three kinds of activities. Additionally, there are different "types" of relationships between participants in the three markets. For example, a program producer (Market 1) that sells its wares to a broadcast network (Market 2) is guaranteed delivery (Market 3) to every home served by cable, even without any exercise of discretion or editorial judgment by the cable operator. The same holds true for "must-have" non-broadcast networks (Market 2) like ESPN or Lifetime; selling a show to one of these networks virtually guarantees delivery (Market 3) to every MVPD home in America. In such instances, either regulation or market forces (or both) allow the Market 1-Market 2 relationship to determine the Market 2-Market 3 relationship; here, cable operators have little or no power to determine which content does or does not reach viewers.

As we noted in our previous comments, for viewers seeking access to video programming, it does not matter whether that video programming (Market 1) obtains carriage on a broadcast network or cable network (Market 2) or is distributed by a broadcast station, DBS system, or cable system (Market 3). After all, consumers watch programs, not aggregators or distributors.

B. <u>Reported "experimental results"</u>

How does the Working Paper contribute to the analysis of these issues? The paper describes several "major results of the experimental study"[46/] that, taken both uncritically and literally, might be thought to provide some basis for determining whether cable operators should be limited in the number of subscribers they may serve and, if so, at what level. For example, the Working Paper reports as one result that "when the number of programming networks exceeds the cable operator's channel capacity, higher levels of horizontal concentration . . . led to a modest reduction in 'economic efficiency.'"[47/] Thus, the study could be read to suggest that the experiment yielded data on the economic efficiency of various market structures or on the performance of firms within various market structures. Further, the paper reports that "the experimental results indicate that in the experimental economics setting the bargaining power of a cable operator that serves 51% of the MVPD market is not substantially greater than the bargaining power of a cable operator that serves 27% of the MVPD market."[48/]

C. <u>Comparing the working paper and the legal standards</u>

The Working Paper reports that the study measured the effects of concentration on "bargaining power" as well as "economic efficiency." The reality, however, is that neither "bargaining power," *as that term is employed in the study*, nor "economic efficiency," *as*

[46/] Working Paper at 3.

[47/] *Id.*

[48/] *Id.* at 4. While Comcast believes that the Working Paper is of no evidentiary value in this proceeding, to the extent that the Commission is inclined to give it any weight at all it must therefore conclude that the Working Paper evidences the *lack* of a need for a tight cap.

measured by these data, are relevant to the issues before the Commission in this rulemaking.[49/] And, even if they were relevant, they address at most only one of the seven statutory objectives Congress specified.[50/] Whatever was intended, when one examines carefully what the authors mean by "economic efficiency" and "bargaining power" as measured in their study, it becomes clear that neither casts any useful light on the issues before the Commission in this proceeding.

1. "Economic efficiency"

As we explained in Part II.A. above, the overall unifying question the Commission must address in the current proceeding is at what point, if any, the size of a cable operator jeopardizes the ability of consumers to access an abundance of video programming. The issue is *not* whether the size of a cable system affects the ability of a cable network to gain carriage on that system. This is because, as we demonstrated at length in earlier comments in this proceeding, video programmers seeking access to viewers are not dependent on being carried by a cable network that may or may not be picked up by a cable operator. For example, creators of video

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49/ Professor Shelanski notes that "the relationship between network/MVPD welfare and the amount and diversity of programming delivered to consumers is never spelled out in the Working Paper and under accepted theory is not a straightforward one by any means." Shelanski Declaration at ¶ 9.

50/ The study sheds no light on the seven enumerated statutory criteria that Congress directed the Commission to consider in formulating ownership rules. *See* 47 U.S.C. § 533(f)(2)(A)-(G). It is clear from the decision in *Time Warner II* that the other six criteria become relevant only if the Commission can first justify a limit with reference to the first criterion. That is, before it can adopt any ownership limit, the Commission must first determine that specific, non-conjectural evidence supports a subscriber limit in order to prevent buyer market power from unfairly impeding the flow of video programming from producer to consumer. Such a determination, the court has plainly stated, must take into account competition between MVPDs for viewers and the ability of consumers to shift from one MVPD to another to exercise program choice. The study, as already noted, rests on a hypothetical world in which no such competition exists. And as we discuss here, the study does not employ or measure proxies for operators' ability to impede unfairly the flow of programs from producers to consumers. Therefore, the study does not address the first criterion. Further, however, the study sheds no light on the other six criteria, which must be assessed if the Commission elsewhere finds real evidence – and there is none in the record of this proceeding – of buyer market power that impedes the flow of programming to consumers.

programming can seek to distribute their wares to consumers via DBS, via any of seven national broadcast networks that need no assent from a cable operator for carriage on any cable system, or via any of several "must-have" cable networks.

Yet precisely what the "economic efficiency" results purport to measure is the frequency with which cable networks and cable operators manage to successfully conclude agreements where it appears in their best interests to conclude those agreements. A change in this frequency does not, according to any evidence in the record in this proceeding, create a genuine risk of blocking the free flow of video programming to consumers. Creators of video programming have available other pathways, independent of cable operator content control, to reach viewers. Because this "economic efficiency" has at most a speculative and indirect effect on program creators' ability to access program viewers, the study's "efficiency" results – even if derived from a reliable experiment – would be quite unhelpful in determining where, if at all, to draw the line on cable system ownership.

2. "Bargaining power"

Similarly, no evidence in the current record purports to demonstrate that whether a programmer has a fair chance to access viewers is affected by how cable networks (a subset of Market 2) and cable distributors (a subset of Market 3) divide the profits from the packaging and distribution of programming. Congress did not charge the Commission with overseeing the distribution of surplus between those who package programs and those who distribute them to the home. The Commission itself has previously eschewed the notion that allocation of rents between middlemen is a legitimate concern of government.[51/] The D.C. Circuit opinion in *Time*

[51/] *See generally* Reply Comments of Comcast at 27 n. 81 (discussion of decisions regarding prime time access and financial interest and syndication rules).

Warner II will not permit the Commission to take the view that one purpose of a limit on cable subscribership is to cabin cable operator profits and redistribute them toward cable networks.

Yet what the study reports as a measure of "bargaining power" is specifically the manner in which packagers and disseminators of programming divide their profits. In the experimenters' own words, "[f]or purposes of the study, the flow of programming to viewers is impeded if a level of horizontal concentration adversely affects the profits earned by programming networks."[52/] In this study, when network profits go up, distributor profits go down – which is reported as network bargaining power rising and distributor bargaining power waning. And vice versa. The record in this proceeding does not contain a shred of evidence to the effect that either pair of profit movements affects the free flow of programming from program creators to program viewers.

Using lost profits to cable networks as a measure of the "harm" from concentration of cable subscribers makes sense only if the Commission takes as the purpose of this proceeding to guarantee success for particular video programming (participants in Market 1) or to redistribute profits among the middlemen (participants in Markets 2 and 3). Neither objective is authorized or contemplated by the statute. Neither purpose can suffice to overcome cable operators' First Amendment rights. Neither will assist in satisfying the *Time Warner II* court that the errors of the prior ruling have been rectified.

D. <u>Summary</u>

In short, some of the reported results are labeled as measures of the impact of various levels of cable operator size on "economic efficiency" and "bargaining power." In fact, if the study measures any real world effects at all, it measures the relative successes of cable networks

52/ Working Paper at 7.

and cable operators in reaching agreements that they "ought" to reach (cooperating) and in dividing the profits that do not accrue to program creators (haggling). Certainly, Congress did not assign this Commission a role in supervising the levels of cooperation and haggling between cable networks and cable operators. Nor is there any basis in the record for concluding that these observed behaviors constitute specific evidence of a harm to the free flow of programming to viewers.

III. Conclusion

As noted at the outset, Comcast appreciates the difficulty of the task facing the Commission in formulating ownership rules that will pass judicial muster. We do not fault the Commission for attempting to determine whether experimental economics can play a role in developing insights relevant to the adoption of new ownership limits. Even now, we do not suggest that no experiment could be designed and executed that could cast a useful light on these issues.

But certainly the factual circumstances of the experiment must "parallel[] the market under investigation."[53/] As the D.C. Circuit has made clear, the availability of substitutes to cable (including the ubiquitous availability of DBS), and the willingness of consumers to switch from one to the other, must be considered in order that the Commission may take full account of the dynamic nature of the MVPD market.[54/] An experiment that assumes away many of the most important characteristics of the real-world marketplace – as this one does – moves the discussion from conjecture to fantasy. And a study of network profits and aggregator-operator bargaining efficiency has no relevance to the factors that, by Congress' direction, must control this

53/ Working Paper at 10.

54/ *See Time Warner II*, 240 F.3d at 1134.

proceeding. Comcast therefore respectfully recommends that the Working Paper be dismissed from further consideration in this proceeding.

Respectfully Submitted,

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