BEAR
STEARNS

Panel **Six**

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Panelists

Jonathan Blake — Partner and Head of Telecom and Media Practice, Covington & Burling

Nat Ostroff — Vice President, New Technology, Sinclair Broadcast Group, Inc.

David Donovan — Chief Executive Officer, MSTV

Panel Time: 2:15 P.M. to 3:15 P.M. **E.S.T.**

Victor Miller: What we're going to talk about right now is just an update on the digital television landscape. And to help us do that, we've got Jonathan Blake, who's a partner and head of the telecom and media practice at Covington & Burling. Welcome, Jonathan. Nat Ostroff, vice president of new technology at Sinclair Broadcast Group. And David Donovan, who's the chief executive officer of MSTV.

Victor Miller: The basics. David, how much money will local broadcasters spend on digital television?

David Donovan: Well, you're talking in the billions in terms of investment right now. And, candidly, there are things that need to be done, both at the commission in terms of getting this rolled out . . . but this is going to be particularly in your smaller markets, it's going to be an absolutely huge investment overall. I mean, you're talking essentially in the billions of dollars in this industry.

Victor Miller: And bring us up to date on how many stations, Jonathan, are broadcasting with DTV signals right now?

Jonathan Blake: About **643.**

Victor Miller: **643** are on the air with digital TV?

Jonathan Blake: Yes,

Victor Miller: And how many stations are left to go?

Jonathan Blake: That leaves. . . 1,540 from **643,** so that leaves.. .

Victor Miller: About 900. . ,900 stations left to go. Okay. In the latest process, the FCC did allow broadcasters to file for extensions as they roll it out. Do any of you know whether a lot of broadcasters took advantage of that or not?

Jonathan Blake: About 507 filed with respect to the November 1 deadline, and, of course, the public station deadline is not until May 1 next year, and that 1,500 figure that I gave you, that did include public stations, so if you subtracted public stations from that 1,500 figure, it would be **300** less or **so;** 200 less.

Victor Miller: So, a significant proportion have filed for extensions. And what do these extensions entitle the broadcaster? What are they extending?

Jonathan Blake: Essentially, it gives them another six months . . . but you can sort of look at this as a bank account, and each time you ask for another extension, your credit at the commission goes down, and the penalties and problems mount.

Victor Miller: Let's talk about what interim step the FCC took to make it easier for small-market stations to get on the air? 1 mean, did they have some kind of low-power alternative? Is that something akin to that? David?

David Donovan: Well, that's certainly one . . . I mean, the commission has really drawn a dichotomy between your large markets and your small markets, and they have, particularly in the small markets, they have allowed lower-power facilities to come on-line. That's one way to deal with it, and, of course, it sort of matches with the population in those small areas. which are generally going to he much smaller than in your large MSAs [metro statistical area] and your large ADIs [area of dominant influence].

Victor Miller: Let's go through just the process of digital television, starting with the content all the way through to the consumer. Where are we right now in HDTV content from a national perspective and a local perspective?

Jonathan Blake: The CBS network has, I think, all but one of its prime-time non-news programs in HDTV. NBC is moving ahead very rapidly, and so is ABC. It's been a sea change over the last 12 months in terms of the amount of HDTV content. Fox believes in the 480 progressive model [lines of progressive scanning], which some do not regard as full HDTV. I just don't have an update on what their plans are. And public television intends to use HDTV in prime time for major events and maybe more and more for its basic schedule in prime time, but has a multicast model for the rest of the broadcast day, with some pretty specific plans about what those other channels would be.

David Donovan: Just to add, I think if you're looking at overall growth, I mean, essentially this year, as we're going into this fall, the number of programs that are out there in HD has increased over 50% from where we were a year ago. I mean, you've got roughly over 2,000 hours of HDTV programming out there. And that includes not only, as John has indicated, your major prime-time program on CBS, ABC . . . but NBC has certainly upped its stance as well. And the WB network, for example, has four HD shows and your major sporting events right now, which, of course, are significant drivers in terms of purchasing equipment — whether it's CBS's coverage of college football, the Masters, the U.S. Open, and Monday Night Football. ABC, I believe, is going to be doing the Stanley Cup fmals as well as the NBA finals. And the Super Bowl, I think certainly . . . a year and a half ago, I was at a conference when essentially the hue and cry was, at that point, coming from the cable industry that there's nothing out there. Well, that just is not the case anymore.

Victor Miller: So, now, we have made content and we're going to now . . . we worry now if we're producers of content that all of this content is going to be stolen because it's all on digital now. Where are we on copyright protection?

David Donovan: On copyright protection, where we are right now, of course, is that the industry appears to be coalescing around the concept of a broadcast flag. Of course, one of the most troubling aspects of broadcasting free over the air is the ability to simply take it over the air and record it and send it down through a modem on the Internet. The industry over the last several months — and though the Broadcast Protection Discussion Group has been coalescing around a broadcast flag proposal, my understanding is that the commission will be receiving comments on that proposal on December 6. And I think there is certainly consensus throughout the industry that this type of — and while you define it in terms of copyright, it really is control over redistribution. Essentially, what it would do is embed within the signal information that would prevent the retransmission of that down over the Internet. And the question, of course, has been over the last several years, what can you do within the confines of your own home with that? Can you copy it and bring a copy of that up to your vacation home? Can you copy it and give it to your brother in the next room? There are some very delicate issues there. I think the concept that has been arrived at is something called — I guess it's a personal, in-home network. which is essentially the ability to copy it for your own use . . . to transmit it for your own use, perhaps to other locations, provided the transmission source is secure. And that, of course, is a very interesting element and one that really still has to be worked out. But I think conceptually, we're there. And, of course, I think if broadcasting is to survive and go forward, copyright protection or control of retransmission of that signal is vitally important.

"When you hear costs like $2 million a station, that's probably a fraction of what the total cost is because, ultimately, when you go to full digital, the whole plant will have to be converted."

Jonathan Blake: Victor, you're doing something very interesting in progressing though this. I think one interesting point about cost is that the cost you hear now, as opposed to the costs that were developed by Dick's committee, is the cost of passing though a network signal. So, when you hear costs like $2 million a station [to convert to digital], that's probably a fraction of what the total cost is because, ultimately, when you go to full digital, the whole plant will have to be converted. That is being done gradually with amortization and other techniques. It may not be as much as $10 million a station, which was the original figure, but it's a whole lot more than just getting on the air in digital.

"One of the problems with the potential copyright protection idea is it would make obsolete all of the HDTV monitors that have been sold into the marketplace to date."

Nat Ostroff: Victor, I'd like to just jump in for a minute about the copyright protection? One of the troubling aspects of this whole discussion — and David mentioned that conceptually, we're there — conceptualization and execution are really two objectives, and they're very far apart. One of the problems with the potential copyright protection idea is it would make obsolete all of the HDTV monitors that have been sold into the marketplace to date. And there's a lot of people struggling with that. They would be obsolete in the sense that they would still display a picture, but it wouldn't be the HDTV picture if it was carrying a broadcast flag. And that kind of onerous outcome, I think, is a huge hurdle in getting past the copyright problem.

David Donovan: I would want to double check, obviously, with my engineers and that the latest version of this, Nat, I wasn't quite sure whether that was correct or not but I will leave that open. Yes, I don't think. . .

Victor Miller: Since I'm not smart enough to know exactly what the heck you guys are talking about, I'll move on to the next topic, if you don't mind. Nat, let's talk about where we are on transmission. We've got a thing, we've got it protected, now we've got to get it into people's homes, people's ears, or whatever. Talk about where we are in transmission?

Nat Ostroff: The transmitter, which is the device that emits the signal from the tower. . . those specifications are very precise, and some of them are quite difficult to meet. On the other hand, a lot of those specifications were written to ensure that the table of allotments that was constructed to allow digital television to be squeezed into the current analog spectrum . . . that you could do that because of the transmitter's performance. As part of that creation of the table of allotments, the commission also made technical assumptions about the receiver. And those technical assumptions involved things like how well the receiver could separate signals that were next to each other and how well the receiver could deal with signals that were of greatly different power levels and how well it could receive a signal that was very weak. Those specifications for the receivers. which were created for the table of allotments, have not been included in the current mandate for a receiver tuner to be placed into all TVs and receivers. And I think that there were really two issues that we're dealing with in terms of this transmission reception system. And, one **is,** can we build a receiver that will work in an indoor environment where the signal is strong enough with simple antennas? That's sort of been the criteria at least for broadcasters on our side of the discussion . . . because earlier, we talked about the preservation of free terrestrial television. And **our** definition of free means that you don't have to pay a cable, and you don't have to pay a satellite to be able to receive the signal. And we also think that asking for outdoor antennas is just not a viable consumer outcome. ***So,*** we're really looking for a system that can receive the transmitted signal indoors with simple antennas. We think that may be on the horizon with some of the latest receiver developments. The issue that we're really faced with is, how do we make sure that these advanced, improved receiver designs find their way in a ubiquitous fashion into the consumer marketplace? I heard arguments that it's a — let the market decide. I think one of the things that we can see here, from this entire seminar today, this summit today, is that there is no business model yet for paying for digital television equipment at the broadcaster level, and that, in fact, the market doesn't really exist yet for digital television. It's a mandated market, it's a government-directed market, and the government has to finish the job. In our view, they can't throw this thing out into the marketplace and say, well, now the market will decide, when they haven't really completed the definition of what this transmission reception system is going to be.

"Can we build a receiver that will work in an indoor environment where the signal is strong enough with simple antennas?"

"It's a mandated market, it's a government-directed market, and the government has to **finish** the **job."**

David Donovan: I think there are a couple of things going on here. The real question is how fast one can get tuners into sets and into the hands of consumers. Now, for the last five or six years, during the entire DTV tuner fight, MSTV asked the FCC to adopt tuner specifications. Once the DTV tuner requirement has been adopted, the real issue becomes whether or not the best way to get them into the hands of the consumers and accelerate that process is to either have to go back to the commission to continually engage in regulatory fights or work with that industry to accelerate that process. That is an issue that, quite candidly, from MSTV's perspective, we have to go back and talk to our board about. I think the real issue, though, is ,whether or not you can accomplish this through discussions and getting this rolling rather than fighting at the commission. We would hope we wouldn't have to fight at the commission. We would hope that the industries would be able to get

"We are still troubled that **CEA** has continued to file suit against the DTV tuner requirements, and we hope they reconsider that approach."

together because it is important to the consumer electronics industry that they sell equipment that works. It's obviously important to us. So, at this point, I think that the issue is fairly raised, but it is an issue that, hopefully, we would be able to resolve without having to fight for years and years and years. On that score, candidly, we are still troubled that CEA [Consumer Electronics Association] has continued to file suit against the DTV tuner requirements, and we obviously would hope that they would reconsider that approach.

Victor Miller: Let's go to the next step. How about interoperability with cable? Who wants to start that one?

"I think that the ATSC standard was developed specifically as a broadcast standard. And the interoperability with cable is still pretty much unresolved."

Nat Ostroff: Well, I'll just make a few comments on it. I think that the ATSC [Advanced Television Systems Committee] standard. as it was conceived, was developed specifically as a broadcast standard. And the interoperability with cable is still pretty much unresolved. And that may he one of the great weaknesses of where we are today in that . . . the ATSC XVSB transmission standard is not as compatible with the cable system as — and I'm going to say a word that'll get everybody's hair standing up — but the DVB system in Europe was designed from the get-go to he compatible with cable and satellite transmissions. The ATSC system really wasn't. So we really have to address that issue. To address that issue successfully, we need to have a lot more interindustry cooperation. We're really like three cats in a cage scratching at each other instead of saying we all will do better and we all will be more healthy and more successful if we could only cooperate. And I really am troubled by the fact that we have been unable to reach that kind of level of cooperation.

Victor Miller: David?

"We want our model to have featurerich sets out there in the hands of consumers that will provide all the services and everything that over the air has to offer."

David Donovan: Well, I agree with Nat. I think interindustry cooperation at this point is critically important. Broadcasting is fundamentally an open system. Unlike other closed subscription-based systems, we are not providing equipment that you're purchasing and having control over that equipment; it is an open system. It will remain an open system. Congress will certainly ensure that. Which means the coordination of elements between broadcasters and consumer electronics receiver manufacturers becomes critically important. It is vital that we have some mechanism so that we have those types of ongoing negotiations so that we don't get in all these particular catfights. With respect to coordination and interoperability between cable, I think there are a number of elements as to what that means. Certainly, VSB is the system, and we will go forward with that. I think, to some extent, though, what we have been watching — I'm shifting just a little bit — is the ongoing discussions between cable and the consumer electronics industry with respect to plug and play — which I think are also critically important for the over-the-air broadcast. Because once that's resolved, and the smarts and the features are being put in the sets, that will clearly benefit over-the-air television broadcasting. We want our model to have feature-rich sets out there in the hands of consumers that will provide all the services and everything that over-the-air has to offer. And I think an agreement between cable and CE as to plug and play will certainly work ultimately to our benefit.

Jonathan Blake: Let me give an example of how important this issue is. A year ago, I took one of my kids on a Saturday and went around to a bunch of retailers and asked about HDTV sets and whether they would work on cable. And the answer on every single retailer was "I don't know." Now, with cable penetration as high as it is, that's got to be a huge dampener to selling digital sets — a huge dampener. *So,* the things are interrelated. You really have to solve that problem if you're going to expedite the sale and the penetration of digital sets.

"We have really not found a single retailer who understood what he was selling."

Nat Ostroff: Jonathan, I agree with you. We did the same experiment, came to the same conclusion in the Baltimore market, that the consumer electronics retail industry is doing a terrible job — or maybe an excellent job, depending on which side of the equation you're on — in deceiving or not fully informing the buyer on what they're getting. And we have really not found a single retailer who understood what he was selling and specifics and could answer detailed questions to the extent that the answers may not be conducive to enticing the sale. This is a real problem for us as broadcasters for the simple reason that you only get a first time — you only get one chance to make a first impression. We put our digital signals on the air . . . the market . . . and if we choose to promote those signals — and I have some issues with the fact that we're operating at low power, by the way — but the fact that we promote these signals in the marketplace, and folks go to the retailer to buy a set, and they ask the question, "Can we receive the local television station — digital station?" And when the retailer says "I don't know" or "no" or "the signal that you're looking at is coming from a server, and we can't receive the digital signal because we haven't put an antenna on the roof of our building," and so forth. We don't get a second chance to get that consumer's eyeballs to look at our off-the-air signal. And there's been an enormous focus, and rightly so, perhaps, on making sure that cable and broadcasters get together and our signals get carried. But the simple reality is that the broadcaster has spectrum. And that spectrum only has value if it's used to deliver our product directly to the eyeballs of our audience. If we have to succumb to a gateway provider like a cable system that has 96% or 87% of the penetration in a market like Philadelphia, for example, then we become a cable programmer; local orientation, no doubt. But you don't need an FCC license to be a cable programmer. And so, we really need to make our spectrum work for us, and that means we need to have receivers that work, we need to have a consumer electronics industry that does not focus so heavily on cable and satellite receivers that it's willing to forget about or to marginalize its product in terms of capable off-air receivers.

"There's been an enormous focus on making sure that cable and broadcasters get together and our signals get carried."

Victor Miller: Let's move to set tuners. What's going on in the development there? You want to start, David, with that?

David Donovan: Set-top boxes or tuners in the sets?

Victor Miller: The tuners in the sets.

David Donovan: I think that there are a number of promising developments in that area. I think Nat is correct. In any reception model, you have both the transmission and the reception side . . . and there are some number of chips that are being developed out there that, quite frankly, will improve or are in the process of improving reception capabilities. There's a Casper link system out there; I know

Broadcom is working on a chip as well. Those types of sort of natural developments in technology, I think, are making great strides.

Victor Miller: Anybody like to follow? Jonathan?

Jonathan Blake: Yes, I've used this analogy before. It seems to me that when we shifted over from leaded gas to unleaded gas, at a certain point in time, car manufacturers had to stop manufacturing cars that ran only on leaded gas. And I think if we're going to make the same kind of conversion to digital, there has to be a similar shift-over to occur. And I actually am kind of optimistic that it's going to happen because I think, increasingly, the CEA industry understands that it's necessary for it to do that.

"There's no money in just producing dumb monitors."

David Donovan: Let me just add one, sort of, incentive here. There are actually. I think, a couple of incentives operating out in the marketplace. One, of course, is, as Nat has raised, the CE guys. And if you listen to . . . CEA makes some statements, well, cable's where it's at and don't worry about broadcasting. But the flip side of it is, and if you begin to talk to some of their strategists among the companies themselves, over-the-air television broadcasting serves as a competitive and a competitor counterbalance to other systems. So that if you're not involved in the set-top business, the set-top box business, or you're not involved in making set-top boxes for satellite companies, you need and want an over-the-air television broadcast industry to be feature-rich in providing those services over the air so that you can provide feature-rich sets as opposed to just providing dumb monitors because there's no money in just producing dumb monitors. So, Nat's emphasis I think is a correct one in terms of the importance of off-air — not only for us, but also for the CE guy.

Victor Miller: Where are we with educating the consumer on the merits of digital television and even how to even buy a set and know what the hell to do with it when you get it home?

Nat Ostroff: Practically nowhere.

Victor Miller: Then what should we do? What can the industry do about it?

Nat Ostroff: I think there's a dual responsibility. I think the broadcaster himself, herself, needs to be more proactive in promoting the fact that they have digital signals on the air, and perhaps tutorials on how to use that — how to receive those signals. And the consumer electronics industry needs to be putting out some literature, at least at the training level, to educate the sales folks on the floor. And I don't think it necessarily needs to go all the way down the mom-and-pop store on the comer, but once the large distributors educate their salesmen, that will put requirements on every sales individual who's going to be effective in making a sale to become more knowledgeable about digital television.

Jonathan Blake: Victor, one thing I think is really going to help is the programming. I think it'll pull people to ask the questions, and then the people who they are asking questions of are going to be responsible for answering. The LIN Television stations and others carry, by multicast, some of the early rounds of the NCAA games in Indiana. Those consumers are going to ask about how you install and how you use digital television, and they're going to know about it. And that, hopefully, will have a kind of snowballing effect.

"The driving force behind getting cable to carry our signal is you create demand by delivering our signals effectively to an audience over the air, which then drives the audience to want to see those signals on the cable system as well."

Nat Ostroff: Jonathan, there's an excellent point that comes out of that. We're so concerned about having cable carry our digital signals. The driving force, I think, behind getting cable to carry our signal is you create a demand in the marketplace by delivering our signals effectively to an audience over the air, which then drives the audience to want to see those signals on the cable system as well. And that gets back to the whole issue of, do we have an effective transmitter/receiver system at this point?

Victor Miller: Let's talk a little bit about the flexible usage of spectrum. As you know, the FCC said that you can pretty much do whatever you want with your spectrum, but if you do something other. . . and you collect revenue doing it and it's not related to your TV signal, you have to pay a toll, 5% of your revenue. But when David Smith and Preston Padden from ABC started talking about using the spectrum for other things, they got hauled in front of Congress, and Congress said, "I thought this was about HDTV." So, where are we right now on the flexible usage? Are we past that to where broadcasters are going to be . . . ?

Nat Ostroff: The fact that you mentioned Dave Smith, my .boss, I have to say at least one thing . . . yes, back in those days, it seemed like prehistoric times . . . we and ABC talked about multiplex, multiple programming, and we actually did a demonstration back in 1988 of five channels on the digital system. And that was really, really received quite negatively by Congress. But I think today, the reality is that multiplexing of the digital signal is one of the applications that can be used in conjunction with transmission of HDTV and shared with HDTV on a time basis. And I don't think it has the same stigma associated with it that it had four or five years ago.

Jonathan Blake: For public television, which has a very specific plan and has spent a lot of money and has entered partnerships with colleges, universities, libraries, they have a plan for five different channels of multicast during the daytime schedule; they've made commitments to that effect. What they stare in the face is the possibility — because of the commission's interpretation of primary video — that they will not be able to reach 80% of their audience. They are placed in a very difficult position because they have this valuable resource . . . if they use it for ACTV, they get carried across the board; if they use it for multicast, only one of the five program streams gets carried — that's going to affect what they do with that channel. And it could be pretty tumultuous.

Victor Miller: Talk about that whole issue of . . .

Jonathan Blake: Primary video?

Victor Miller: Primary video, yes, please,

Jonathan Blake: Well, the act calls for cable to carry primary video; it calls for cable to do **so** in analog and calls for it to do so in digital. The commission, in December **2001,** interpreted primary video to mean a single channel of programming. The commission is reconsidering that quite open-mindedly to determine whether that should include all free channels of programming or just one channel. That issue is up in the air; there *are* a number of ways that it could be resolved, and it could be resolved by negotiations between the industries, it could be resolved by a further notice of proposed rulemaking, which would be . . . after all, this proceeding was supposed to start six years ago. It could be resolved by a determination that multicasting should be provided as free programming. It could be part of the all free bit solution, or the commission could stick with its earlier determination that it was just one program stream.

Victor Miller: Am 1 right, did Commissioner Abernathy say something recently on this where she questioned the constitutionality of the whole issue?

Jonathan Blake: Well, there is a legal issue. and I think she would, perhaps, like more comment on it, although the record is very, very well teed up on this issue. The argument would he that if there's a constitutional . . . a serious constitutional issue raised, that you want to interpret the term "primary video" narrowly . . . but, to oversimplify somewhat, after all, carrying the HDTV requires a certain amount of capacity. If you split that same capacity up among various channels of multicasting, the burden isn't any greater — the capacity being required to be accommodated by the cable system isn't any greater. But that's where her concern is, and I think the other commissioners regard that **as** an important issue to resolve, although she might come around and feel that could be done without raising constitutional issues.

Victor Miller: They think that right now the Federal Communications Commission has been much more active in proposing and making the parties talk and putting out proposals; obviously, they've formed an internal group, headed by Rick Chessen, that looks just this issue, which I think was a good move. Obviously, Billy Tauzin's been very, very involved. And you can say that now Senator McCain is the bead of the Commerce Committee in the Senate . . . that he's also with the $70 billion spectrum value in mind . . . could also be *an* agitant and/or proponent, and/or **a** part of it that could actually get things done. What do you think the government should do? What areas should they get involved with? Do we need legislation? Do we need FCC? Do we just need the parties to sit down in a room and not let them out? I mean, what's the biggest issue here, and how do we solve it?

"**It** isn't a **$70** billion giveaway — never has been. This is a transition designed to benefit consumers."

David Donovan: Well, I think if **you start** from where we were about a year ago, which was essentially, the government had done nothing for the longest period of time. Chairman Powell and Chairman Tauzin have done a terrific job in getting momentum on the issue — whether it's getting tuners going, forcing people to sit in a room and talk. . . they have done a terrific job getting the ball running. Where do we **go** from here? First of all, I would hope that we do not get bogged down in debates regarding the $70 billion giveaway because I think, as the most recent auctions proved when they auctioned three to four channels, they got ***$85*** million nationwide . . . it isn't a **$70** billion giveaway — never has been. This is a transition that is designed to benefit consumers. The reason why we had digital channels . . . were allocated in the first place was for consumers, not necessarily for the industry. For the industry, I think, is going to be spending all day discussing the reality that it has been an economic burden to make this transition . . . and, up to now, one that has been very painful, particularly in the small markets. So, I hope we don't go down that road, but what do we need to get done? It seems to me that we need to get, as a first step, we have to resolve the carriage issues. Nat is absolutely correct that what we need competitive-wise is to get our off-air signals out there, to have . . . and to compete at that level. But we also have to face the realization that as we're switching transmission systems, as we're switching over to digital, the vast bulk of many markets today are people subscribed to cable. And the decisions that are made in the context of carriage are going *to* affect how we roll *this* . . . how fast this digital process rolls out. So, I think that has to be at least one of the critical issues as we go forward. I think the other issue, of course, is to make sure that the tuners roll out — and roll out in an expedited fashion. And I also believe one of the things that we really need to do, of course, is to try to reach resolution on the cable interoperability issues and particularly the plug and play. At tlie end of the day, consumer convenience is going to be king. People have to be able to walk into a Circuit City or any other retailer. buy a television set, take it home, have it plug into the wall. have it feature-rich, or get it off the air.

"At the end of the day, consumer convenience is going to be king."

Jonathan Blake: I actually think . . . it probably looks really darkest and bleakest now, and, in fact, all of the industry players have an incentive to have the digital transition succeed. Cable gets the benefit of getting back half the capacity that it devotes to analog because, in digital, it can put two channels of television programming in a space where it now can only carry one.. Receiver manufacturers will want to have it succeed because they want to sell sets that have greater benefits to the consumer. And broadcasters want it to succeed and to be over with because they do not want to be operating two plants with two sets of operating costs. When you're negotiating a deal, and people's personalities get in the way of getting it done you say, "well, this deal ought to be done," and, therefore, it will get done. And that's what I think is the momentum that will eventually drive a solution, while I can't really be sure how we get there.

"**All of** the industry players have an incentive **to have** the digital transition succeed."

Victor Miller: Now I'd like to ask a final question of you before we go to questions from the floor. What do you conceptualize as the business model for your digital spectrum at Sinclair?

Nat **Ostroff:** I wish I could tell you we had an answer to that question. I think it was said earlier that nobody yet has come up with a robust business model for the digital spectrum, and I think we, at Sinclair, are more or less on that same train. This is a government-driven initiative; it's not a market-driven initiative. And it was driven by technology, not by economics. And we're still struggling to figure out what the economics are. One of the points that I'd like to throw out *is* that there has been a discussion throughout the day today looking for second revenue streams for broadcasting. And the numbers, the horrendous disparity between the revenues generated off of our signals by subscriber fees for cable and how broadcasters get none of it. I think there's an interesting possibility here, and that is that the cable industry, to answer your question about revenue stream and business model, is looking to entice its subscribers to move to the digital tier. There's a real economic upside for them to do that. The broadcasters are broadcasting expensively produced, expensively transmitted HDTV, and we're doing more and more of it every day. And that HDTV is something the cable company would like to put on its digital tier as an incentive to move people up to that digital tier. The question I pose is this: the broadcaster today is deriving zero revenue from that digital signal. There is no economic risk at this point for the broadcaster to turn to the cable systems and say, "if you want our digital signal, pay us for it."

Victor Miller: Let's say, theoretically, they say, that's all right, we said we would offer our five slots, and if you broadcast it, we'll give it HBO, and we have to do this and do that . . . and they'll take your spots instead?

"When a cable channel wants to get carried on the local cable system, and it's not being carried, it *promotes* itself."

Nat Ostroff: Well, when a cable channel wants to get carried on the local cable system, and it's not being carried, it promotes itself. We have the mightiest promotional engine in the world called our broadcast analog TV station, and we could be talking about the fact that ***The West Wing*** is being broadcast in HD, that the football games are being broadcast in HD. If you want to see it on your cable system, call your cable system. We could create that demand. We market for General Motors, we market for Ford, we market for everybody but ourselves. We have a product to sell: it's HDTV, it's the only business model that we know how to make money with. We sell advertising; that's our business. A lot of the other business models are experiments in creative business models. But what we do know how to do is sell advertising. We need to have eyeballs to sell it. We, first of all, have to sell ourselves, our product, to the marketplace, and, I believe, we could create a demand for our HDTV signals on the cable system, and we could generate a second revenue stream. Why are we not doing that? I just don't know.

Victor Miller: The grand marshal for the DTV parade, ladies and gentlemen, Nat Ostroff. Any questions on the DTV subject?

Audience Participant: Just really quickly on the issue of multicast. It seems if you're going to get consumers to go out and spend whatever it's going to be, $100, to buy a new receiver box to receive digital if they're thinking of shutting off the analog signals, putting multicast on would be sort of an incentive or giveback to the consumer in terms of more content for going out and spending our money. I can understand the cable guys not wanting to carry all that because it really cuts into their business. But what's the likelihood of that happening? Multicast being permitted under the . . . the FCC saying "go ahead with multicast because this is how we're going to give back to the consumers," and they're going to force the cable to take it because that's the only way it makes sense for the local broadcasters to invest in doing multicasting.

David Donovan: ***You*** have this going on in ***two*** venues right now, one at the FCC, and also one on the Hill, in which the issue of ultimate carriage and multicast carriage is still left open with respect to Billy Tauzin's staff draft. I think in the end, the commission, precisely for the reason that you've recognized, is that if you want to accelerate the digital transition, you want to permit — particularly with respect to broadcasting, which is linked to spectrum reclamation . . . getting spectrum back — then you have to take steps to accelerate the off-air television portion of that transition. But to do that, you really need to have situations where consumers want to buy sets and want to watch digital television. The ability to provide HDTV, which Nat is absolutely right, which is a known driver of this, there's clearly one way to do it, and, at this point, I think the most important way to do it. But the other, of course, is during certain time periods, perhaps, to offer alternate services and multicast free over-the-air options. And I am hopeful that the commission will recognize that, especially those who are in the room right now.

Jonathan Blake: One of the big challenges is that the carriage rules that the commission is focusing on only go into effect, as presently contemplated, after the transition is over. So, you think of it as trying to drive the transition, but how do you drive it? The timing is off. David is right, I think, in saying the commission should start thinking about whether there are rules that would apply during the transition in order to speed the transition because, in the end, all the industries benefit from a faster rather than slower transition.

Anne Marie Fink: *You* talked about getting multiple multicasting, and one of the ways to do it is by promoting yourselves on your own air. But the other way that cable networks get is through launch fees. Are you guys contemplating paying launch fees to get cable carriage?

Nat Ostroff: I don't think so

David Donovan: They'd buy our share of the additional advertising revenues zero-zero.

Victor Miller: Thank you

Panel Seven

BEAR
STEARNS

Panelists

Richard Wiley — Managing Partner, Wiley, Rein & Fielding LLP

Wade Hargrove — Partner, **Brooks,** Pierce, McLendon, Humphrey & Leonard, L.L.P.

Greg Schmidt — Vice President of New Development and General Counsel, LIN TV Corp.

Panel Time: 3:15 P.M. to 4:15 P.M. E.S.T.

Victor Miller: The three people who are going to help us go through the Washington perspective are Greg Schmidt, who's the vice president of new development and general counsel of LIN Television. Good afternoon, Greg. Wade Hargrove, partner of Brooks. Pierce, McLendon, Humphrey & Leonard, and Richard Wiley, of course, managing partner of Wiley, Rein, and Fielding.

Let's talk about the midterm elections. First of all, a few weeks ago, the Republican Party retained control of the House, actually picked up seats in the House and recaptured control of the Senate. Let's look at the legislative side. Please review for us what changes will occur in leadership in the Senate and the House relative to the Commerce Committee? And what that might mean for television and the radio business.

Dick Wiley: Well, I think we're going to see a more deregulatory bent. Senator McCain **is** certainly in that pew compared to Senator Hollings. He, after all, was one of the handful of Senators that voted against the **1996** Act because it was too regulatory. And I think he favors a reexamination of the media ownership rules. He has, in the past, introduced legislation to eliminate the newspaper broadcast cross-ownership rule. So, I think, compared to the Democratic leadership, I think we're going to head into that direction. Having said that, I think Senator McCain also has some positions that have tended to worry the industry in the past. He's asked the GAO to study cable rates. He's called the spectrum for digital television "that $70 billion giveaway," as we've heard. He favors free air time for political candidates . . . 1% of broadcasters' gross revenues. So there are a number of things that must balance that.

Victor Miller: What influence, Wade, do you think Congress is likely to have on the NPRM's process now?

Wade Hargrove: Well, I agree with Dick. ***On*** ownership issues, Senator McCain, who will now chair the Commerce Committee, has been very laissez-faire with respect to ownership issues. But Senator Hollings will still be there. We know very much, we know that he very strongly opposes relaxation of the newspaper/broadcast cross-ownership issue. He will not have the influence at all that he's had in the past. One of the important positions he had on the side from chairing the Commerce Committee was he chaired the Senate Appropriations Committee that appropriated funds for the Commission. So, Chairman Powell will not have to respond to

Chairman . . . to Senator Hollings' chair of the Appropriations Committee. Nevertheless, he's still there, and he'll be a force to be dealt with. There's not likely to be any change in the Commerce Committee with respect to its leadership on the House side. And Congressman Tauzin has not expressed a great deal of interest in ownership issues. The point being, I do not believe that there will be any serious pressure from Congress on relaxation of the ownership rules — with one exception, and that is the cap. The cap, the national television cap, a **35%** cap, has been an issue that historically has attracted the interest of Congress. And when the 1996 Telecom Act was passed, the networks then were attempting to get the cap repealed in its entirety, or at least get it to ***50%.*** The Senate passed legislation, initially, that retained the cap at ***25%;*** it was reconsidered at Senator Dole's request. and the compromise was struck at 35%. So, it remains to be seen whether there will be any Congressional interest with respect to maintaining the cap. And that's an issue that, frankly, dorsn't split along party lines. It's an interesting coalition . . . Byron Dorgan and Senator Jesse Helms, for example, led the coalition in the Senate to **keep** the cap at ***25%.*** So, it's hard to predict on a partisan basis how members are likely to come down on the cap.

Greg Schmidt: I think Senator Lott's already sent some indication

Wade Hargrove: Yes, Senator Lott said he's troubled by increasing the cap.

Dick Wiley: I think had there been a changeover in the House that would have been very big because, **as** you know, in the House, the majority can get what they want done. In the Senate, going Republican means that Senator — **as** Wade said — Senator Hollings isn't in a position to implement his will directly **as** chairman, but in the Senate, you can still cause a lot of mischief or maneuver around if you're an adept legislator — and he certainly is that — even if you're in the minority. So there's still going to be a lot of play in Congress, but it's, at this point, doubtful they will play a major role in the ownership procedures.

Dick Wiley: And I think it's fair to say that the leadership of both Commerce Committees has a lot of respect and liking for the current chairman. I think Chairman Powell has an opportunity, therefore, to move in the direction that he wants to without any feeling that there's going to be any kind of legislative effort to block his effort.

Victor Miller: This is for Greg — the appeals court threw out **the** cable broadcast cross-ownership rule. The FCC decided not to take it up in its NPRM . . . and you could argue that out of all the ownership rules, local ownership rules, that could be the most offensive — that a cable system could actually buy a TV station in the local market, but, yet, a local TV station can't buy another **one** in St. Louis, for example, and a newspaper can't buy a TV station because of the cross-ownership rules and the eight-voice test. **Is** that a very important thing, or am **I** just kind of reading too much into that?

Greg Schmidt: I think it happened largely because of the procedural posture in which things came up. I mean, the cable rule had not been vigorously contested below, and there really wasn't much **of** a record. It is peculiar, and I agree with Shaun Sheehan of the Tribune Company, who made the comment earlier, that if I had any one combination in my market that would worry me, it would be cable and my largest broadcast competitor. And that's now fair game. And the fact that I can . . . in markets where there are seven stations I can't have or. . . go and buy a WB where I have a Fox affiliate seems completely upside down. But I think the courts . . . the basic message coming out of the courts, and this one, it's kind of amazing it went on this long. I mean, we had a series of rules that said, we consider radio and television to be competitors; therefore, we're going to have a rule that limits the number of those you can have. We consider cable and broadcast to be competitors, and we're going to eliminate that combination. We consider newspaper and broadcasting to be competitors, and we're going to limit that. But then when we look at broadcast-only, we don't regard any of them as competitors. I mean, that was so on its face inconsistent that they said, we're not going to go along with this anymore, we're going to make you do something rational here. And that's going *to* get them into some very interesting questions as to how to reconcile all of those different proceedings, and they've made a great start at it. But I think that's the role the courts played, and I don't think that's going to change materially. They may not have, I think, enough information in front of them to make some rational decisions at the margin as to which of these rules is really important and which is not. But I think in terms of the overall responsibility of making the commission do things that are, on their face, rational, they're doing a pretty good job.

Victor Miller: Talk about the concept of a voice. If you were the chairman of the FCC, how would you handle the whole concept of what a voice is, or would you just abandon that?

"Diversity gets you into **all** the slippery-slope issues **of** whether it's program, viewpoint, outlook, outlet. **.. you can** get yourself tied into some nice pretzels trying to define it in the right **way."**

Greg Schmidt: The voice concept really flows out of the diversity. Of course, we have the two objectives that the commission pursues: one is competition and the other is diversity. And diversity gets you into all the slippery-slope issues of whether it's program, viewpoint, outlook, outlet, diversity, and gets into a real . . . you can get yourself tied into some nice pretzels trying **to** define it in the right way. What it seems to indicate, at least in the competitive sense, and I have a problem with the diversity analysis generally, by the way, just in how you would have an objective that would go beyond a perfectly competitive marketplace. In theory, if you have a perfectly competitive marketplace, you've got an optimal number of outlets. **If** you try to legislate additional outlets, they will not be able to compete, and, ultimately, someone will go out of business, and you'll get back down to the optimal level. Alternatively, if you restrict the number below the optimal level, the solution is to simply make the market more competitive, and it's not clear what diversity, in and of itself, adds to that, at least in terms of being able to, long term, increase the number of outlets. But I think the conundrum the commission faces here is trying to define — is trying to put weight on these various voices the same way that you would in a competitive analysis, where you're defining substitutability or cross-elasticity **of** demand. How do you define cable **as** a voice? It's obviously different in markets where there's **a** 24-hour cable news channel than it is where there's simply ***36*** or **54** or a 154 national cable channels. If the operator, the cable operator themselves is having an input in terms of the local news content or information, that's different than if they're not; but how different? And how much should you weight that? The same thing goes for radio and weekly newspapers versus daily. I think it's very, very difficult to get into this with any degree of precision and be able to support it based on any sort of empirical evidence that's in the record or even out of the studies that

"How **do you** define cable **as a** voice?"

the commission's come up with now. And I think that's going to lead, to some extent, to some sort of bright lines like rule, no rule, in certain situations that . . . we'll have to see whether the courts . . . how much leeway the courts will give them when they come up with that?

Victor Miller: Well, Dick, if you were chairman again what would **you** do?

"Whatever you do, you've got to have consistency."

Dick Wiley: Well, whatever you do, I agree with what Greg says, but whatever you [the **FCC]** do, you've got to have consistency. That's where the court dinged the commission in a number of instance's. For example, in the duopoly rule, you have to have eight independent full-time television stations. In the radio or television cross-ownership rule, they counted cable and newspapers; you can't have that kind of inconsistency. And also, you've got to have a rationale for these rules, which the court found on numerous occasions were very thin. And so, the commission knows, and Chairman Powell knows this. That's why they've thrown all these rules into one comprehensive rulemaking so they can come out with a consistent treatment, one that has some rationale. My own guess is that he's going to be looking for a competitive analysis of some kind — it may be a voice test, it may be some sort of a point system — something with an antitrust background that shows what the true competitive conditions are. And I think, under those circumstances, I agree with what was said in previous situations: if you want to have a free over-the-air broadcast system, which, I think, is in the public interest, you've got to let it have an opportunity to grow and to converge into adjoining industries in order to be able to compete in the future against multichannel subscription-based services.

Victor Miller: Wade . . . do **you** have a follow-up?

"The commission held that there would **not** be a lessening **of** program diversity with the merger, but there would be a lessening **of** source diversity."

Wade Hargrove: The analysis, forget about whether you agree with the conclusions or not. But the analysis was very thorough on the issue of competition. And there's some interesting things there . . . struck me. One, the conventional wisdom was, among a lot of lawyers, when Chairman Powell assumed the chairmanship, that this commission would probably not concern itself a lot with competitive issues — with competition issues, but would be, perhaps, predisposed to defer to the Federal Trade Commission or the Justice Department and focus its efforts on the diversity issue and general public interest considerations — not so. Not so at all. If you read the EchoStar/DirecTV . . . a 135-page decision, probably 130 of those pages **are** directed to a competition analysis. And that analysis [of the proposed combination **of** EchoStar/DirecTV] might very well be the road map that the commission and the staff — that we could expect to see taken and the analysis of — at least the competition component of these other ownership issues and local markets and the national cap. Very little was said about program diversity in the EchoStar/DirecTV merger. The commission held that on the issue of program diversity, there would not be a lessening of program diversity with the merger, but there would be a lessening of source diversity. But the focus and all the heat and light were on competition, and I encourage you to look at that, And, I think that those who have an interest in the relaxation of the other ownership rules will want to look at that road map and see **if** it . . . if their rationale for whatever position they may be advocating could be fit into the analysis there; it was very well done.

Victor Miller: Can you talk to **us** a little bit, Dick, about the Jonathan Adelstein? He was confirmed. Can you provide some background on him?

Dick Wiley: Well, he's, of course, an aide to Senator Daschle, he's been up there a long time. He's from South Dakota. His father, interesting enough, is not only a businessman but a Republican state legislator. **So,** he's got a little bipartisan background in there. Reportedly very well liked on Capitol Hill, very smart, able guy. His views are — in our areas — are largely unknown. Some people are guessing that he's going to be closer to Commissioner Copps than to, say, some of the conservative Republican majority. But we'll have to see. We're going to give him the opportunity to establish his own credentials, it seems to me.

Victor Miller: Any follow-up, Greg?

Greg Schmidt: He clearly has a mandate to watch out for the rural interests. hut I'm not sure how that cuts in these proceedings. It may help us in terms of the small-market relief that people are looking for, but it may not.

Wade Hargrove: It could cut either way.

Victor Miller: The FCC, in conjunction with the release of its NPRM, released 12 or so white papers on various media ownership issues. Do you have any highlights of anything that surprised you or you found out in these, if anything? And why did the FCC do the white papers? Is this a first?

Greg Schmidt: That was a paper where . . . not allowed? Most of it was, I think, Dick can jump in too, but most of it, I think, was stuff, at least to some extent, that we're all comfortable with and familiar with and documenting in some detail the increase in competition and number **of** outlets and media outlets over the last three decades. **But** since many of these rules were changed . . . **1** found particularly interesting the fact that the analysis . . . and some of these are going to be obviously parsed and taken apart by people who question the methodology and some. . . even the people on my side of the debates. But the finding that ad pricing . . . I mean, one **of** the big issues we face in TV is a **sort** of reaction to the consolidation in radio, both in terms of the belief that it may have affected radio pricing and radio programming diversity. And I think the [FCC] studies that show at most a very small percentage **of** the radio ad pricing increases that we've seen, which had **been** substantial, were due to consolidation. And that most of it was due **to,** in **part,** economic conditions was significant. And the fact that program diversity hasn't suffered in any material way and even in some local levels has increased due to radio consolidation, I thought was very interesting also.

Dick Wiley: I thought it was interesting that the study showed that O&Os and newspaper-owned outlets do more news and public affairs, which seems **to** me **to** help in connection with some of the rules changes. **The** combinations don't reflect a particular slant, that it's just **as** likely that those combinations will take different positions **as** other groups of stations, that there's been a tremendous growth in the number of outlets over the last couple of decades, and, in particular, that consumers and advertisers are continuing seeking a substitutability of media — including the Internet — for television. A lot of younger people looking for news and public affairs turn to the Internet instead of television. And whether that's good news or bad news, as far as the rules are concerned, it's certainly . . . are good cases for alleviation of some of these age-old restrictions, which, you could argue, are outmoded.

Victor Miller: Wade, do you have any follow-up?

"It's a credit to Chairman Powell and the commission and the staff that it has embarked upon this very thorough approach."

Wade Hargrove: No, I thought the studies were very constructive. And, whether you agree, depending on your point of view, with the conclusions reached, this commission is certainly not . . . does not appear to be embarked on a process that will lead to the kind of comments from the court of appeals that the court has made with respect to its review of other decisions involving the ownership issues. It's a credit to Chairman Powell and the commission and the staff that it has embarked upon this very thorough approach. There are a lot of . . . continued to be debate . . . among economists about the substitutability, as Dick mentioned. of these various media for advertising purposes. And it's always been interestiny to me — I mean, if, indeed, radio and TV are not substitutes or newspaper not substitutes, why, for gosh sakes, would there be any concern about competition? I mean, if they don't compete in the same markets, then the combination of newspaper and broadcast or combination of radio and television would not have any anticompetitive effects. On the other hand, if you conclude that they are substitutes, and I think the conventional wisdom is, for the most part, they can be substituted. I mean, if you got to any television meeting — go to a TVB session, I've spent a lot of time talking about competing with newspapers. Radio guys talk about competing with television. But the *stark* reality is, which cannot be denied, is that's there's enormous diversity in the study. The voices that you illustrated from the University of Missouri study? The statistics that were in the working papers, various parties in the newspaper broadcast proceeding, have already submitted voluminous information showing the number of voices and the great diversity that exists — even in the smallest markets. Hearst submitted a study that showed that nine of the smallest of the 210 DMAs have 11 separately owned voices applying the traditional test for a voice. And that doesn't take into account new media. So, there's an enormous amount of diversity at the local level, and I think the question is, for most of us, to what extent will the commission, in the context of this proceeding, move the teutonic regulatory place of ownership? This proceeding, I think, everyone recognizes, has the potential of being, as all those who live in California keep anticipating, the real big one, and this is going to be a big, big event. And the evidence certainly indicates the commission is approaching it in that fashion.

Victor Miller: Dick, just give us an update. What's the timing now on the comment period, the closing of the record on the NPRM?

Dick Wiley: Yes, the initial comments are due January 2 and then replies in February, and the commission has said that they're going to make a decision in spring. Now, if August and September are spring months, I think they can probably meet that. But, being cynical, it is difficult to have major decisions like this get out in a couple of months after the comments close. On the other hand, the commission always could consider certain first report and order and spin out some once they know where their major directions are — spin out some of these rules and decide some of them. The newspaper rule, for example, newspaper broadcast . . . the record closed on that proceeding last February. All those comments were in, and all we're doing — and I do represent people in this area — is refreshing the record in that, to some extent. . . answering some **of** the commission's questions this time around. The commission has lots and lots of information; they could move ahead on that decision earlier if they wanted to do and actually do it in the "spring" [before the end of June **2003,** the original "deadline" for the FCC rulemakings].

Wade Aargrove: Victor, I'd like to ask Dick and **Greg** a question. Last month, the court of appeals, in a three-vote majority decision, struck down the commission's video description rules, a very interesting decision. If you haven't read it, I recommend it to you. The commission said, struck those rules down, because Judge Harry Edwards, a Democrat appointee to the court, held that to the extent that a commission regulation significantly implicates programming. and there is not a specific statutory authority to regulate in that area, the commission would be acting without authority and could not regulate. **And** this has raised among a number of us, who toil in these vineyards, a lot of questions about the scope of the commission's authority. What raises questions about any sort of decision that touches on programming . . . the question in my mind is, does this place any sort of jeopardy over the commission's ability to take program diversity into account? Is there anything in the act that says the commission shall take diversity of programming into account when it makes its decisions?

Greg Schmidt: Well, I know, there are some Supreme Court and some court of appeals cases. But it is an interesting decision, and it will be interesting to see where it goes.

Dick Wiley: Of course, the commission has previously said that diversity was something that the commission could **look** at when they were questioning the grounds for some of these ownership rules before. So, if someone took the consistency **of** the court of appeals, they might . . . if there was the Supreme Court looking at the court of appeals, they might have the same problem **as** the court does with the FCC. It's an interesting decision, 1 agree with you. I don't think you can push it too far, though.

Victor Miller: I'm glad you asked that question, Wade, because I could have never thought of that. Let's talk a little bit about some current events. Senator McCain suggested local TV stations should provide two hours of political time per week for a specified period of time prior to the elections.

Greg Schmidt: I think that's as viable constitutionally **as** .the bill that's currently being challenged — McCain-Feingold — which is to say, not. I mean it's a nice suggestion, and in some markets and in some situations, it may make sense. I think any sort of an across-the-board rule tends to do more damage than good in these kinds of situations, I think we all work really hard on that, on political. I don't think, **as** a general matter, consumers suffer from an underexposure to the candidates or their issues. But he's definitely on this one. Now he's going to stay on it and it's going to continue to be something that he's going ***to*** throw into the **mix** whenever we want anything else.

Dick Wiley: Yes, but I don't think it will ultimately be passed **as** legislation, and **I** think broadcasters, a lot of broadcasters, have stepped up to the line and provided more free time before elections. And, **as** you suggest, Greg, I think there's **an** awful lot of coverage out there. I don't think I went to the polls uniformed, and I doubt that many Americans did.

Victor Miller: Recently, Wade, the ABC network gave affiliates a five-year right to assign its network affiliation agreements, which can be particularly good for ABC affiliates in a deregulated world. Why do you think Walt Disney Company decided to take that tack with its affiliates in light of comments Mr. Eisner made about affiliates a couple years ago. Is this a sign?

Greg Schmidt: Let me just step in and just say I think it's because they had such — the ABC affiliates association has such able counsel.

Victor Miller: That's a fair . . . that could be it. And, also, is this a sign that the networks and affiliate relations could be thawing, or am I just . . . wishful thinking?

"The network affiliate relationship is an interesting relationship. It's a mutually dependent relationship. **It** has characteristics **of** a **love/hate** relationship. Each party needs the other."

Wade Hargrove: Well. the network affiliate relationship is an interesting relationship. I've had a seat on the 50-yard line for 20 years watching it. And it is a fascinating relationship; it's a mutually dependent relationship. It has characteristics of a love/hate relationship. Each party needs the other. And each party works in concert and in partnership toward the goal of trying to amass the largest possible audience for the programming — the networks' programming. On the other hand, they squabble about how to split the money up. And also they squabble about control of the station and the station's time. The network wants to control the time periods from the station; the station wants to retain its right to make specific program decisions . . . on a program-by-program basis. So, there's a built-in tension in the relationship, and the relationship, of course, has built an incredible broadcast system in the country. Why did ABC suddenly agree to abandon its practice and, in certain cases, abusing the assignment process to renegotiate the economics of an existing contract, which it had been doing for some five to six years? It was part of a negotiated resolution on a wide range of issues, renewal of the rights to ***Monday Night Football,*** calling for affiliate contribution in the aggregate of some ***$34*** million. Reaffirmation of the existing arrangement on repurposing and providing certain windows of exclusivity for network programming, renewal of the soap channel, deal that the network had with its affiliates. So, it was part of a larger resolution of a number of issues, and I think the parties felt that was an example of the relationship working in a very functional rather than dysfunctional mode. The negotiations started last January, and they were concluded in early September of this year. And there was a lot of discussion about it, and the parties, I thought, exercised very good judgment in the way they dealt with each other, and it was very professional. And tried to find the areas where they could create value for each other. ***So,*** I think it's good news for the network affiliate relationship.

Victor Miller: In terms of the Telecommunications Act of 1996 . . . the biannual review requires that the commission look and renew tests, only keep rules in place that are necessary in the public interest. The word "necessary" could likely come under a lot of scrutiny — that word and whether that means absolutely, positively, has to be there overnight kind of necessary or whether it's convenient necessary. What is this debate all about, and why is it important, Dick?

Dick **Wiley: Well,** I think it is a very important situation, but I want to say even if the commission ends up saying — the courts end up saying that "necessary" in the public interest only means convenient, the basic standard for review now, the court has also said there's still a presumption for repeal built into the 1996 Act. And, so, either way, I think the commission has got a burden here to show that if it's going to maintain these rules, there has to be a rationale better than the ones that they've given in the past that justifies the rules. I think Chairman Powell fully recognizes that, as I said before. And I think the court has waited — the court has relented on "necessary" meaning essential or indispensable at the request of the commission and has said, we'll wait and see, but we're going to look at this issue again. So, whether it's necessary, it's going to have that higher standard or review or it's the presumption — either way, I think the commission has its work cut out for it; it's on some of these old rules.

Greg Schmidt: And this is something that when we were lobbying for this bill, I don't think all of us thought — most of us thought this was a terribly significant provision because we were really focused on the specific regulatory relief we got in the 1996 Act. It turns out to be, I think. something . . . one of the most important things we did. And, in retrospect, it should be. I mean, look how long we have gone without a lot of these rules getting any reexamination, much less a serious reexamination. And as long as this provision is around, however you define "necessary," I think we're at least going to be satisfied that the commission's going to have to take a hard look at what the reality currently is and not what it was 15 or 20 years ago.

Victor Miller: Wade, could you just talk a little about the right to reject rule? And is there a compromise position on this between the networks and the affiliates, do you believe?

Greg Schmidt: Could you give away your position in a negotiation?

Victor Miler: That's sensitive, I . . .

Wade Hargrove: No, it's not sensitive at all. I mean, this **is** a very public dispute. There's some difference at the margin, I think, of what the rule really means. First of all, the commission has statutory authority to regulate networks under ***303*** of the Act. And it has given stations a specific mandate under **310(d) of** the Act to retain control and exercise control over the programming and operations of the licensee station every second of the day. And, even in the absence of right to reject, if the commission had not enacted a rule, if it repealed the right to reject rule, in my view, the 310 of the Act would still require that affiliates retain the flexibility to make program decisions on a program-by-program basis and, therefore, retain the right to ***reject*** programs. What the rule itself says, quite simply, is that the licensee shall have the right to substitute an alternative program in lieu of the network program if it believes the content of the network program to be unsuitable for its viewers — obscenity, whatever. . . content unsuitability . . . or, if it believes the alternative program would better serve national, local interests of its viewing area. And, the question arises, the networks believe, in fairness to the network position; the networks contend that the affiliates cannot **use** that rule to take what they characterize as cheap economic preemptions; that is to say, blow out a low-performing network program and put on what the affiliate might be able to do on a onetime only basis — a program that might achieve a higher rating. *Or* a program in which the affiliate might have more inventory. And the affiliate position is there's nothing in the Act or nothing in the rule that speaks to economics; it's not an economic decision. That the affiliate simply has to have a good faith belief, and we're talking about good faith, we're not talking about contrived, but a good faith belief that the network program is not as responsive to the interests of its community as the alternative program. And, in fact, if the alternative program makes more money for the affiliates, for the affiliate, so be it; that's inconsequential, that's not part of the analysis. And the tension has arisen because of the vertical integration. I mean, this tension has always existed between networks and affiliates. The networks' mandate and job responsibility . . . for affiliate relations, the network level is to get clearance of the shows. The affiliate. on the other hand, is faced with the responsibility of trying to provide the best, most competitive programming for its service area . . . regional sports, local sports . . . traditionally, the networks have recognized that in order to maintain its relevancy as a local station, a station has to be sensitive to local program needs. On the other hand. with the ownership of programming by the networks now and the repeal of the fin-syn rules and the syndication rules; the networks have an interest in the aftermarket, the vitality of its network programming and, therefore, wants those shows cleared. It's a natural tension. The issue is pending at the commission. We believe about all the arguments that could ever be made have been made for and against the petition that the affiliates filed. And we hope the commissioner will address those arguments and issue a decision.

Victor Miller: But is there a compromise position where the . . . obviously one argument **is,** you want to show ACC basketball down in Virginia on a local station — you should be able to preempt the show and show ACC basketball. The major complaint [from the broadcast networks] has been, "I'm going to be short on my budget, so 1 want to blow out that show and put **on** a movie." I've got all the inventory, I make my budget, and the network winds up without a clearance and spent a hell of a lot of money not getting a clearance? **Is** there a compromise position where network and the affiliate group can get together and say, look, you got to make me whole to this extent, and then you keep the economics above that, but at least **you** made me whole on my economics of not clearing that show . . .

Dick Wiley: I think a number of the networks have given the affiliates, and Wade knows this, a large basket of acceptable preemptions. And I think, in many instances, that seems to work. In some instances, there are still some.. . . with several of the networks, still some pressure out there. But I think there's been progress made in the relationship, and I just want to say I've *got* clients on both sides of this abyss and . . .

Victor Miller: And you're with your client.

Dick Wiley: And I'm with my clients, right. But, beyond that, 1 think it's very important that solutions be found to this. **I'd** rather see them be found in the private sector than at the commission because I think this relationship has to work. Broadcasters . . . biggest problems lie outside of the industry, as far as competitive pressures are concerned. And I think they need to find solutions to work together, and I think that's happening in most instances — certainly, the ABC affiliate agreement that Wade had such an important role in, it was a good step in that direction. I agree with you.

Wade Hargrove: Dick's right. I think while this petition has been pending, the relationship on some of these very sensitive issues that have divided the two parties — the relationship has improved. The right to reject issue is one that's in front of the commission . . . has nothing *to* do with the application of the rule to any specific program. It simply has to do with whether . . . the issue before the commission is whether the contractual language in these contracts violates the rule. We're asking for a declaratory ruling with respect to the words of the contract. not how it may be applied in a specific context. But the relationship has improved, and there have been several filings by the affiliates to document the fact that some of the original points that were raised in the petition with respect to some networks no longer exist.

Greg Schmidt: Before my current life, I was counsel to the CBS affiliates' association, and this thing has been going on for many: many years. And. in fact. some of the things that were brought up today — the fact that, for example, the third-placed morning show would probably benefit everybody involved, including tlie network involved in its O&Os, if it were replaced with local time. We've been fighting over the allocation of local versus network time forever. There was a suggestion made that maybe there would be an hour . . . that one of the networks would benefit also through its O&Os and reduce its expenditures by doing an hour less of prime time. Maybe. All of those negotiations . . . this rule just means they've got to sit and talk to **us** about those issues and negotiate them, and there does seem to be, frankly, I mean, quite aside from the financial interest rules, there's something in the network economics and mindset that when people go to the network, they lose sight of how to maximize the total pie for everybody in terms of taking into account affiliate interests. And the rule has sort of balanced that, which 1 think is an irrational mindset, for the most part, that we really could find a way to make the pie bigger for everybody. And it's great and encouraging that we're beginning to have talks that I think have the potential to really do that on all the networks.

Dick Wiley: Well, as far as irrationality goes, I mean, I think we have to, as Wade suggested, I mean, they do spend a great deal of money to develop these programs, and, therefore, it is essential for them to get heavy percentages of clearances. **On** the other hand, I agree the local stations have a very important — if we want to have a system **of** localism, then local stations have to maintain some control over the programming that they put into their local community. ***So,*** I'm saying I think practical solutions can be worked out here. I'd rather see them, again, worked out in the private sector.

"The debate is over the extent to which an **affiliate** is compelled by its network to clear **a** show that has **no** vitality."

Wade Hargrove: The irony, if I may add a comment, the irony of it is, the debate is not over clearance of good programs . . . there's nothing wrong with a relationship that a few good shows on all four networks probably wouldn't **fix.** The debate is over the extent to which an affiliate is compelled by its network to clear a show that has no vitality. And particularly with the repurposing now by the networks, which is understandable, nobody's critical of that, but this is **a** very, very important proceeding because the affiliate wants to have the commission validate the fact that — which has always been the commission's position — that it does have a right to make a judgment about the programs on its station and cannot be penalized by its network for rejecting a network program. That's what it's all about.

Victor Miller: Dick, we'd be remiss not to get your update on what you think about the Tauzin and Powell plans on digital television.

Dick Wiley: I would echo some of the statements that were made in the previous panel. I think the government . . . I was a big critic. The government really did not give **us** leadership in the development of this transition; it has done so now. Chairman Powell and the digital television task force under Rick Chcssen. I think. stepped tip, come up with an interesting plan. and just put the plan out there. He's working with the industry to try to get private sector solutions to many of these issues. I really think the whole issue of cable interoperability is just a few weeks away, perhaps, from a terrific solution. That's been a huge problem that you buy the set and take it home, and it doesn't work on cable. For 70% of the audience, that's a real impediment. I think that's going to change. I think the programming is developing, the receivers are terrific. The copy protection is the big one, assuming cable interoperability is out there, that needs to be solved. **And,** of course, the commission should step up to the plate now and decide this cable carriage issue. I do agree also that the idea of experimentation to encourage broadcasters to look at standard definition multicasting during the daytime. I think ultimately they'll develop business plans that will make them money in a second revenue stream. I think that's important. If it's not carried, that's a real problem. So, I think both Chairman Powell and Billy Tauzin and other people on the Hill deserve a lot of credit for getting the leadership, but the industry is also, I think, moving to this transition. I'm more encouraged about the **DTV** transition than I've ever been before. I think it's going to work..

Victor Miller: Are there any questions from the audience?

Chris Gleason: Yes, hi, I just have a few questions. One, what is the FCC's position today with regard to open access and rate regulation? And, the second part, of the three Republican commissioners, which one may be a swing factor to potentially slowing the deregulatory forces?

Dick Wiley: Well, on the latter, none of the above is the answer I would give there. I think all three commissioners on the Republican side — I hope on the other side, too — will see that we need change. ***So,*** **1** don't see a swing vote there. You want to comment on the other issue?

Greg Schmidt: I'm really not up to speed on the others. I think the open access issue is — well, rate regulation is, at least for the moment, dead. It may revive. I'm particularly optimistic, since it's one **of** my little pet peeves, the issue that's come **up** a couple of times today, which is the basic tier arrangement and the move to *A* la carte. **I** think that would be potentially of enormous significance to **us** and would help to highlight the kinds of cross-subsidy issues that we've been hearing about today, which I think, unquestionably, have prejudiced **us.** And that if we could move to *A* la carte, it would be great. And, **of** course, the irony there is, of course, the small cable operators are coming in petitioning the commission to hold that the retransmission arrangements that we've gotten, which the cable industry forced on **us,** are a tying arrangement and a violation of the antitrust laws . . . when they're tying **50** or 60 channels together and forcing the consumer to buy those. I think there's no small irony there, **and** McCain is firmly focused on that one, and I hope maybe he'll do something about that in his upcoming set of hearings that he's scheduling for the Commerce Committee.

Dick **Wiley:** And I should say the open access rule I think . . . maybe you'll want to comment on this as well, Wade . . . I think it's all part of the broadband proceeding that the commission's got going, or a series of proceedings. And the question is whether or not we're going to have the same kind of deregulatory regimen for the telephone companies for their DSL service as we have for the cable modem services. And I think the commission's got to solve that issue.

Wade Hargrove: Yes, we really moved past the open access issues. ISPs [Internet service providers] and local governments that have tried to regulate, mandate open access or forced access, as the cable industry chooses to characterize it . . . all those court cases have been victories for the cable industry. And the commission has not mandated it, and the cable MSOs have pretty much taken most of the wind out of those sails by offering . . . opening up their facilities to other competitive Internet service providers. But Dick's point about regulatory parity between regulations of Internet access by — which is provided by telephone companies and that provided by cable — is an emerging issue that's going to occupy a lot of attention both at the state level and at the federal level.

Victor **Miller:** Are there any other questions? *Thank* you so much for all of you who made it the whole day.

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