National Association of
NAB
BROADCASTERS

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May 13, 2003

The Honorable Michael K. Powell, Chairman
The Honorable Kathleen Q. Abernathy, Commissioner
The Honorable Michael J. Copps, Commissioner
The Honorable Kevin J. Martin, Commissioner
The Honorable Jonathan S. Adelstein, Commissioner
Federal Communications Commission
445 Twelfth Street, SW
Washington, DC 20554

Re: Television Duopoly Rule; MB Docket No. 02-277

Dear Mr. Chairman and Commissioners:

As the Commission nears the conclusion of its biennial review of the broadcast ownership rules, NAB again urges you to recognize the urgent need for reform of the local television ownership rule to allow duopolies in medium and small markets. Press reports indicate, however, that the staff's recommendation for reforming the duopoly rule would merely modify the existing voice test so as to permit duopolies only in certain markets depending on the number of broadcast television stations in those markets. As the record in this proceeding indisputably demonstrates, this "voice test" approach is not the best approach for reforming the duopoly rule because it will fail to permit duopolies in smaller markets where financially struggling stations most need to adopt more efficient ownership patterns. The public interest in maintaining the viability of small market television stations, and their local news operations, would be better served by the Commission's adoption of an audience share test, such as NAB's "10/10" proposal.

<u>Television broadcasters in medium and small markets are facing severe financial pressures</u>. Several factors have combined to place unprecedented financial pressures on television broadcasters today, especially those in smaller markets. As has been well documented, the costs of the digital television (DTV) transition are substantial for all broadcasters, but are "overwhelming" for many medium and small market stations.[1] Beyond greatly increased expenses due to the DTV transition, local broadcasters are also facing a significant decline in overall revenues as a result of reductions in network compensation payments to affiliated stations. Broadcast networks have already substantially cut the

[1] BIA Financial Network, Inc., *State of the Television Industry 2001, Ownership Report: What Is Owned by Whom and Where* at 7-9 (2001). *Accord* General Accounting Office, Report 02-466, *Many Broadcasters Will Not Meet May 2002 DTV Deadline* at 17-18 (April 2002).

compensation that they traditionally paid to stations that carry their programming, and compensation payments will very likely be eliminated entirely in the future.[2] Stations in smaller markets, which have thinner profit margins than stations in larger markets, are disproportionately adversely affected by these reductions in network compensation. And local television broadcasters are, of course, bearing the expense of the DTV transition and the loss of network compensation at the same time they are facing ever-increasing competition from cable and Direct Broadcast Satellite (DBS).[3] NAB stresses that these pressures on local station finances will only continue to mount in the future.

These three factors – the costs of the digital transition, reductions in network compensation, and increased competition – have combined to create a challenging competitive environment for local stations in medium and small markets. A report prepared by NAB clearly demonstrated the dire financial situation of television stations, especially the lower rated ones, in smaller markets. NAB's study examined the profitability of ABC, CBS, Fox and NBC affiliated stations in DMAs ranked from 51-175 in 1993, 1997 and 2001. It showed that the average low-rated affiliated station in these markets not only experienced declining profitability from 1993 to 2001, but, as of 2001, the average low-rated station experienced *negative* profitability. The steepness of the declines in profitability of these stations was also striking. For example, in markets 101-125, the average low-rated station suffered an astounding *581% decline* in pre-tax profits from 1993 to 2001, and low-rated stations in markets 76-100 and 126-150 experienced average *declines of 320% and 301%*, respectively. And even the average *highest-rated* affiliated stations in markets 51-76, 76-100 and 126-150 experienced declining profits from 1993 to 2001. *See TV Financial Report* at 5-9.[4] Certainly the financial pressures on low-rated stations in smaller markets are sufficiently severe to call into question their continued viability as independent operations, or, at the very least, to threaten the viability of local news operations at these stations. NAB also emphasizes that this evidence concerning the seriously declining financial position of smaller market broadcasters has not been refuted, or *indeed even challenged, by any commenter in this proceeding*.

<u>The declining financial position of smaller market television broadcasters threatens the viability of their local news operations</u>. Other commenters in this proceeding have documented the significant number of television stations that have already reduced or eliminated their local

[2] *See* Comments of NAB in MB Docket No. 02-277, Attachment C, *The Declining Financial Position of Television Stations in Medium and Small Markets* at 5-9 (Dec. 2002) (*TV Financial Report*) (showing that network compensation to affiliated stations in Designated Market Areas (DMAs) ranked 51-175 declined substantially from 1997 to 2001).

[3] *See, e.g.*, J. Levy, M. Ford-Livene, and A. Levine, OPP Working Paper Series #37, *Broadcast Television: Survivor in a Sea of Competition* at ii, 20, 22 (Sept. 2002) ("DBS and the expansion in cable availability and channel capacity have created an increasingly competitive environment for television broadcasting," as cable has already "cut substantially into the broadcast audience" and "broadcast [viewing] shares are likely to continue to fall").

[4] *See also* NAB *Ex Parte* in MB Docket No. 02-277 (April 30, 2003) (showing that (i) the decline in average gross revenues from large markets to small markets is considerably more rapid than the decline in the number of stations, so that a proportionately greater number of stations in smaller markets compete for far smaller total revenues than do stations in larger markets; and (ii) both average revenues per station and average market revenues by household decline steeply in smaller markets).

news operations.[5] And as the financial situation of stations, especially lower-rated ones, in medium and small markets continues to worsen, many additional stations may have no choice but to cease or cut back on their local news operations. A study by media consultants Smith Geiger found that the "costs of starting up and maintaining a local television news operation in medium and small markets continue to increase," while "audience" share and "revenue" are "more and more difficult to come by."[6] Because acquiring alternative programming (such as syndicated programming) "represents a much lower cost than news production," one can therefore only expect more local stations to "forego their news" for the "cheaper, less financially risky, and often more profitable option of acquired programming." *Smith Geiger Newsroom Report* at 13-15. Again, these findings about the financial viability of local news operations remain unrefuted.

The record in this proceeding clearly demonstrates the case for reforming the television duopoly rule in medium and small markets. Permitting common ownership of two stations in smaller markets will provide greatly needed financial relief to stations in these markets, help ensure the long-term viability of lower-rated stations and the viability of local news operations at all smaller market stations, and strengthen local broadcasters in competing against cable and DBS.

<u>An audience share test, rather than a voice test that counts only broadcast television stations, would be more effective in preserving local stations and their local news operations in smaller markets</u>. Merely modifying the existing duopoly voice test so as to permit duopolies only in certain markets depending on the number of broadcast television stations in those markets will not adequately ameliorate the looming financial crisis in small market television broadcasting. Under a voice test such as that reportedly proposed by FCC staff, no duopolies at all could be formed in markets lacking the requisite number of broadcast television stations, thereby providing no financial relief whatsoever to the struggling stations (especially the lower-rated ones) in these markets.

In contrast, an audience share test, such as NAB's 10/10 proposal, would allow duopolies in almost all DMAs, subject to an audience share limitation. Under this standard, two stations each with a year-long average 7:00 a.m.-1:00 a.m. viewing share of less than 10 could be commonly owned, and a station with a viewing share of 10 or more could be co-owned with another station with a share of less than 10.[7] NAB's proposed rule would provide greatly needed financial relief for stations in medium and small markets that are facing seriously declining economic conditions. The rule would in particular provide regulatory relief for struggling low-rated stations by allowing two lower-rated stations to combine to form a stronger entity, or by permitting a lower-rated station (many of which are unprofitable) to combine with a profitable, competitively viable higher-rated station. At the same time, NAB's proposal would still promote

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[5] *See, e.g.*, Comments of Media General, Inc. in MB Docket No. 02-277, at Appendix Three, Attachment B.

[6] Smith Geiger, *Newsroom Budgets in Midsize (51-100) and Small Markets (101-210)* at 2, 15 (Dec. 2002), Attachment D to Comments of NAB in MB Docket No. 02-277 (*Smith Geiger Newsroom Report*).

[7] These viewing shares are determined by Nielsen four times a year, and they reflect each station's share of *total* viewing in each DMA, appropriately taking into account the significant viewing of broadcast stations located outside the market and, especially, of cable networks/channels.

the FCC's traditional goals of competition and diversity by preventing the combination of two higher-rated stations in the same market and by encouraging combinations between stronger and weaker stations, thereby preserving voices and promoting programming diversity. For all these reasons, the adoption of a broadcast-only voice test that fails to permit television broadcasters in DMAs of all sizes to reduce costs by combining operations will inevitably prevent many smaller market broadcasters from completing the expensive digital transition, from maintaining their local news operations, and even from surviving as competitively viable operations.

The record in this proceeding also demonstrates the clear benefits to be derived from permitting duopolies in local markets of all sizes. The Commission should not be hesitant to adopt an audience share approach that would allow duopolies to be formed in DMAs of all sizes, subject to an audience share limitation. Commenters in this proceeding with existing duopolies and local marketing agreements (LMAs) have demonstrated that these same market combinations – beyond merely preserving existing news operations – can also improve news operations and can lead to the commencement of such operations at stations formerly without any locally produced news.[8] You will recall the testimony of Edward Munson of LIN Television at the Commission's hearing in Richmond. Mr. Munson described in detail how combining with another station in the same market enabled a technically deficient home shopping station in Norfolk, Virginia to be transformed into a major network affiliate with a local news operation that is transmitting in digital. Indeed, additional studies submitted in this proceeding demonstrated that stations in duopolies and LMAs have outpaced standalone stations in the transition to digital broadcasting and have outperformed standalone stations in attracting both viewers and advertising revenue.[9]

In sum, the record provides ample support for the Commission to reform the local television ownership rule to allow duopolies in markets of all sizes. Just as the Commission acted in 1992 to liberalize the local radio ownership rules when the radio industry (and particularly smaller stations) were suffering financially, the Commission should similarly act here to ensure the "economic viability" of local television broadcasters and therefore their "ability to function in the 'public interest, convenience and necessity.'" *Report and Order* in MM Docket No. 91-140, 7 FCC Rcd 2755, 2760 (1992). If the Commission wishes to protect consumers' access to free, over-the-air television, including such costly programming as local news – a goal NAB strongly supports – then the Commission must reform the duopoly rule to ensure the continued economic viability of local broadcasters providing free, over-the-air service in all DMAs, including the smallest.

A voice test that counts only broadcast television stations ignores unrefuted evidence in the record about competition in local video markets and appears difficult to reconcile with the opinion of the D.C. Circuit Court of Appeals in *Sinclair v. FCC*. In that case, the court remanded the FCC's existing duopoly rule, holding "that the Commission has failed to

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[8] *See, e.g.*, Comments of Nexstar Broadcasting Group and Quorom Broadcast Holdings at Appendix A; Belo Corp. at 22-24; and Coalition Broadcasters at 15-33 in MB Docket No. 02-277. These commenters also showed that same-market combinations allowed them to improve other programming services to the public, including local sports, weather, specials and programming focusing on minority communities.

[9] *See* Comments of Coalition Broadcasters at Attachment B; BIA Financial Network, *Television Local Marketing Agreements and Local Duopolies: Do They Generate New Competition and Diversity?* (Jan. 2003), Attachment A to Comments of Coalition Broadcasters in MB Docket No. 02-277.

demonstrate that its exclusion of non-broadcast media in the eight voices exception is not arbitrary and capricious." *Sinclair*, 284 F.3d 148, 152. The adoption of a broadcast-only voice test that would not permit duopolies in many smaller markets appears particularly questionable under *Sinclair*, given the remarkably low levels of television viewing attributable to in-market broadcast stations in DMAs ranked 101-210. A study conducted by BIA Financial Network showed that, in DMAs 101+, only *39.7 percent* of total day viewing is attributable to the in-market broadcast stations that would be counted in a traditional voice test.[10] Even in medium-sized markets (DMAs 51-100), only 50.0 percent of total day viewing is attributable to in-market broadcast television stations, and in *no* market grouping does the percent of viewing attributable to local broadcasters reach 60 percent. Moreover, the viewing of in-market television stations has declined by 17 percent in just the last five years.[11] Thus, a revised duopoly rule based, like the current rule, on a count of only the broadcast television stations located in each DMA, seems inconsistent with applicable judicial precedent and the evidence in this proceeding.[12]

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Based on undisputed evidence submitted by NAB and others in this proceeding, the public interest in maintaining the viability of small market television stations, and their local news operations, would be better served by the Commission's adoption of an audience share test, such as NAB's 10/10 proposal, than by a voice test that counts only the number of broadcast television stations located in each DMA. NAB therefore again urges you to reform the television duopoly rule so as to permit the formation of duopolies in DMAs of all sizes, depending on the share of total viewing earned by the local stations in question.

Respectfully submitted,

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[10] In these small markets, over 60 percent of the viewing accordingly goes to cable/satellite channels and to broadcast stations located in other DMAs.

[11] *See* BIA Financial Network, *Out-of-Market Listening and Viewing: It's Not to be Overlooked* at 15-16 (Jan. 2003), Attachment A to NAB Comments in MB Docket No. 02-277.

[12] And if the voice count methodology chosen by the Commission were to fail to include noncommercial stations, then any revised duopoly rule would also be deficient for ignoring yet more outlets that compete for viewers in local video markets.