These facts supported by this evidence formed the basis for the Commission's decision in the *1998 Biennial Review*. As Granite demonstrates in its Reply Comments, none of these facts have changed, and the Commission consequently has no basis for reversing its decision.[12]

Moreover, the evidence provided in the *1998 Biennial Review* and in this proceeding disprove Capitol's assertion that the UHF Discount "result[s] in our current 35% cap actually being a 70% cap . . ."[13] In the analog world, UHF stations simply do not have the ability to reach anything approaching every household in their DMAs, even when cable carriage is considered. PCC presented evidence showing that in some cases, its stations covered as little as 27% of the area covered by VHF stations in the same market, and, in one case, could obtain cable carriage of only 4 of the 29 counties in the station's DMA.[14] Because cable carriage is based on a station's ability to deliver a quality signal to a sometimes distant headend, it is not surprising that UHF stations would be unable to garner the same level of cable carriage as their VHF counterparts. These types of disparities continue to exist and, with the additional DTV-generated interference noted by Univision and PCC, will only be made worse as additional DTV stations commence full power operations.

The persistence of all these physical and economic handicaps serve to confirm the wisdom of the Commission's retention of the UHF Discount in the *1998 Biennial Review*. Counting each UHF station as reaching only 50% of the households in its DMA allows station-group operators like PCC and Univision to use the UHF Discount to acquire and operate stations that otherwise might fail, enabling them to serve niche audiences that are frankly underserved by the Big Four networks. Rather than seeking ways to curtail UHF broadcasting by eliminating the Discount, the Commission should be seeking ways to encourage this type of service to the public.

It Is Far Too Early for the Commission to Conclude that the DTV Transition Will Render the UHF Discount Obsolete.

The Commission also found in the *1998 Biennial Review* that completion of the DTV transition might make it appropriate to modify or eliminate the UHF Discount.[15] Accordingly, the Commission indicated that it would conduct a rulemaking to examine the Discount's future near the close of the DTV transition.[16] As PCC indicated in its Comments, the DTV transition has not progressed sufficiently to determine whether the Commission's predictions will be accurate. As described above, Univision has persuasively demonstrated that the transition itself is harming analog UHF broadcasters' ability to serve their viewers, and that such harm is likely

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[12] *See* Granite Reply Comments at 6.

[13] *See* Capitol *Ex Parte* at 1.

[14] *See* PCC Comments in MM Docket No. 98-35, filed July 21,1998 at 7; PCC Reply Comments in MM Docket No. 98-35, filed August 21, 1998 at 5-7.

[15] *See 1998 Biennial Review*, 15 FCC Rcd 11058 11079-80.

[16] *See id.*

to increase as the transition progresses. Accordingly, eliminating the UHF Discount now based on the possibility of future obsolescence would be a grave error based on unsubstantiated speculation.

The Commission cannot yet be certain that the UHF Discount will not be needed in the post-transition world. Although the Commission properly has noted that UHF broadcasters' ability to maximize their service area could be an equalizer between UHF and VHF stations,[17] the Commission should be equally aware that its decision to base its initial DTV Table of Allotments on a principle of replication of service has locked in the signal-coverage disparities of the analog world. For example, in the Seattle market, PCC station KWPX-DT currently is licensed with 175kW ERP, while ABC affiliate KOMO-DT operates at 810 kW. Likewise, in the Washington, D.C. area, PCC station WPXW-DT is licensed at a power of 90 kW, while ABC affiliate WJLA-DT is licensed at 646 kW. As a consequence , PCC reaches 30% fewer Washington area viewers – or nearly 1,000,000 fewer viewers – than WJLA-DT. If these types of disparities remain widespread in the digital world, then some discount will be required if the Commission wishes to maintain the integrity of the over-the-air broadcast system. Thus it is simply too early to tell whether the UHF Discount will be needed in the DTV world. The Commission should follow the path laid out in the *1998 Biennial Review* and defer consideration of the rule until the post-transition world begins to take shape.

The Commission Cannot Use a Section 202(h) Review to Re-Regulate Broadcasters.

As PCC and Granite have pointed out, the Commission's responsibility under Section 202(h) of the Act is to evaluate its restrictions on broadcast ownership in the light of current levels of competition. Section 202(h) does not empower the Commission to impose new or increased restrictions through the biennial review process. Even if it did, however, the Commission still would bear a tremendous burden to show by the clear weight of the evidence that such new or increased restrictions are justified by the available evidence.

As demonstrated above, the parties advocating re-regulation of UHF broadcasters have presented no evidence to support that result. Consequently, the Commission has been given no justification for a conclusion that increased regulation of UHF broadcasters is at all warranted, let alone necessary in the public interest. It would be a perverse result indeed, if the Commission used this proceeding – intended by Congress to be a vehicle for principled deregualtion – to re-regulate a class of broadcasters without any evidence to support that effort.

Conclusion

Finally, the Commission must recognize that eliminating the UHF Discount would be flatly inconsistent with nearly all the Commission knows about UHF broadcasting. Even if the Commission could find that the 50% discount underestimates somewhat the number of households some UHF broadcasters reach, it knows even more certainly that ascribing them the same viewership as is ascribed to local VHF stations would substantially overestimate their

[17] *See id.*

accessible audience. The Commission also knows that UHF stations already are competitively disadvantaged as compared to their VHF counterparts. Given their extensive competitive handicaps, it would be much more reasonable to err on the side of undercounting rather than overcounting UHF broadcasters' audience. Perhaps the greatest burden the Commission would bear in this entire proceeding would be to explain how it could possibly be necessary in the public interest to eliminate a rule that injures no one and contributes so much to the level of competition in the American broadcasting system. The Commission cannot meet that burden on this or any other record containing even a kernel of common sense. Accordingly, the Commission must reaffirm its findings and conclusions in the *1998 Biennial Review* and find that the UHF Discount continues to be necessary in the public interest.

Respectfully Submitted,

John R. Feore, Jr.
Counsel for Paxson Communications Corporation

Attachments

cc w/ attachments:

Chairman Michael K. Powell
Commissioner Katherine Q. Abernathy
Commissioner Kevin J. Martin
Commissioner Michael J. Copps
Commissioner Jonathan S. Adelstein
W. Kenneth Ferree, Chief, Media Bureau
Paul Gallant, Special Advisor, Media Ownership Working Group

bcc: w/ attachments:

Lowell W. Paxson
William L. Watson

I will send with cover letter and a stapled in copy of the filing bbcc w/attachments:

Jason E. Rademacher
Susan E. Anderson

ATTACHMENT

A

The "UHF Penalty" Demonstrated

Stephen E. Everett, Ph.D.

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Audience Measurement and Policy Research

National Association of Broadcasters

July, 1998

Introduction

Do people at home watch a UHF network affiliate less, just because it's a UHF station? The findings reported here suggest the answer is "yes" – even after considering other factors that might enter into the mix, such as a station's network and its DMA rank.

Viewing data gathered in November, 1997, by Nielsen Media Research were analyzed for all Nielsen DMAs in an effort to identify systematic differences in viewing levels between UHF and VHF network affiliates (for the four major networks). In order to minimize programming differences from station to station, only prime-time ratings were included in this analysis. The research question: after controlling for possible intervening factors such as network programming line-up and market size, do UHF affiliates generate lower prime-time ratings than do VHF affiliates, on average? As a follow-up question, are VHF/UHF ratings differences related in any way to network affiliation or market size?

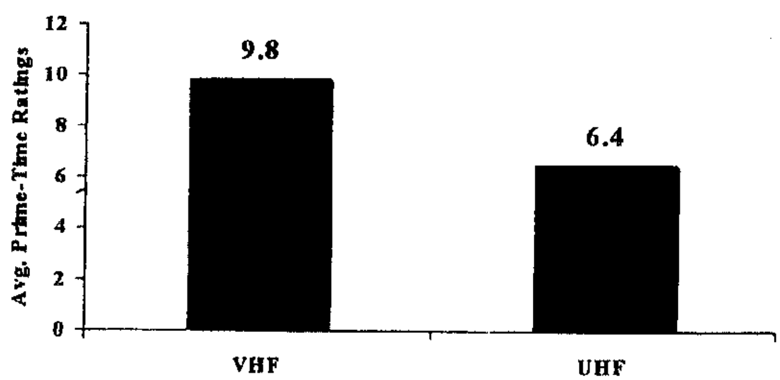
Data analysis was performed using Analysis of Variance (ANOVA).

Results

<u>VHF Affiliates Draw Higher Ratings</u>

As Figure 1 shows, the group of VHF affiliates from all markets in this analysis averaged a 9.8 prime-time rating, while UHF affiliates averaged only a 6.4 rating. This is strong evidence that the conceptual premise for the "UHF discount" remains in force and, consequently, the discount is justified.

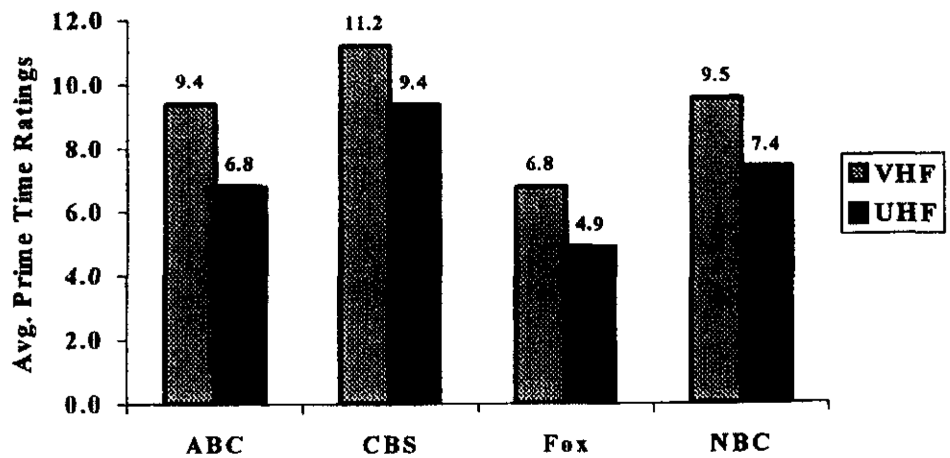
Figure 1
VHF/UHF Ratings Differences



"UHF Penalty" Worse for Some Networks

Figure 2 shows that the difference between VHF and UHF affiliates' average prime-time ratings is more pronounced for ABC and NBC affiliates than for CBS and Fox.[1]

Figure 2
Interaction Between VHF/UHF Status and Network Affiliation



When the mean ratings are adjusted through ANOVA for market size differences and the overall VHF/UHF difference, this result is even more pronounced:

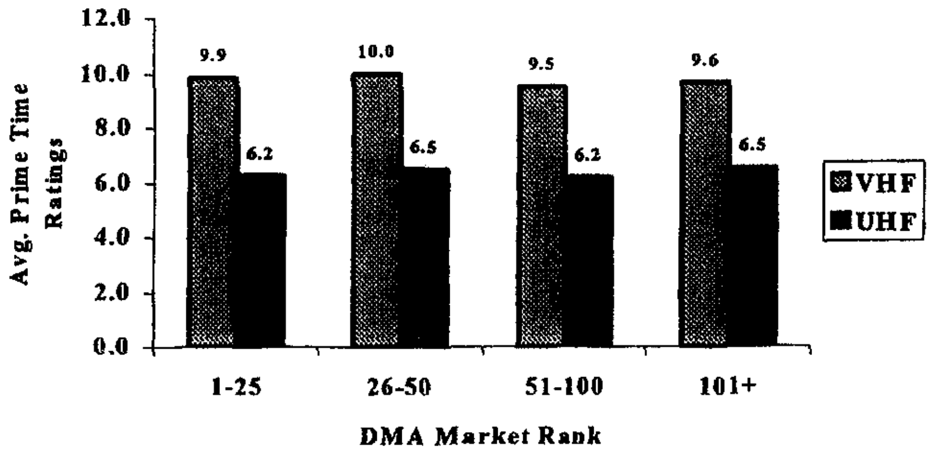
Affiliation	V/U Difference
ABC	3.1
NBC	3.6
CBS	1.2
Fox	1.0

[1] The average rating shown for each network is the unweighted mean of average ratings of affiliates for *all* DMAs (one average rating per affiliate in each DMA). As such, large and small markets have equal influence upon the national averages. Therefore these averages may not reflect the relative positions of the networks as commonly reported.

"UHF Penalty" Present Across All Market Sizes

As shown in Figure 3, the difference between VHF and UHF affiliates' prime-time ratings exists for all four market groups analyzed in this study. There are only very slight differences in the magnitude of these "UHF penalties" from market group to market group.

Figure 3
Interaction Between VHF/UHF Status and Market Size



Conclusion

The "UHF Penalty" apparently continues to exist. When we account for the statistical effects of market size and network affiliation – two factors reasonably expected to be related to prime-time ratings from station to station – strong evidence emerges to continue to support the notion that UHF affiliates draw lower ratings because they are UHF stations.

This "UHF Penalty" shows up across markets of different sizes and for all four networks. However, the penalty is greater for ABC and NBC affiliates. Perhaps the station affiliation changes between CBS and Fox in recent times, in which Fox picked up numerous new VHF affiliates while CBS signed new deals with UHF affiliates, is responsible for diluting the difference somewhat for these two networks. The difference still is there, however.

ATTACHMENT

B

A FINANCIAL ANALYSIS OF THE UHF HANDICAP

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July 1998

A FINANCIAL ANALYSIS OF THE UHF HANDICAP

Introduction and Overview of Study

Within the television industry there is a noticeable distinction between those stations on the VHF and UHF bands. Due to technical properties, the coverage patterns of VHF stations generally are much larger than UHF stations. For a given service area, UHF stations have to use more power, thereby increasing their operating costs compared to VHF stations.

Given their inherent coverage disadvantages, UHF stations tend to attract smaller audiences than for their VHF counterparts, for the same programming.[1] With these smaller audiences, it easily follows that advertising revenues, pre-tax profits, and cash flows should be lower than comparative VHF stations. Of course, there are exceptions to this general conclusion, but we would expect to see a generally worse financial profile of UHF stations as compared to their VHF cohorts.

In this report we examine that hypothesis. Using data collected by NAB, Broadcast Cable Financial Management Association (BCFM), and Price Waterhouse, we can evaluate the past four years worth of data to determine whether UHF stations face a financial disadvantage.[2] These data are from an annual survey of all commercial television stations that attracts nearly a 70% response rate providing a reliable picture of the financial situation faced by commercial television stations.

To try and focus in on the impact of the UHF disadvantage we only examine affiliates of the four major networks – ABC, CBS, Fox, and NBC. By only looking at these stations we can compare stations with identical, or near-identical prime-time programming (assuming they clear a similar amount of their network programming). Comparisons are presented on a national historical basis for the years 1993-1996, by market size (Nielsen DMA) and affiliation type for the most recent year that data are available, 1996.

National Comparison

In Figure 1 we present the comparisons of all affiliates from the four major networks for the years 1993 through 1996. Three station's variables are compared – net revenues, pre-tax profits and cash flows. The averages for these two groups of stations are compared to generate the reported percentage.

The relative performance of UHF affiliates has improved in the four years shown, though they still suffer from a noticeable disadvantage, with the average UHF affiliate generating less than 50% of average VHF affiliate revenues, slightly more than a third of the cash flow and less than a quarter of the pre-tax profits.

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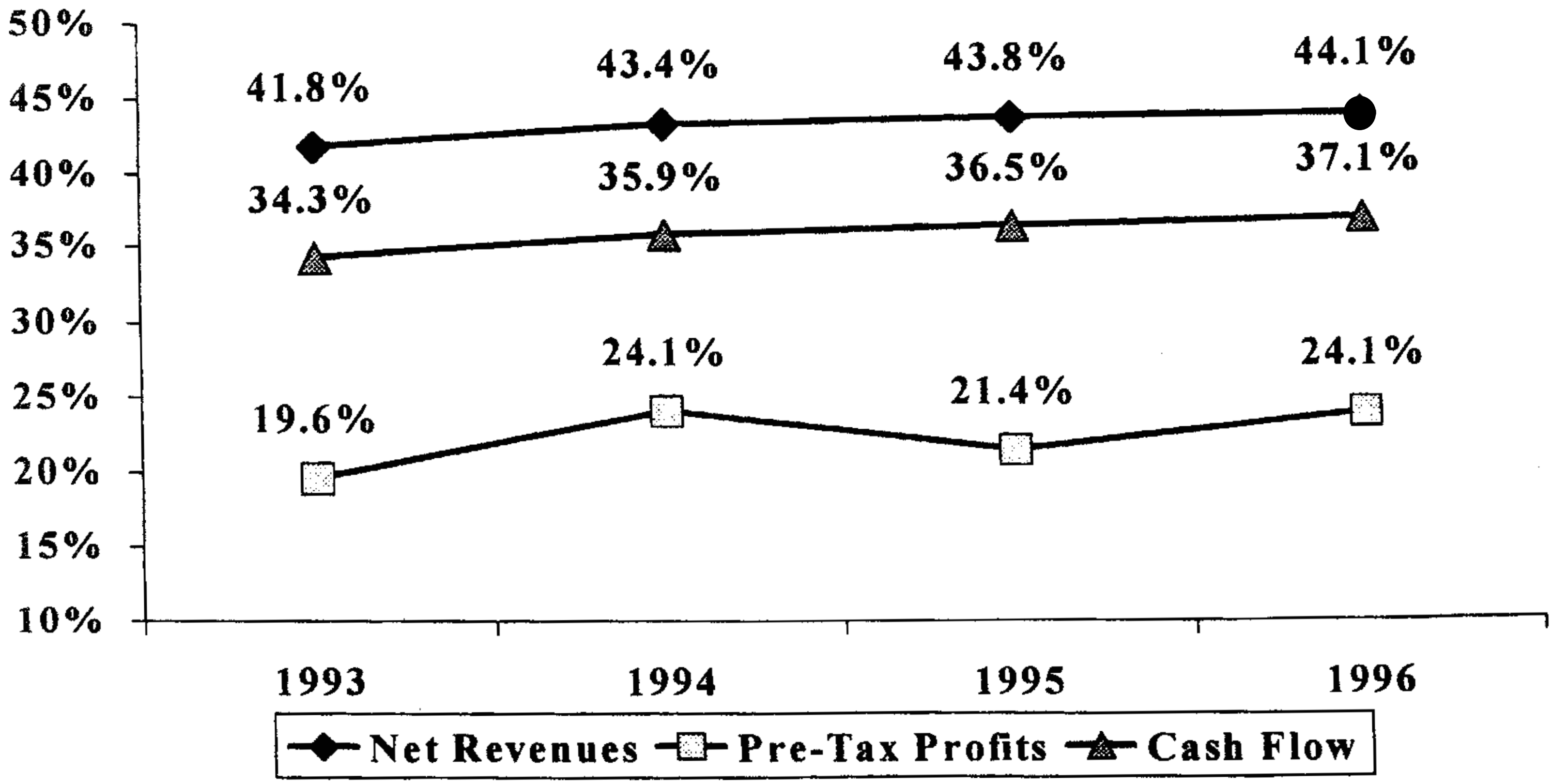
1 See S. Everett, "The 'UHF Penalty' Demonstrated," Appendix C, Comments of the National Association of Broadcasters, in MM Docket 98-35.

2 Unfortunately, the data from previous years (before 1993) are not available for easy analysis.

Figure 1
UHF Affiliates* Performance as a Percentage of VHF Affiliates*



* Includes ABC, CBS, Fox & NBC affiliates

Source: 1994 - 1997 NAB/BCFM Television Financial Surveys.

Market Size Comparison

This disadvantage is evident when examined on a market size basis. Figure 2 shows the same comparative values for four market size groupings for 1996. What is particularly noticeable is that the disadvantage becomes less pronounced when you examine the smaller markets. In fact, in the smallest markets, DMA rankings 101 and above, the UHF affiliate generates only 20.3% less in revenues, 30.0% less in cash flow, and 32.7% less in pre-tax profits.

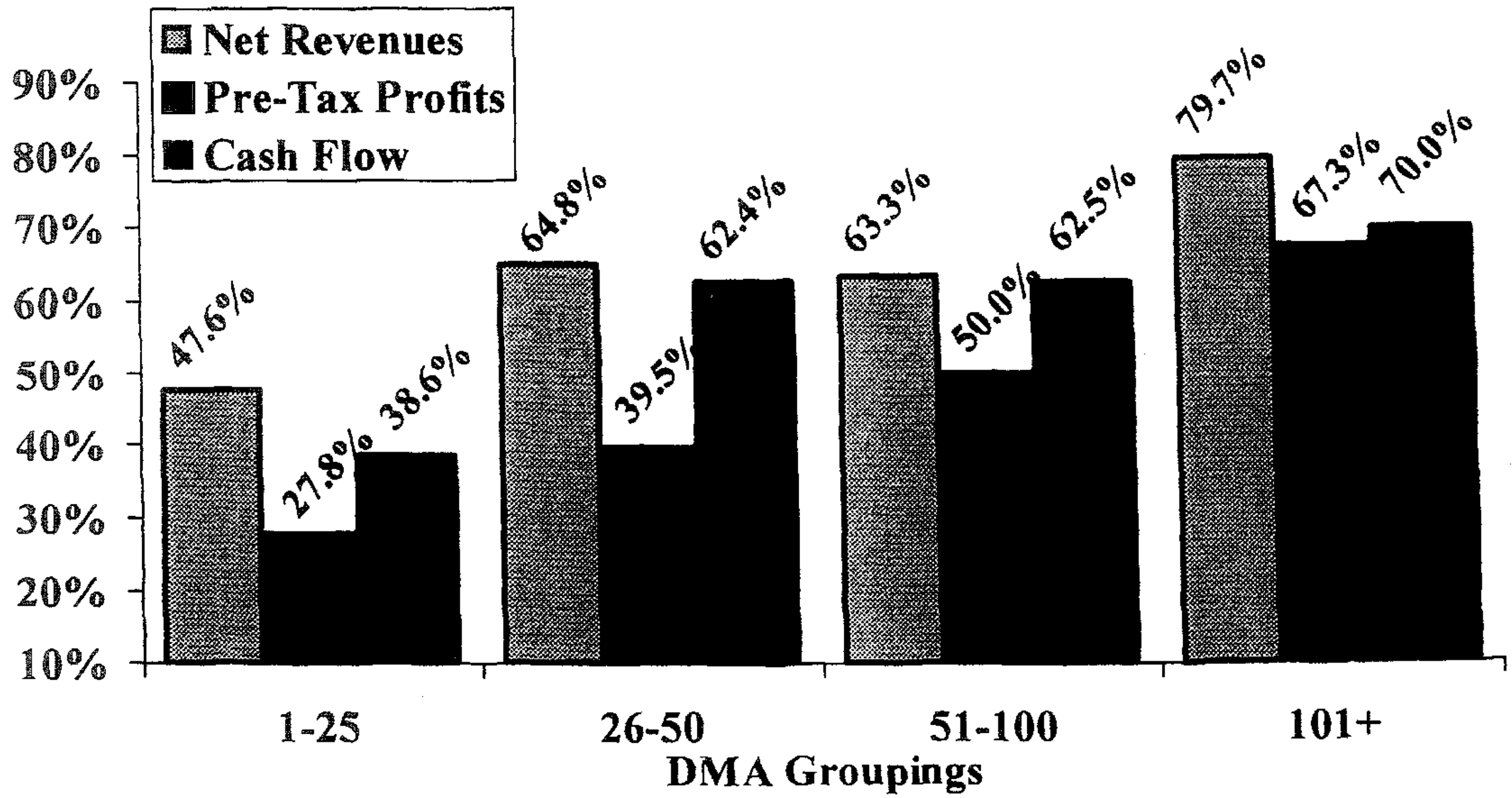
Affiliate Type Comparison

The final comparison is with the different affiliate types. Figure 3 shows the comparative values for the four major affiliate types for 1996. All comparisons reinforce the UHF disadvantage, though to vastly different degrees. In fact, the average UHF CBS affiliate actually generated a loss while the average VHF affiliate generated positive pre-tax profits. On the other hand, the average UHF CBS affiliate came closest to their VHF counterpart in terms of net revenues, generating nearly 50% of that value.

Conclusion

By examining the relative values for UHF and VHF affiliates nationally for the past four years, by market sizes and by networks, one only can conclude that UHF stations fared worse than their VHF counterparts. While in some cases (e.g., UHF stations in the smallest markets) that poorer performance is small, in all cases by examining several financial indicators (net revenues, pre-tax profits and cash flows) UHF stations still face a disadvantage.

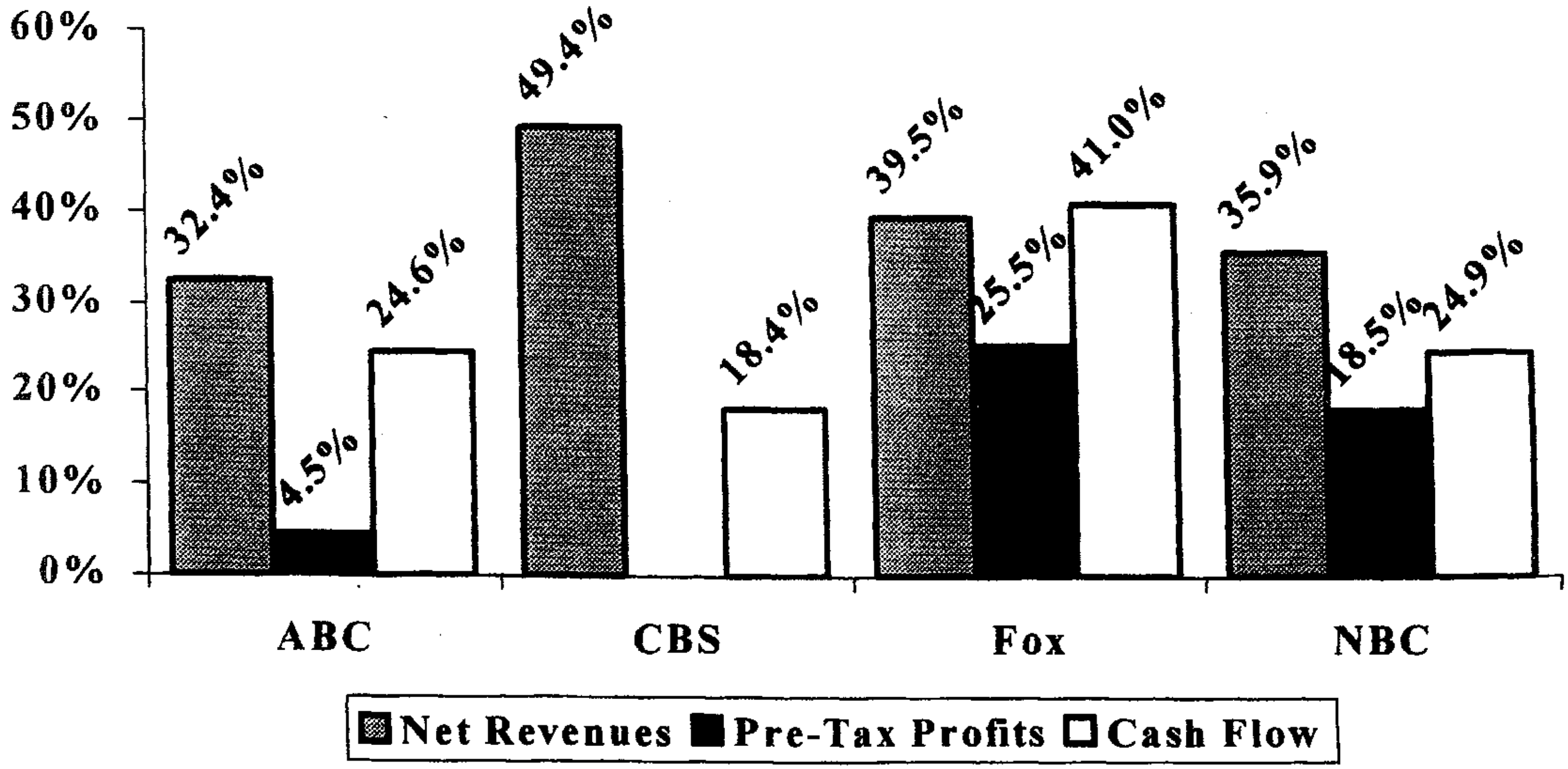
Figure 2
UHF Affiliates* Performance as a Percentage of VHF Affiliates* By Market Size in 1996



* Includes ABC, CBS, Fox & NBC affiliates

Source: 1994 - 1997 NAB/BCFM Television Financial Surveys.

Figure 3
UHF Affiliates Performance as a Percentage of VHF Affiliates By Affiliation Type in 1996



Source: 1994 - 1997 NAB/BCFM Television Financial Surveys.

ATTACHMENT

C

Reply Comments of Paxson Communications Corporation, MM Docket No. 98-35, pp. 2-27, filed August 21, 1998.

I. INTRODUCTION.

The same rationale which supported adoption of the UHF discount in 1985 warrants retaining the discount as the television industry moves toward the 21st century. UHF stations remain at a serious technical and competitive disadvantage to VHF stations. In its *Notice of Inquiry*, the Commission questions whether "improved television receiver designs, as well as the fact that many households receive broadcast channels via cable rather than by over-the-air transmission" have "corrected" the UHF/VHF disparity and therefore warrant eliminating the discount.[2] As shown herein, although advances in receiver technology and mandatory cable carriage have allowed UHF stations to improve economically, the physical disparity between UHF and VHF television signals remains and still places UHF stations at a disadvantage vis-a-vis their VHF competitors. The Commission's suggestion that the conversion to digital television will further "equalize" UHF and VHF stations' signal reach is inaccurate. The Commission has continued the disparity by limiting the DTV power granted to UHF television stations. Accordingly, the UHF discount must remain intact to ensure UHF stations' continued ability to compete effectively in the DTV world.

Retaining the discount also will be critical to the development of new broadcast networks. Although the three largest broadcast networks -- ABC, CBS, and NBC -- own a small fraction of their affiliates,[3] they are becoming economically unfeasible, and a new broadcast network utilizing UHF stations and subsequently lower power digital television

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[2] *Id.* ¶¶ 26, 27.

[3] ABC owns 10 of its 193 affiliates, CBS owns 14 of 210 affiliates and NBC owns 11 of its 214 affiliates. *See* sources cited *infra* notes 40-41; <ABC, http://www.abc.com/local stations/>; *Broadcasting & Cable Yearbook 1998* at F-77-83.

stations will be unable to succeed in the long term unless it owns its network distribution system. Paxson is well-acquainted with the challenges of establishing a new broadcast network. In less than two months (on August 31, 1998), Paxson will launch the seventh broadcast network, PAXTV, which will air a seven day a week schedule of family-oriented programming to communities across the United States. PAXTV will compete with the six existing networks for advertisers and viewers, enhancing the level of competition and diversity among the broadcast networks as well as cable networks. The UHF discount has enabled Paxson to acquire a significant number of UHF stations that will serve as its new network's primary distribution system. Absent the UHF discount, however, Paxson's ownership of a majority of its distribution would not be possible, and the PAXTV network would not exist.

In addition to retaining the UHF discount, the Commission should increase to 40% the national audience share cap on television station ownership. An increase by only 5% would not adversely impact competition or diversity at the national level and would provide important economic benefits for emerging networks.

Paxson also urges the Commission to relax the television ownership rule in one small but strategic way.[4] As Paxson has asserted in its comments in related rulemakings, the increasingly competitive and diverse nature of the television industry warrants changes in the rule. The Commission should modify the ownership rule to permit common ownership of television stations in separate Designated Market Areas, as defined by A.C. Nielsen, irrespective of contour overlap. Use of these separate, defined markets to determine

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[4] 47 C.F.R. § 73.3555(b)(1998).

permissible ownership would reflect far more accurately the economic realities of television service and competition than the current Grade B contour overlap standard.

II. THE UHF DISCOUNT.

A. Background.

Since 1985, the Commission's UHF discount rule has fostered the economic development of UHF television stations. In December of 1985 there were 365 UHF commercial television stations operating in this country.[5] Since that time, the number has grown to 652, a 42% increase.[6] The FCC adopted the UHF discount in connection with its overall review of the national television ownership rule which at that time provided that an entity could own up to 12 television stations nationwide so long as the stations' aggregate audience reach did not exceed 25% of television households in the U.S.[7] The Commission applied and continues to apply the UHF discount to determine compliance with the audience limit cap, now 35% of total U.S. television households.[8] In calculating a UHF station's audience reach, the Commission attributes to that station only 50% of the audience in its market whereas a VHF station is attributed with 100% of the audience in its market.[9]

5/ *Broadcasting Cablecasting Yearbook 1985* at A-2.

6/ *Broadcast Station Totals as of May 31, 1998, News Release* (rel. June 19, 1998).

7/ *See Amendment of Section 73.3555 of the Commission's Rules Relating to Multiple Ownership of AM, FM and Television Broadcast Stations*, *Memorandum Opinion and Order*, Gen. Docket No. 83-1009, 100 FCC 2d 74 (1985) ("*1985 MO&O*").

8/ 47 C.F.R. § 73.3555(e).

9/ *Id.*

As the Commission stated in its *1985 MO&O*, the UHF discount's underlying purpose was to address the technical disparity between UHF and VHF stations. It was well-established at that time, and still is, that UHF station signal strength declines more rapidly over distance than VHF station signal strength. Because UHF stations by their very nature are unable to reach as many viewers as VHF stations, the Commission found that the technical disparity created a significant economic disparity, reducing competition among VHF and UHF stations and adversely impacting diversity. The UHF discount, thus, was designed to level the television playing field so that UHF stations would be in a much stronger position to compete with VHF stations. Nothing has changed since that time to establish equality of coverage between UHF and VHF stations.

B. The Same Rationale Underlying Adoption of the UHF Discount Warrants Retaining the Discount.

The disparities between UHF and VHF stations that existed in 1985 have not changed over the last 13 years. Although economically, due largely to changes in receiver technology and mandatory cable carriage, UHF stations are in an improved competitive position, the playing field vis-a-vis VHF stations remains uneven. Moreover, the cost of operating a UHF station continues to exceed the cost of operating a VHF station. In addition, it is too early in the digital television transition to predict its impact on the traditional UHF/VHF disparity. These circumstances warrant retaining the UHF discount.

1. Changes in Technology and Cable Carriage Have Not Created a Level Playing Field Among UHF and VHF Stations.

The last 15 to 20 years have witnessed dramatic changes in the television industry that have benefitted UHF stations. There have been significant advances in television receiver technology making it easier for viewers to receive UHF signals over the air.[10] In 1997, the United States Supreme Court upheld the constitutionality of the FCC's mandatory cable carriage rules.[11] Those rules,[12] adopted by the FCC pursuant to the Cable Television Consumer Protection and Competition Act of 1992,[13] established the rights of television stations to mandatory carriage on cable systems within their television market. These rights have been critical to ensuring that UHF stations could reach via cable viewers who could not receive UHF station signals over the air especially in larger cities with large multi-family dwellings.

Unfortunately, receiver technology and mandatory carriage have not completely solved the basic disparity between UHF and VHF television stations -- the difference in over-the-air signal strength. The fact remains that UHF stations, based on technical disparity alone, do not reach as many viewers with an over-the-air signal as VHF stations. Although an improved television receiver may make it easier for a viewer to receive a UHF station's signal, receiver technology does not and cannot enhance signal strength nor can it overcome the topographic conditions that substantially weaken a UHF station's signal but have a minimal impact on VHF signal transmissions. It is well-established that the inherent propagation characteristics of a UHF channel make its signal transmissions far more

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10/ *Notice of Inquiry* ¶ 26; *Broadcast Television National Ownership Rules, Notice of Proposed Rule Making*, MM Docket Nos. 96-222, 91-221, 87-8, 11 FCC Rcd 19949, 19954 ¶ 12 (1996).

11/ *Turner Broadcasting System, Inc. v. FCC*, 117 S.Ct. 1174 (1997).

12/ *See* 47 C.F.R. §§ 76.51-76.70.

13/ Pub.L.No. 102-385, 106 Stat. 1460 (1992).

susceptible to terrain obstructions than VHF signals. VHF signals more easily can "bend" to accommodate terrain factors than can UHF signals. There is accordingly, an inherent technical handicap that cannot be corrected with receiver technology. These disparities are evidenced by the following Grade B coverage comparison of certain Paxson stations to VHF stations in the same market.

	Paxson coverage as percent of VHF Stations
Boston, MA	27%
San Francisco, CA	54%
Philadelphia, PA	57%
Washington, DC	62%

Similarly, mandatory cable carriage does not resolve the problem of how a UHF station reaches viewers who do not subscribe to cable. Cable penetration has increased over the past 13 years,[14] but there remains a substantial number of television households that do not subscribe to cable. Indeed, cable penetration in the United States in 1997 was only 65%.[15] In the five largest Designated Market Areas ("DMA") in the United States, as defined by A.C. Nielsen, cable penetration is less than or barely exceeds 75%. Cable penetration in the New York, New York DMA is 71%, and in the Los Angeles, California

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[14] In 1985, cable penetration in the U.S. was 43.7% of U.S. households. *Broadcasting Cablecasting Yearbook 1985* at D-3. Cable penetration increased to 57.1% in 1990. *The Broadcasting Yearbook 1990* at D-3.

[15] *Broadcasting & Cable Yearbook 1998* at xxxi.

DMA is 63%.[16] The Chicago, Illinois DMA has a cable penetration of 62%, and the Philadelphia, Pennsylvania DMA has a cable penetration of 76%.[17] The San Francisco, California DMA has a cable penetration rate of 71%.[18] Thus, in these five largest markets alone, approximately 25% or more of the television households do not receive cable. Moreover, a significant percentage -- 55% -- of total television viewing in United States cable homes is on non-cable connected television sets. In cable homes, there are, on average, 2.6 television sets but only 1.4 are connected to cable.

In sum, notwithstanding must-carry and the expansion of cable, 30% to 35% of U.S. households still do not have cable. Because of their inferior signal strength, UHF stations are seriously handicapped in their ability to deliver a viewable signal to these non-cable viewers. Accordingly, neither cable penetration nor cable carriage of broadcast signals provides any justification whatsoever for the Commission's suggestion that the UHF handicap no longer exists.

2. *UHF Stations Continue to Operate at an Economic Disadvantage When Compared to VHF Stations.*

As the technical disparity between UHF and VHF stations has continued, so has the economic disparity. Given their weaker signal strength and inability to reach as many viewers as VHF stations, UHF stations simply do not garner the same revenues or audience share ratings as their VHF competitors. Moreover, the costs of operating a UHF station

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16/ *Id.* at C-8.

17/ *Id.*

18/ *Id.*