

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

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<i>In the Matter of</i>)	
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<i>A La Carte and Themed Tier</i>)	MB Docket No. 04-207
<i>Programming And Pricing Options for</i>)	
<i>Programming Distribution on</i>)	
<i>Cable Television and Direct</i>)	
<i>Broadcast Satellite Systems</i>)	
)	

COMMENTS OF THE DIRECTV GROUP, INC.

The DIRECTV Group, Inc. (“DIRECTV”) hereby responds to the Commission’s request for comment on issues relating to a la carte and themed tier programming.¹ In particular, DIRECTV focuses its comments on the proposal under which programmers would be “required to allow [multichannel video programming distributors (“MVPDs”)] to offer their programming on an a la carte or themed-tier basis if the MVPD chose to do so.”² Under this approach, MVPDs could decide whether or not to offer a la carte service to their subscribers.

On its surface, this “voluntary” proposal might appear to benefit MVPDs such as DIRECTV. By requiring programmers to offer their products on an a la carte basis, the new regime would give MVPDs at least some incremental increase in leverage when bargaining with programmers. Moreover, because MVPDs would be allowed to provide

¹ *Comment Requested on A La Carte and Themed Tier Programming and Pricing Options for Programming Distribution on Cable Television and Direct Broadcast Satellite Systems*, Public Notice, DA 04-1454, MB Docket No. 04-207 (rel. May 25, 2004) (“Notice”).

² *Id.* at 2.

their services to customers on an a la carte basis but would not be *required* to do so, MVPDs would ultimately be able to make their own distribution decisions.³

Nonetheless, from DIRECTV's perspective, a la carte distribution brings with it at least two negative consequences for MVPDs and their subscribers. First, everything DIRECTV has seen suggests that programmers would charge extremely high affiliate fees for a la carte distribution and that many networks would not survive such a regime. Second, DIRECTV is quite sure that it would incur substantial costs in offering such service, regardless of the number of subscribers that actually signed up.

DIRECTV would thus strenuously oppose any requirement that it distribute programming on an a la carte basis. Moreover, because of the market distortion and increased complexity associated with a la carte distribution, DIRECTV would urge policy makers to proceed with extreme caution before adopting even the purely voluntary approach at issue in this proceeding.

I. ALL EVIDENCE SUGGESTS THAT A LA CARTE DISTRIBUTION WOULD LEAD TO HIGHER PROGRAMMING FEES AND LESS PROGRAMMING DIVERSITY

One aspect often cited in support of an a la carte regime is the ability it gives consumers to determine what programming they receive – and what programming they do not wish to receive. DIRECTV would note at the outset that, since it launched service 10 years ago, it has offered a free parental viewing “locks and limits” control feature on all television receivers, enabling parents to restrict access to channels. This feature is available on every DIRECTV system receiver and is easily accessed via the DIRECTV System remote control. With a remote control, parents simply use a four-digit access

³ DIRECTV does not understand the Commission to propose that MVPDs be required to offer a la carte programming to their customers. Were such a requirement under consideration, the implications would be far more deleterious for DIRECTV.

code to activate the lockout feature and block any number of channels from viewing. (Viewers can also use these controls to set ratings – those established by the MPAA – and spending limits.) Every DIRECTV viewer can thus avoid unwanted networks quite easily.

The other aspect most often cited in favor of an a la carte approach is that consumers could lower their bills by dropping unwanted networks.⁴ This conclusion, perhaps, rests on an assumption that per-channel pricing in an a la carte regime would be comparable to today’s implicit per-channel pricing in a tiered regime. All of the evidence DIRECTV has seen, however, suggests that this would not be the case.

As the General Accounting Office (“GAO”) explained last fall, programmers’ per-subscriber affiliate fees would likely increase significantly in an a la carte environment. This is because programmers make money from advertising as well as from affiliate fees – indeed, most programmers earn the majority of their revenues from advertising.⁵ Advertising, in turn, is tied to achieving the widest possible distribution.⁶ According to programmers and other observers, any movement of networks from the most widely distributed tiers to an a la carte format would reduce the amount that

⁴ See, e.g., Frank Ahrens, “Channels a la Carte: Big Dish Customers, a Dying Breed, Choose What They Pay For,” Wash. Post, Apr. 15, 2004 at E1 (“Like most cable and satellite television subscribers, Mike Cooper gets WGN, Turner Classic Movies, MTV, TV Land, Nickelodeon, Country Music Television, and the Independent Film Channel. What makes him different from almost everyone else is that he pays for only the channels he wants. His television bill is about \$25 per month. Yours? Often twice that much. . .”).

⁵ See General Accounting Office, *Issues Related to Competition and Subscriber Rates in the Cable Television Industry*, GAO-04-8 at 34 (Oct. 2003) (“GAO Report”), available at <http://www.gao.gov/new.items/d048.pdf> (noting that “3 of the 15 cable network representatives we interviewed indicated that they receive approximately 60 percent of their revenue from advertising”). Affiliate fees are also known as subscriber fees and licensing fees.

⁶ See, e.g., Letter from John S. Hendricks, Discovery Communications, Inc., to Senator John McCain at 3 (July 2, 2003) (noting that, without a distribution of at least 70 million households, a cable network’s “advertising revenues are miniscule because of the inability to reach a mass audience”).

advertisers are willing to pay, because there would be a reduction in the number of potential viewers.⁷ Moreover, programmers may well face higher marketing and administrative costs in an a la carte distribution model.⁸

Those selling programming on an a la carte basis, therefore, must somehow account for reduced advertising revenues and a smaller subscriber base. Presumably, they would do so in part by seeking much higher per-subscriber affiliate fees. This is why practically everyone who has looked at the question believes that, if required to offer a la carte distribution, programmers would seek to set affiliate fees at prohibitively high levels. Discovery Communications, for example, has stated that consumers would have to pay \$6.33 for a la carte distribution of the Discovery Channel.⁹ Bear Stearns likewise estimates that a viewer subscribing to the Disney Channel, ESPN, MTV, Fox News, and TBS would pay \$28.61 per month (or \$15.82 per month for ESPN alone) in an a la carte system.¹⁰

DIRECTV, of course, cannot know exactly what programmers would charge if required to offer MVPDs an a la carte option. But every indication is that a la carte affiliate fees would be significantly higher than tiered affiliate fees today. DIRECTV thus has every reason to believe that its subscribers would pay much more on a per-

⁷ See *GAO Report* at 35 (“To receive the maximum revenue possible from advertisers, cable networks strive to be on cable operators’ most widely distributed tiers. In other words, advertisers will pay more to place an advertisement on a network that will be viewed, or have the potential to be viewed, by the greatest number of people.”).

⁸ National Cable & Telecommunications Association, *The Pitfalls of A La Carte: Fewer Choices, Less Diversity, Higher Prices*, at 6 (May 2004) (“*NCTA White Paper*”), available at http://www.ncta.com/pdf_files/NCTA_White_Paper_-_Pitfalls_of_A_La_Carte.pdf.

⁹ See Letter from Judith McHale, Discovery Communications, Inc. to Rep. Nathan Deal (Apr. 27, 2004).

¹⁰ See *NCTA White Paper* at 9-10.

channel basis – and very likely more on an aggregate basis – for a la carte service than they do for tiered service.

Moreover, the evidence also suggests that, because viewers are likely to choose only those channels with which they are already familiar, an a la carte regime would threaten smaller, nascent channels and stymie the development of innovative new channels.¹¹ The result would be a diminution in programming diversity, as the available choices converge to the formats with the widest general appeal at the expense of niche and specialty programming and their audiences. Reducing the current depth and breadth of programming to a much more limited and homogenized slate of offerings would be a significant loss to all viewers. In addition, this diminution in available programming would be a particular loss to DIRECTV, which offers far more channels than many other MVPDs, and has always made this an important selling point for its service.

II. A LA CARTE WOULD IMPOSE SIGNIFICANT COSTS ON DIRECTV

As discussed above, DIRECTV’s subscribers would likely pay more for a la carte channels than they do for tiered channels. At the same time, offering a la carte service would cause DIRECTV to incur substantial costs even if few subscribers ultimately were to sign up. These costs would, in one form or another, have to be passed on to DIRECTV’s subscribers.

Perhaps the most significant set of costs associated with a la carte relates to customer service. Today, when somebody calls DIRECTV seeking to order or change

¹¹ See, e.g., *GAO Report* at 36 (noting that “some cable networks, especially small and independent networks, would not be able to gain enough subscribers to support the network”); *NCTA White Paper* at 6-7 (suggesting that a la carte distribution would “cause the demise” of basic tier networks); *id.* (arguing that, “[i]n particular, niche networks that have relatively small audiences, even if they could raise their prices, would not be able to attract enough subscribers in an a la carte world to generate the subscription fees and advertising revenues to cover the cost of producing their services).

service, the process is relatively simple. Customer service representatives (“CSRs”) can easily guide the caller through the available options, and the call usually takes a matter of minutes. Subscribers selecting programming on an a la carte basis, however, would have to choose among thousands of possible combinations, making the entire customer service experience far more complicated and time consuming.

In order to offer a la carte service, therefore, DIRECTV would have to revamp its customer service operations in a number of ways. *First*, it would have to retrain its CSRs. While CSRs must now handle a dozen or so programming options, they would have to familiarize themselves with at least 218 national 24-hour networks (not to mention regional networks and, possibly, thousands of broadcast stations¹²) in order to help subscribers construct individualized packages.

Second, because adding a la carte subscribers and changing a la carte service plans would require greater and more complex interaction, DIRECTV would have to increase the number of CSRs dramatically if it hoped to approach today’s response times. Given the existing volume of calls handled by DIRECTV and the average cost of every incremental minute that CSRs spend with customers, even a “back of the envelope” calculation suggests that such costs could run into millions of dollars per month. DIRECTV would also have to purchase equipment for these new representatives, and may need new call centers to house them.

Third, DIRECTV would likely have to revamp its customer service software. DIRECTV’s existing software allows customer service representatives to process orders

¹² It is not clear from the *Notice* whether subscribers could choose broadcast stations on an a la carte basis.

based on the dozen or so packages DIRECTV now makes available. It does not allow customer service representatives to create a la carte packaging.

DIRECTV would, one way or another, have to pass at least some of these costs along to its subscribers. One possibility would be to pass these along to only a la carte subscribers, which of course would make a la carte service that much more expensive. Another possibility would be to pass them along to *all* subscribers, which means that many subscribers would have to bear the burden of an a la carte regime even if they were perfectly happy with the current tiered approach.

DIRECTV would also incur more intangible costs arising from customer dissatisfaction with the unavoidably cumbersome a la carte customer service experience.

As another observer has described this phenomenon:

Most restaurant-goers have a hard time remembering the three or four “specials” described to them by a waiter. Imagine if the waiter had to describe hundreds of specials and the consumer had to remember all the options, sort through them, and then make a decision about which to choose. That would be the consumer’s experience with ordering programming in an a la carte world.¹³

DIRECTV agrees with this assessment, and speaks from some experience in this regard. When it first launched service in 1994, DIRECTV explored the possibility of offering an a la carte-like service called “Personal Choice.” It discovered, however, that subscribers found the process of choosing a la carte offerings too complex. Indeed, one DIRECTV executive involved in the research on Personal Choice observed that, while viewers supported a la carte in the abstract, they found choosing programming on an a la carte basis to be “paralyz[ing].” Parenthetically, DIRECTV’s research regarding Personal Choice showed that customers overwhelmingly would limit their choices to the most well

¹³ *NCTA White Paper* at 16-17.

known channels (ESPN and the like), giving credence to programmers' claims that newer networks would struggle or fail in an a la carte world.

Finally, before actually offering an a la carte service, DIRECTV would have to develop a potentially complicated and confusing set of rules for administering the service. For example, DIRECTV currently subsidizes set-top boxes in order to attract new subscribers, and recoups some of that revenue through the sale of programming. Presumably, it would need to calibrate equipment subsidies with the choice of programming – by, for example, offering different levels of subsidies depending on the value of programming chosen by an a la carte subscriber.¹⁴ This would greatly complicate – if not preclude – national advertising of rates and special offers for DIRECTV's services. Moreover, in an a la carte regime, consumers could at least theoretically change their programming on a minute-by-minute basis (subscribing to HBO, for example, just long enough to watch a particular episode of *The Sopranos*). DIRECTV would presumably need to set some sort of limits on how often customers could change their channel lineups. These rules would take some time and effort to develop, although the cost of doing so might not be overwhelming. They would, however, add to customer frustration with what would surely already be a complicated system.

CONCLUSION

Everything DIRECTV has seen to date suggests that programmers will charge very high prices for programming distributed on an a la carte basis, and that some networks would not survive. And DIRECTV knows that offering a la carte service will

¹⁴ Because only a limited number of programming options are available today, DIRECTV's rules governing equipment subsidies are quite simple – one must order certain programming packages for a certain amount of time in order to receive the subsidy.

entail significant costs, even if few people ultimately sign up. DIRECTV would strenuously object to any policy mandating such a result. And it urges policy makers to proceed with caution before pursuing even the voluntary a la carte approach at issue here.

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