BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554

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

COMMENTS OF TIME WARNER CABLE INC.

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Time Warner Cable Inc. respectfully submits these comments in response to the Commission's request for comment on "questions regarding the provision of a la carte and 'themed-tier' services on cable television and direct broadcast satellite systems."[1] As the Nation's second-largest cable operator, Time Warner Cable has a vital interest in the debate concerning a la carte.

Introduction and Summary

Cable operators' practice of selling video channels in tiers is no different from the bundling of goods and services that occurs throughout the economy. In the absence of market power, there is nothing nefarious about such bundling. The way in which firms bundle their products simply expresses the way in which aggregate consumer welfare can be optimized at the lowest cost. There is no plausible reason to believe that central planners can outperform the market in striking an optimal balance. That is no less true in the MVPD industry, which is now fully competitive.

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[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, 19 FCC Rcd 9291 (2004).

Thus, a forced a la carte requirement would make consumers worse off. Industry costs would increase: cable operators would have to provide every subscriber with a set-top box, would have to create a marketing infrastructure to enable each subscriber to select a unique combination of channels, and would have to pay higher license fees to video-programming services (which would see their marketing costs increase and their advertising revenue shrink). All these costs would be passed on to subscribers, who would likely end up paying more for fewer channels. And they would have fewer channels from which they could choose: a la carte would likely sound the death knell for some existing channels and would impair the creation of all new ones.

Although some have argued that an a la carte requirement would be harmless, that notion is mistaken. It is wrongheaded to say that, if current offerings are optimal, no subscribers will order a la carte. Our argument is not that current offerings optimally satisfy the preferences of each individual consumer — just that those offerings strike an optimal balance between industry costs and aggregate consumer welfare. Similarly, the Canadian experience does not prove that an a la carte requirement would be harmless: Canadian a la carte is quite limited in scope, may reflect only Canada's unique regulatory system, and, given Canada's small market, does not jeopardize video-programming services in the same way a la carte would in the United States.

Caution is particularly warranted because prior government intervention in the MVPD marketplace caused unintended consequences. For example, rate regulation in the early 1990s did little to restrain rates but in effect halted all development of new video-programming services. A la carte might similarly do little good and cause massive unforeseen harm.

Quite apart from constituting bad policy, an a la carte requirement would likely be struck down as violating the First Amendment. The way in which cable operators package channels in bundles is a critical part of their exercise of editorial discretion. Yet, a la carte's proposed justifications all appear to be rooted in the notion that government can do a better job than private speakers in exercising that editorial discretion. Thus, any a la carte requirement would, by seeking to change the content of speech available to subscribers, trigger strict scrutiny, which it plainly could not withstand.

At a minimum, an a la carte requirement would be subject to intermediate scrutiny, which it likewise could not survive. A desire to lower cable rates is an insufficient justification: in the absence of market failure, there is no "important" governmental interest in rate regulation. Besides, an a la carte requirement is not rationally related to any purported rate problem: it is unclear that an a la carte requirement would reduce rates and it might actually increase them.

If the point of an a la carte requirement is to combat indecency on cable, the requirement seeks to alter content and therefore triggers strict scrutiny. Besides, an indecency-inspired a la carte requirement would be so poorly tailored as to flunk even intermediate scrutiny: enabling subscribers to block channels that they consider indecent is a much more direct yet far less speech-intrusive way of addressing the purported problem. If instead the point is that cable subscribers should not be made to pay for channels that they consider indecent, the justification is no different from the rate-regulation rationale and fails scrutiny for the same reasons.

Argument

I. ANY A LA CARTE REQUIREMENT SHOULD BE REJECTED AS A MATTER OF POLICY.

This proceeding finds its genesis in the suggestion that, "[w]hen it comes to purchasing cable channels beyond the basic tier today, consumers have virtually no choice but to pay for a large package of expanded basic channels even if they watch only a couple of the channels."[2] In this view, the logical course of action for Congress or the Commission is to require multichannel video programming distributors ("MVPDs") to offer cable channels a la carte — *i.e.*, on a stand-alone, separately priced, basis.[3] But, as explained below, whether the requirement be that cable operators offer all channels a la carte or merely that they offer themed mini-tiers, such a prescription would harm, not help, consumers.[4]

A. In the MVPD Industry as Elsewhere, Identifying Bundles That Optimize Consumer Welfare Is Best Left to Market Forces.

MVPDs' provision of bundles of services is hardly unique. Producers of goods and services package their products in bundles throughout the economy, even in markets that are ideally competitive. In the absence of market failure, there is nothing nefarious about this: the size and shape of these bundles simply reflects the most efficient way of satisfying the demands of the most consumers.[5] For example, car manufacturers make available some

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[2] Letter from Senator John McCain, Chairman, United States Senate Committee on Commerce, Science, and Transportation, to Michael K. Powell, Chairman, Federal Communications Commission, at 1 (May 19, 2004) ("*McCain Letter*").

[3] *See id.*

[4] *See* General Accounting Office, *Issues Related to Competition and Subscriber Rates in the Cable Television Industry*, GAO-04-8, at 37 (Oct. 2003) ("*GAO Report*") ("[a]ll of the issues associated with an a la carte regime would also apply to minitiers.").

[5] *See, e.g.*, Dennis W. Carlton & Jeffrey M. Perloff, *Modern Industrial Organization* 303-04 (3d ed. 2000) ("For example, laced shoes are typically sold with laces; everyone who

automotive features "standard" (*e.g.*, a radio and air conditioning), others as "options" (*e.g.*, sunroofs, leather seats), and still others (*e.g.*, a purple paint job) not at all.

Manufacturers could provide every conceivable variation of every automotive feature as an option. That would have the advantage of giving consumers extensive choices, but aggregate costs would rise: there would be an increase in transaction costs (in that manufacturers would have to create an infrastructure for matching individual consumers to myriad feature permutations) and a loss of scale economies (in that virtually every car would be a custom order).[6] Thus, competitive firms balance two objectives: on the one hand, they seek to offer consumers as much choice as possible, while, on the other hand, they seek to keep costs under control.

Which balance between those two objectives will optimize aggregate consumer welfare is precisely the kind of complex and dynamic question that is best answered by market forces. Inevitably, reasonable persons disagree on the best place to strike the balance

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buys laced shoes needs shoe laces. As long as people's tastes for shoe laces do not differ dramatically, it is more efficient (that is, it lowers transaction costs) to sell laced shoes with standard shoe laces than to sell the shoe laces and shoe separately. In the extreme, every product can be thought of as composed of multiple products. For example, a radio consists of many individual components. The same is true of an automobile, which could be regarded as a package including an engine, tires, and a car body. Obviously, each of these products could be sold separately, but because consumers desire assembled products, they come tied together."); Robert H. Bork, *The Antitrust Paradox* 344 (1993 ed.) ("[E]very product or service could be broken down into smaller components capable of being sold separately, and every seller either refuses at some point to break the product down any further or, what comes of the same thing, charges a proportionally higher price for the smaller unit.").

[6] *See*, *e.g.*, 9 Phillip E. Areeda, *Antitrust Law* ¶ 1717a (2002) ("[A]ttaching windshield wipers to every automobile moving along an assembly line probably costs less than dealers' stocking and attaching them after the consumer explicitly orders them. The relevant costs include not only labor, the separate shipment of wipers, and multiple management of inventories, but also the time, energy, and costs of dealers and consumers in ordering wipers, billing for them, and the like.").

between choice and cost. But when firms strike a balance that does not optimize consumer welfare, the market disciplines their mistakes by reducing their earnings. It is axiomatic — and a fundamental tenet of this Nation's political economy — that, in the absence of market failure, central planners cannot outperform the market in maximizing consumer welfare.[7]

That is no less true in the MVPD industry than in any other. Plainly, there is no market failure: the MVPD industry is competitive and becoming more so every day. Cable operators compete head-to-head with DBS and other MVPDs, which have mopped up about a quarter of aggregate demand in less than a decade.[8] In addition, after many false starts, ILECs are now finally upgrading their networks to provide video, which will bring a whole new wave of competition to the MVPD industry.[9] And, increasingly, consumers obtain video

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[7] *See Bundling of Cellular Customer Premises Equipment and Cellular Service*, Report and Order, 7 FCC Rcd 4028, ¶ 21 (1992) ("[B]undling may be used by carriers as an efficient distribution mechanism. . . . [B]ecause a decision as to how to distribute one's product may have a significant impact on the type of service or the quality of the product provided, interference in these relationships should be approached with caution.") (internal quotation marks omitted); *Amendment of 47 CFR § 73.658(j)(1)(i) and (ii), the Syndication and Financial Interest Rules*, Tentative Decision and Request for Further Comment, 94 F.C.C.2d 1019, ¶ 107 (1983) ("[T]he Commission should not intervene in the market except where there is evidence of a market failure and a regulatory solution is available that is likely to improve the net welfare of the consuming public, *i.e.*, does not impose greater costs than the evil it is intended to remedy.").

[8] *See Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, Tenth Annual Report, 19 FCC Rcd 1606, ¶ 8 (2004) ("*Tenth Annual Report*").

[9] *See* Verizon Communications, *Verizon Begins Deploying Packet Switches to Provide Local Phone Service*, Press Release (June 22, 2004), *available at* http://newscenter.verizon.com/proactive/newsroom/release.vtml?id=85654&PROACTIVE_ID=cecdcacfc6cfc7cecfc5cecfcfcfc5cececacecacdcdcec7c7c5cf (last visited July 15, 2004); SBC Communications, Inc., *SBC Communications Announces Advances In Initiative To Develop IP-Based Residential Network For Integrated Video, Internet, VoIP Services*, Press Release (June 22, 2004), *available at* http://www.sbc.com/gen/press-room?pid=5097&cdvn=news&newsarticleid=21207 (last visited July 15, 2004).

from the Internet over broadband connections.[10] In short, the notion that there is market failure in the MVPD industry makes less sense today than at any time in history.

Accordingly, MVPDs are subject to the market-place imperatives described above: they must continuously provide a combination of optimally attractive products or suffer a punishing loss of earnings. Which bundles MVPDs offer may change as consumers' preferences change, as competitors' offerings change, and as MVPDs experiment with new offerings. For example, cable operators offer some video-programming services in tiers, some on a per-channel basis, some on both a per-channel and a tiered basis, some on a per-program basis ("Video on Demand," or "VOD"), and some in such a way that viewers can select individual programs on a subscription basis ("Subscription VOD," or "SVOD"). If these choices are not optimally responsive to consumers' preferences, DBS operators and others stand ready to tempt subscribers with more attractive combinations.[11]

B. An A La Carte Requirement Would Harm Consumers.

Given that market forces are better at constructing welfare-maximizing bundles than are central planners, any a la carte requirement would harm consumers. Because such a

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[10] *See Tenth Annual Report* ¶ 106 ("Analysts expect that over the next several years, video streaming subscription services will increase significantly, reaching an estimated $4.7 billion in revenues by 2007."); Tim Gnatek, *Internet TV: Don't Touch That Mouse!*, N.Y. Times, July 1, 2004, at G1 ("Increased broadband access and enhanced streaming technologies have boosted Internet video from the blocky slide shows of the past to presentations that can begin to rival conventional television.").

[11] Ironically, the only limitation on this dynamic consists of regulation. Cable operators are required to carry all broadcast stations and all PEG channels on the basic tier, and cable subscribers must subscribe to that tier before they may subscribe to any other tier. *See* 47 U.S.C. § 543(b)(7)(A); *id.* § 534(b)(7); 47 C.F.R. § 76.901(a); *id.* § 76.920.

requirement would increase industry costs, consumers would likely wind up paying more for less.

1. An A La Carte Requirement Would Increase Industry Costs.

Any a la carte requirement would cause three major cost increases. *First*, to ensure that subscribers receive only those channels that they affirmatively choose, cable operators would have to scramble every channel and would have to provide every subscriber with a set-top box for each TV set. That would add more than $4 per box per month to a subscriber's cable bill, an increase of more than 10% over the average cable bill just to support a la carte on a single TV set.[12] For the average cable household with three TV sets, it would add up to about $150 per year — reason enough by itself not to go down the a la carte road.

Second, cable operators would have to create a marketing infrastructure allowing each subscriber to select a unique combination of channels. They would have to create new billing systems to address the myriad possible permutations of subscriber options. In addition, cable operators would have to retrain customer service representatives to guide customers through their many new choices. Representatives would also have to spend much more time on each customer call, which would increase costs and hold times.[13]

Third, costs would increase not only for cable operators, but also for video-programming services, which would have to embark on a new marketing task of gigantic

[12] *See GAO Report* at 32 ("average monthly rental price for a box is approximately $4.39").

[13] *See id.* at 33 ("a cable operator offering 150 channels of a la carte programming could have its subscribers choosing all different numbers of networks, which would mean that subscribers would be spending much longer periods of times on the telephone with customer service staff").

proportions: they would have to persuade each individual subscriber to "check the [X Channel] box on your cable ordering form."[14] Meanwhile, video-programming services would lose revenue from advertising, which currently accounts for more than half their revenues.[15] Advertisers place a premium on programming that has national coverage, and will therefore pay less for exposure on networks that reach only a subset of the national audience.[16] Inevitably, video-programming services would seek to make up for the shortfall by raising license fees.[17]

2. As a Result, MVPD Subscribers Would Likely Pay More for Less.

All these additional costs — investment in set-top boxes, investment in an a la carte infrastructure, higher license fees for video-programming services — would eventually be passed on to MVPD subscribers. Subscribers might receive only the channels on which they place the highest value. But they would likely pay more for those few than they now pay for

[14] *See* Banc of America Securities, *Broadband Brief, Could Cable "Rate Regulation" Benefit Cable Operators?*, at 2 (Mar. 19, 2003) ("*BofA Report*").

[15] *See GAO Report* at 34-35.

[16] *See id.* at 35 ("[A]dvertisers 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."); *id.* ("[A]ny movement of networks from the most widely distributed tiers to an a la carte format could result in a reduced amount advertisers are willing to pay for advertising time because there would be a reduction in the number of viewers available to watch the networks.").

[17] *See id.* ("To compensate for any decline in advertising revenue, network representatives contend that cable networks would likely increase the license fees they charge to cable operators."); *id.* at 30 ("A move to an a la carte approach could result in reduced advertising revenues and might result in higher per-channel rates and less diversity in program choice."); *BofA Report* at 2 ("Cable programmers would likely need to raise prices substantially to offset the lower revenues and higher costs.").

many.[18] And they would no longer have the option of occasionally watching the channels they lost, even if most consumers "place value [o]n having the opportunity to occasionally watch networks they typically do not watch."[19]

Not only might subscribers pay a higher price for a smaller package of programming, they might have fewer channels from which to choose. By increasing video-programming services' marketing costs while diminishing their advertising revenue, a la carte might threaten marginal video-programming services' viability.[20] Niche networks might be harmed worse than mainstream channels: because "below certain sub counts advertisers don't even consider it worth their while,"[21] niche channels would find it difficult to earn any advertising revenue at all.

New programming networks would likewise be hard-hit. Under an a la carte system, new networks would have to persuade subscribers to pay separately for an untested and unknown service. Because subscribers would be much less likely to order fledgling services, it would be virtually impossible for new channels quickly to achieve critical mass. Put differently, barriers to entry would increase significantly.[22]

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[18] *See GAO Report* at 34 ("[I]t is possible that cable rates could actually increase for some consumers."); *id.* at 36 ("[S]ubscribers' monthly cable bills would not necessarily decline under an a la carte system."); *BofA Report* at 2 (subscribers "might just end up paying the same or more to get less stuff").

[19] *GAO Report* at 37.

[20] *See id.* at 36.

[21] *BofA Report* at 2.

[22] It is no answer to say that "it's not that easy right now to break into cable." Ted Hearn, *He'd Be One Tough FCC Top Cop*, Multichannel News, July 5, 2004, at 26 (quoting Commissioner Copps); *see id.* ("I think Ted Turner could appear in town tomorrow morning and say he was starting a new cable network, and he'd have a heck of a difficult time doing it."). Barriers to entry are relatively low: since 1998, nearly 100 new video-programming

None of this is to say that a trend towards more subscriber choice will always harm consumers. Particularly in the case of expensive programming with a limited audience, the "it's cheaper just to give everything to everyone" logic may break down. That is why premium channels are provided on an a la carte basis: the additional license fees that MVPDs pay for such premium programming outweigh the costs accompanying a la carte treatment. A la carte may also be efficient in the case of certain sports channels.[23] But whether and when a la carte works is best addressed in the market place, not by regulatory fiat.

C. Arguments That An A La Carte Requirement Would Be Harmless Are Mistaken.

It has nonetheless been suggested that an a la carte requirement would be harmless — on two grounds. *First*, it has been argued that, if current offerings are optimally responsive to consumer demand, consumers will not order a la carte, and costs will not increase.[24] But our argument is not that current offerings are optimally responsive to the demand of each individual consumer; rather, our argument is that current offerings strike an optimal balance between aggregate consumer preferences and industry costs. If cable operators are required to provide video-programming services a la carte, average rates will increase, and *aggregate* consumer welfare will decrease.

Second, some have pointed to a la carte offerings in Canada, apparently on the theory that, by voluntarily providing a la carte, cable operators there have demonstrated that a la

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services have come into being. *See Tenth Report* ¶ 142, Table 8. Besides, even if entry were difficult, that would be no reason to make it even more difficult.

[23] *See GAO Report* at 38 ("officials of 5 of the 11 cable operators we interviewed indicated that the tier concept might be viable in the case of sports programming").

[24] *See McCain Letter* at 2.

carte is efficient. But the availability of a la carte in Canada is very limited. A la carte options in Canada are available only to subscribers to digital cable; analog channels remain bundled. Moreover, very few subscribers appear to take advantage of it.[25] That is not surprising, because Canadian cable operators price tiers in such a way as to make a la carte offerings unattractive.[26] Thus, Canadian a la carte may represent nothing more than a practically insignificant experiment in a smaller market — much too thin a foundation to support broad-ranging and permanent intervention in a much larger market.

Moreover, the availability of a la carte in Canada may merely reflect Canada's unique regulatory regime, which includes extensive content controls that, in the United States, would be unthinkable. To protect Canadian-produced content, the Canadian Radio-television and Telecommunications Commission ("CRTC") regulates which video-programming services cable operators may offer on the analog CPST: cable operators may offer on analog cable only video-programming services that appear on a CRTC-approved list.[27] As a result, some popular channels (including MTV) that in the United States are on the analog CPST are available only on the digital tier in Canada. That may explain why Canadian cable operators

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[25] *See, e.g.*, Ted Hearn, *A La Carte Lives, Up North*, Multichannel News, June 14, 2004, at 57.

[26] *See, e.g.*, Rogers Communications Inc., http://www.shoprogers.com/store/cable/digitaltvcontent/digitaltv_programming_Specialty.asp (offering single channel at $2.49, entire digital tier of more than 50 services at $37.99) (last visited July 15, 2004); Shaw Communications Inc., https://secure.shaw.ca/apps/digital_ services/channel_selection.asp (offering single channel at $1.99, entire digital tier of 30 channels at $19.95) (last visited July 15, 2004).

[27] *See* CRTC, *Revised Lists of Eligible Satellite Services*, Broadcasting Public Notice CRTC 2003-43 (Feb. 18, 2002), *available at* http://www.crtc.gc.ca/archive/ENG/Notices/2003/pb2003-43.htm (last visited July 15, 2004).

would want to offer — or at least be perceived as offering — their subscribers an opportunity to select individual must-have channels without requiring them to buy the entire digital tier.

Finally, Canadian a la carte has only a limited economic effect on video-programming services. Although many of the major video-programming services carried in Canada are American (or at least Canadian-owned versions of American networks), Canadian MVPDs account for only a *de minimis* part of their revenue.[28] Thus, even though a la carte puts revenues at risk, video-programming services might be more willing to experiment in Canada than in the United States, where they must recover their fixed costs.[29]

D. Caution Is Particularly Justified Because Prior Intervention in the MVPD Marketplace Resulted in Unintended Consequences.

Caution is particularly in order because, when government previously intervened in the MVPD marketplace, unintended consequences followed. In particular, when Congress considered the 1992 Cable Act, some members of Congress warned that rate regulation would have a negative effect on the development of new programming.[30] Sadly, this

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[28] In 2002, there were only 7.3 million residential MVPD subscribers in Canada — versus nearly 90 million in the United States. *See Canadian Cable Television Ass'n 2002-2003 Annual Report* at 4, *available at* http://www.actc.ca/english/publications/annual-reports/2003/pdf/2002-03.pdf; *Tenth Annual Report*, Table B-1. Revenues for the Canadian cable industry in 2001 were less than US$2.5 billion, compared to more than $46 billion for the United States. *See CCTA 2002-2003 Annual Report* at 11; *Tenth Annual Report* ¶ 27.

[29] Even so, several programming networks have expressed dismay. *See, e.g.*, Ted Hearn, *A La Carte Lives, Up North*, Multichannel News, June 14, 2004, at 57 (citing an official at A&E as saying that a la carte "was not part of the business proposal at the time [the network launched in Canada]. If it was, we wouldn't have done the deal.").

[30] *See, e.g.*, S. Rep. 102-92, at 97 (1991) (minority views of Committee members Packwood, Stevens, and Burns) ("We are deeply concerned that the net, albeit unintended, effect of many of S. 12's provisions — including rate reregulation and program access — would be to curtail greater investment in increased channel capacity, new technologies, and programming. In the end, consumer choice could be drastically reduced.").

prediction proved correct: for years, rate regulation — which eliminated cable operators' incentive to add new video-programming services to their line-ups[31] — stopped all such development dead in its tracks.[32] Meanwhile, rate regulation did little to lower rates.[33] A few years later, Congress abandoned most rate regulation as a failure.[34]

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[31] *See* Paul Farhi, *FCC Considers Easing of Cable Price Rules; Firms Would Have Latitude on New Channels*, Wash. Post, Oct. 7, 1994, at C1 ("Cable companies say the price rules effectively froze the development of new channels because operators could not be assured of a profit if they added a channel and were restricted in what they could charge for it."); Edmund L. Andrews, *Looser Cable Pricing Rules Weighed To Spur Investment*, N.Y. Times, Oct. 8, 1994, at 39 (cable operators complained that "the price restrictions effectively prevent them from offering new channels or investing in new technology to expand the channel capacity of their systems").

[32] *See, e.g.*, James C. Goodale, *Newt Gingrich, the 104th Congress and the First Amendment*, N.Y. Law J., Dec. 2, 1994, at 3 ("It is universally conceded, most recently by the Federal Communications Commission itself that price controls and other provisions in the act have crippled the creation of new programming by the cable industry."); Paul Farhi, *FCC Considers Easing of Cable Price Rules; Firms Would Have Latitude on New Channels*, Wash. Post, Oct. 7, 1994, at C1 ("Cable companies have generally not expanded their lineups in the past 18 months.").

[33] *See BofA Report* at 1 ("[I]ronically, cable rates increased at a much faster clip than they do today, with rate increases averaging 7%-10% annually over the period, compared to 4%-6% since the regulation sunset in early 1999.")

[34] *See Telecommunications Act of 1996*, Pub. L. No. 104-104, 110 Stat. 56, 114-15, § 301(b) (1996); *see also* H.R. Rep. No. 102-204(I), at 54 (1995) ("The 1992 Cable Act was designed to rein in 'renegade' cable operators that charged unreasonable rates. However, in implementing the Act, the Commission broadened the intent of the Act by adopting rate regulations that affected the rates of virtually all cable operators. In doing so, the Commission created a complicated regulatory structure and a large bureaucracy to manage it. . . . The complicated and intrusive regulatory structure created by the Commission has severely inhibited the industry's growth. During testimony at hearings on the legislation, the Committee heard evidence that the regulations have slowed development of new programming and dampened the industry's efforts to expand system capacity and introduce new technology. The Committee also heard testimony that the regulations have severely hampered the industry's ability to obtain capital from the financial community, which, in turn, has delayed cable operators' efforts to rebuild their systems and develop new infrastructures. . . . The Committee believes there is a need to enact reform legislation that deregulates the industry. The legislation eliminates the Commission rate regulations, and relies instead on the development of marketplace forces to ensure that consumers have diverse and high quality entertainment and information choices at affordable rates.").

II. ANY A LA CARTE REQUIREMENT WOULD VIOLATE CABLE OPERATORS' FIRST AMENDMENT RIGHTS.

Quite apart from its uncertain policy foundation, an a la carte requirement would likely be struck down as violating the First Amendment. An a la carte requirement would at a minimum face intermediate scrutiny. And, whatever may be its justification, an a la carte requirement plainly could not withstand such review.

A. Any A La Carte Requirement Would Face, at a Minimum, Intermediate First Amendment Scrutiny.

1. "[C]able operators engage in and transmit speech, and they are entitled to the protection of the speech and press provisions of the First Amendment."[35] That protection translates into demanding judicial scrutiny of regulations that burden cable speech. As the D.C. Circuit put it in reviewing rules imposing rate regulation on the cable industry, "laws of less than general application aimed at the press or elements of it are always subject to at least some degree of heightened First Amendment scrutiny."[36]

The most exacting review — so-called strict scrutiny — is due in connection with "content based" restrictions.[37] Restrictions are "content based" when "Congress's purpose in enacting them was to promote speech of a favored content,"[38] or when they "impose burdens

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[35] *Turner Broad. Sys., Inc. v. FCC*, 512 U.S. 622, 636 (1994) ("*Turner I*").

[36] *Time Warner Entm't Co. v. FCC*, 56 F.3d 151, 181 (D.C. Cir. 1995) (internal quotation marks omitted); *see also Turner I*, 512 U.S. at 640-41 ("[L]aws that single out the press, or certain elements thereof, for special treatment pose a particular danger of abuse by the State, . . . and so are always subject to at least some degree of heightened First Amendment scrutiny. . . . Because the must-carry provisions impose special obligations upon cable operators and special burdens upon cable programmers, some measure of heightened First Amendment scrutiny is demanded.") (internal quotation marks omitted).

[37] *See Turner I*, 512 U.S. at 642.

[38] *Turner I*, 512 U.S. at 646; *see id.* at 645 ("Our cases have recognized that even a regulation neutral on its face may be content-based if its manifest purpose is to regulate speech because of the message it conveys."); *id.* at 642 ("the principal inquiry in determining

and confer benefits [by] reference to the content of speech."[39] When strict scrutiny applies, the government must show that the restriction is "narrowly tailored effort to serve [a] compelling [government] interest."[40]

In all other cases in which cable-specific regulation burdens speech, courts apply intermediate scrutiny.[41] To survive intermediate scrutiny, a regulation must "furthe[r] an important or substantial governmental interest" and may not impose a burden that is "greater than is essential to the furtherance of that interest."[42] It is not enough that the Commission "simply posit the existence of the disease sought to be cured."[43] Rather, the Commission "must demonstrate that the recited harms are real, not merely conjectural, and that the regulation will in fact alleviate these harms in a direct and material way."[44] This showing must be made through "reasonable inferences based on substantial evidence."[45]

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content-neutrality . . . is whether the government has adopted a regulation of speech because of agreement or disagreement with the message it conveys") (internal quotation marks and brackets omitted).

[39] *Id.* at 643.

[40] *Sable Communications of Cal., Inc. v. FCC*, 492 U.S. 115, 131 (1989).

[41] *See Turner I*, 512 U.S. at 661-62.

[42] *Turner I*, 512 U.S. at 662 (internal quotation marks omitted); *see Turner Broad. Sys. v. FCC*, 520 U.S. 180, 189 (1997) ("*Turner II*").

[43] *Turner I*, 512 U.S. at 664 (plurality) (internal quotation marks omitted).

[44] *Id.*

[45] *Id.* at 666 (plurality) (internal quotation marks omitted); *see also Home Box Office, Inc. v. FCC*, 567 F.2d 9, 50 (D.C. Cir. 1977) (*per curiam*) (courts will require the Commission to point to "a record that convincingly shows a problem to exist"); *id.* at 37 n.60 (where "there is no evidence of any urgent need for preventive action," courts will withhold any "benefit of the doubt."); *Quincy Cable TV, Inc. v. FCC*, 768 F.2d 1434, 1457-58 (D.C. Cir. 1985) (the burden of proving any prediction "susceptible of empirical proof" is on the Commission).

2. An a la carte requirement would likely be subject to strict scrutiny. All justifications for an a la carte requirement seem to be rooted in the notion that cable operators do not provide their subscribers with optimal choice, and that government can do a better job. But, just as it is a crucial part of a newspaper's editorial discretion to decide, say, whether to sell a sports section along with an op-ed section, so cable operators exercise core "editorial discretion in creating programming packages."[46] An a la carte requirement directly interferes with that discretion, as would a requirement that newspapers sell sports and op-ed sections separately. "[G]overnment [may] not dictate the content of speech absent compelling necessity."[47] Strict scrutiny applies whenever government seeks to "exercise content control over what subscribers view on cable television."[48]

But it is not even necessary to decide whether strict scrutiny would apply: at the very least, intermediate scrutiny would apply, and a la carte would fall under that test as well. Because an a la carte requirement would "impose special obligations upon cable operators

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[46] *Turner II*, 520 U.S. at 214; *see Turner I*, 512 U.S. at 636 ("cable operators engage in and transmit speech" by "exercising editorial discretion over which stations or programs to include in [their] repertoire").

[47] *Riley v. National Fed'n of the Blind of N.C., Inc.*, 487 U.S. 781, 800 (1988).

[48] *Turner I*, 512 U.S. at 652; *see id.* at 645 (strict scrutiny due if Congress used "subtle means of exercising a content preference"); *id.* at 646 (same if "purpose in enacting [must-carry measures] was to promote speech of a favored content"); *id.* at 648 (same if "Congress' purpose in enacting must-carry was to force programming of a 'local' or 'educational' content on cable subscribers"); *id.* at 649 (same if "Congress designed the must-carry provisions . . . to promote speech of a particular content"); *id.* at 649-50 (same if "Congress mandated cable carriage of broadcast television stations as a means of ensuring that particular programs will be shown, or not shown, on cable systems"); *id.* at 655 (same if Congress had "grant[ed] access to broadcasters on the ground that the content of broadcast programming will counterbalance the messages of cable operators"); *id.* at 658-59 (same if Congress prefers one group over another "based on the content of programming each group offers").

and special burdens upon cable programmers, some measure of heightened First Amendment scrutiny is demanded."[49] For that reason, the Supreme Court applied intermediate scrutiny to must-carry requirements.[50] Likewise, lower courts applied it to subscriber limits, channel-occupancy rules, rate regulation, leased-access rules, and program-access rules.[51] An a la carte requirement would burden cable operators at least as severely and would therefore minimally be subject to the same intermediate scrutiny.

B. An A La Carte Requirement Could Not Survive Intermediate First Amendment Scrutiny.

That the Supreme Court upheld must-carry under intermediate scrutiny provides no reason to think that an a la carte requirement would similarly be upheld. In *Turner*, the government justified must-carry on the theory that it was necessary to preserve "access to free television programming for the 40 percent of Americans without cable."[52] Even on that theory, the Supreme Court sustained must-carry by the narrowest margin — after a vast

[49] *Id.* at 641.

[50] *See Turner I* (must-carry obligations); *Turner II* (same).

[51] *See Time Warner Entm't Co. v. FCC*, 56 F.3d 151, 181 (D.C. Cir. 1995) (rate regulation); *Time Warner Entm't Co. v. FCC*, 93 F.3d 957, 969 (D.C. Cir. 1996) (leased access); *id.* at 978 (program access); *Time Warner I* (statutory subscriber-limit and channel-occupancy provisions); *Time Warner Entm't Co. v. United States*, 240 F.3d 1126 (D.C. Cir. 2001) (regulations implementing statutory subscriber-limit and channel-occupancy provisions).

[52] *Turner I*, 512 U.S. at 646. In particular, the theory was that cable operators had an incentive to drop broadcasters to make room for video-programming services on which they could sell advertising; that, because they faced little or no competition, cable operators had the ability to drop broadcasters without subscriber loss; that television viewers usually discontinue reception of over-the-air stations after subscribing to cable; that dropped stations would therefore see their audience and advertising revenue shrink; and that, in the end, consumers unable or unwilling to subscribe to cable might therefore have fewer or less well-financed free, over-the-air television signals to watch. *See id.* at 632-34, 646-47.

record was created on remand, in a five-to-four decision, and without a single majority opinion.[53] And the *Turner* justification is plainly unavailable here: proponents of an a la carte requirement apparently seek to justify it not on the basis of any theory that intervention is necessary to benefit non-cable subscribers, but, rather, on the theory that intervention is necessary to benefit cable subscribers themselves. Although it is not entirely plain what purported disease they seek to cure, two justifications have been suggested in particular.

1. A La Carte Cannot Be Justified on the Basis of a Rate-Regulation Rationale.

Senator McCain's letter suggests that an a la carte requirement may be necessary to "disciplin[e] cable rates."[54] But for such a concern to constitute an "important" government interest, there must be a showing that cable operators possess substantial market power: government has no "important interest" in depressing the price of speech below competitive levels.[55] As explained above, cable operators possess no market power: they face

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[53] *See Turner II.*

[54] *McCain Letter* at 2.

[55] *See Riley v. National Fed'n of the Blind of N.C., Inc.,* 487 U.S. 781, 790 (1988) (where state sought to justify rate regulation of charitable fund-raising on basis of interest in enabling charitable organizations "to negotiate fair or reasonable contracts," Court rejected claimed interest as being "in sharp conflict with the First Amendment's command that government regulation of speech must be measured in minimums, not maximums"); *see also USTA v. FCC*, 290 F.3d 415, 429 (D.C. Cir. 2002) (imposing rate regulation is arbitrary and capricious for purposes of the Administrative Procedure Act "where [an agency has] no reason to think [it] would bring on a significant enhancement of competition"), *cert. denied*, 538 U.S. 940 (2003); *Fox Television Stations, Inc. v. FCC*, 280 F.3d 1027, 1041 (D.C. Cir. 2002) ("first amendment 'intermediate scrutiny,' . . . is more demanding than the arbitrary and capricious standard of the APA"), *modified in other part*, 293 F.3d 537 (D.C. Cir. 2002); *cf. Time Warner Entm't Co. v. FCC*, 56 F.3d 151, 184 (D.C. Cir. 1995) (upholding cable rate regulation because it served an interest in "protecting consumers from monopoly prices charged by cable operators who do not face effective competition").

competition from DBS and other MVPDs, and they are further disciplined by imminent entry by ILECs and providers of Internet-based video.

Besides, it is highly doubtful whether an a la carte requirement would do *anything* to control rates. As the GAO has explained, an a la carte requirement may actually cause rates to go up, not down.[56] Where an arm of Congress has made that prediction, it is unlikely that a court would find that an a la carte requirement "will in fact alleviate [the purported] har[m] in a direct and material way."[57] "A regulation cannot be sustained if it provides only ineffective or remote support for the government's purpose, or if there is little chance that the restriction will advance the State's goal."[58]

2. A La Carte Cannot Be Justified on the Basis of an Indecency-Related Rationale.

Senator McCain's letter also hints at an interest in combating indecency.[59] But it cannot seriously be disputed that an indecency purpose would trigger strict scrutiny: a regulation that is adopted out of a desire to alter speech content is subject to strict scrutiny.[60] And an indecency-based a la carte requirement could not possibly withstand such scrutiny: "[w]here the designed benefit of a content-based speech restriction is to shield the

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[56] *See supra*, pp. 9-10 & n.18.

[57] *Turner I*, 512 U.S. at 664 (plurality).

[58] *Lorillard Tobacco Co. v. Reilly*, 533 U.S. 525, 566 (2001) (internal quotation marks and citations omitted); *see also Greater New Orleans Broad. Ass'n v. United States*, 527 U.S. 173, 188 (1999) (same).

[59] *See McCain Letter* at 2 (a la carte "would allow parents to reject channels that they find objectionable without being required to pay for the very same programming").

[60] *See supra*, p.15.

sensibilities of [viewers], the general rule is that the right of expression prevails, even where no less restrictive alternative exists."[61]

Besides, an indecency-inspired a la carte requirement would flunk even intermediate scrutiny. If the point of the requirement is simply to allow subscribers to prevent unwanted indecent channels from coming into the home, the requirement does not address a problem that is real: set-top boxes allow cable subscribers to block any channels that they do not wish to receive, and, if a cable subscriber does not currently have a set-top box, cable operators like Time Warner Cable "will provide one, *at no cost to the consumer*, upon request."[62] Blocking unwanted channels is a far less speech-burdening (and therefore more narrowly tailored) approach than would be an a la carte requirement.[63]

Perhaps the point is not merely to prevent unwanted channels from being received, but also to ensure that subscribers do not pay for content that they find objectionable. But the premise of that rationale is that subscribers' bills would decline if cable operators provide customized channel lineups — a premise that, for the reasons stated above, is incorrect.

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[61] *United States v. Playboy Entm't Group*, 529 U.S. 803, 813 (2000). Requiring cable operators to offer minitiers free of, say, violence or indecency would likewise trigger strict scrutiny. Any such requirement would necessarily dictate the content of a cable operator's speech: it would require that cable operators devote a particular tier to speech of only a particular bent, and would presumably punish cable operators who, within that tier, utter speech deemed unsuitable by government censors. A restriction that is more clearly content-based is hard to envision.

[62] Testimony of Thomas G. Baxter, President, Time Warner Cable, *On A La Carte and Themed Tier Regulation*, Before the House Committee on Energy and Commerce, Subcommittee on Telecommunications and the Internet, July 14, 2004.

[63] *See Ashcroft v. ACLU*, No. 03-218, slip op. at 8-9 (U.S. June 29, 2004) ("impos[ing] selective restrictions on speech at the receiving end, not universal restrictions at the source" is "less restrictive" of first amendment rights); *Playboy*, 529 U.S. at 815 ("targeted blocking enables the Government to support parental authority without affecting the First Amendment interests of speakers and willing listeners").

Besides, as already shown above, in the absence of market failure, government's interest in regulating rates is not "important" for First Amendment purposes.

Conclusion

For the reasons set forth above, the Commission should urge Congress not to adopt an a la carte requirement.

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