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

Applications of	)	
ADELPHIA COMMUNICATIONS CORPORATION,	)	
COMCAST CORPORATION,	)	
and	)	MB Docket No 05-192
TIME WARNER CABLE INC.,	)	
For Authority to Assign and/or Transfer Control of Various Licenses	)	

COMMENTS OF DIRECTV, INC.

William M. Wiltshire
Michael Nilsson
Amy Richardson
HARRIS, WILTSHIRE & GRANNIS LLP
1200 Eighteenth Street, N.W.
Washington, DC 20036
202-730-1300

Counsel for DIRECTV, Inc.

Susan Eid
Vice President, Government Affairs
Stacy R. Fuller
Vice President, Regulatory Affairs
DIRECTV, INC.
444 North Capitol Street, N.W.
Suite 728
Washington, DC 20001
(202) 715-2330

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OVERVIEW AND SUMMARY

In this proceeding, Comcast and Time Warner propose a series of Transactions that, if approved, would enhance the market power of the nation's two largest cable MSOs in regions across the country. Both of these cable operators have a history of exercising such market power where they already have it. In particular, both have arranged to withhold, or raise the cost of, "must have" regional sports network ("RSN") programming in strongholds such as Philadelphia and Charlotte. The Transactions would create many more such "regional monopolies" where anticompetitive behavior would be likely.

The Transactions, then, present a far more serious threat to the public interest than did earlier proceedings raising similar issues. In the most recent such proceeding (*News/Hughes*), the Commission found that DIRECTV – an entity *without* market power in the distribution market – could adversely affect competition by arranging for temporary withholding of affiliated RSN programming. At the request of some of the nation's largest incumbent cable operators, the Commission therefore imposed conditions on the parties that prohibited exclusive arrangements between DIRECTV and affiliated RSNs and established an arbitration mechanism to safeguard against various forms of discrimination. These Transactions would give Applicants at least as much ability to raise their rivals' costs for RSN programming. But unlike the *News/Hughes* transactions, they would also create the conditions for Applicants to deny their MVPD rivals access to this crucial programming altogether – and Applicants' track record demonstrates the likelihood that they will do just that. Because the public interest concerns here are so much greater than in *News/Hughes*, the Commission – if it is to approve the Transactions at all – should impose conditions here at least as stringent as those adopted in that proceeding.

*   *   *

A fundamental tenet of the Commission's public interest review is that, absent significant offsetting efficiencies or other public interest benefits, a transaction that enhances market power disserves the public interest. Here, the potential competitive harms from the Transactions are real and immediate, while the alleged efficiencies and public interest benefits are neither transaction-specific nor supported by the record. The Commission thus should not approve the Transactions without imposing conditions to address their anticompetitive effects.

Potential Public Interest Harms. As the Applicants themselves freely admit, creating or enhancing regional concentration is the primary objective of the Transactions. This is not, however, the entirely benign process of "geographic rationalization" described in the Application. Rather, it is part of the cable industry's ongoing strategy of "clustering" – combining large groups of contiguous cable systems. The Transactions would dramatically accelerate this process, single-handedly creating more and bigger clusters than any transaction previously considered by the Commission.

Indeed, the clustering resulting from the Transactions would create "regional monopolies" in many markets. According to the antitrust enforcement agencies, where the post-transaction Herfindahl-Hirschman Index ("HHI") in a market exceeds 1800 and the transaction produces an increase in HHI of more than 100, there is a presumption that the transaction is likely to create or enhance market power or facilitate its exercise. As set forth in the examples below, the Transactions exceed these benchmarks by staggeringly high amounts in a number of regions.

RSN	Post-Transaction HHI	Change
C-SET	4,210.6	403.7
Comcast SportsNet Philadelphia	4,156.7	376.9
FSN Florida	2,529.2	580.7
Sun Sports	2,515.2	578.0
FSN Ohio	2,395.7	837.8
FSN West/West 2	2,216.9	740.5
Mid-Atlantic Sports Network	2,168.7	358.6
Comcast/Charter Sports Southeast	2,148.6	325.8
Comcast SportsNet MidAtlantic	2,126.4	390.8
FSN Pittsburgh	2,080.1	576.9

The concern raised by such levels of concentration is not merely theoretical. In areas where Comcast and Time Warner already enjoy large market shares – such as Philadelphia and Charlotte – they have demonstrated their willingness and ability to obtain exclusive RSN distribution arrangements and/or to raise the cost of RSN programming for their MVPD rivals.

The Commission has consistently recognized the importance of access to "must have" RSN programming and the competitive harm that results when such programming is temporarily or permanently withheld. Armed with more and larger regional monopolies resulting from the Transactions, the Applicants will be able to use this "must have" programming as a weapon against DIRECTV and other MVPDs in many more areas than they do already.

Claimed Public Interest Benefits. On the other side of the equation, the Applicants have asserted a number of benefits that they claim will arise from the Transactions. Most of these would allegedly result from placing Comcast or Time Warner in charge of systems said to be underperforming in the hands of Adelphia. Of course, any such benefit would be inapplicable to the many non-Adelphia systems simply swapped or divided up between Comcast and Time Warner – which account for more than 25% of all subscribers affected by the Transactions.

In any event, this purported benefit is not transaction-specific because *any* non-bankrupt operator (including Cablevision and many of the other competing bidders in the bankruptcy process) would claim that it will improve Adelphia's service, but could do so without raising concerns about regional monopolies. In addition, Comcast's and Time Warner's customer satisfaction ratings as measured by J.D. Power are lower than the industry generally – hardly a ringing endorsement from current subscribers.

The Application also asserts the economic efficiencies inherent in cable system clustering. These conclusory assertions are not the kind of evidence necessary to demonstrate that such efficiencies are transaction-specific and verifiable. Indeed, publicly available information suggests the opposite – that clustering leads to higher prices, less competitive entry, and worse service.

The Application also touts the public interest in aiding the financial interests of creditors in the Adelphia bankruptcy proceeding. But, as the multiple bidders in bankruptcy suggest, these interests could be served without raising the public interest harms discussed above. More importantly, the Commission has a statutory obligation to exercise its own judgment in determining whether approving the Transactions would serve the public interest.

Finally, the Application claims that the Transactions will achieve the public interest goal of unwinding Comcast's passive interest in Time Warner and Time Warner Entertainment Company, L.P. Comcast was already obligated to achieve this "benefit" as a condition of its purchase of AT&T, however, and it is self-evident that such a divestiture could be achieved by other, competitively neutral transactions.

Remedies. The Commission cannot rely upon existing rules to address the harms clearly foreseeable from the Transactions. For example, although the program access rules prohibit discriminatory or exclusive programming arrangements with cable-affiliated programmers, Comcast has for years circumvented that provision in order to withhold the Philadelphia RSN from competitors. More problematic still are more subtle forms of discrimination such as uniform overcharge pricing and other inventive fee structures that technically may fall outside the scope of the program access rules.

As stated above, the Commission in *News/Hughes* imposed conditions on the parties that prohibited exclusive arrangements with affiliated RSNs and established an arbitration mechanism as a safeguard against various forms of discrimination, even though – unlike the Applicants here – DIRECTV, with a nationwide market share of less than 13%, had no power in the distribution market. If conditions were appropriate in *News/Hughes* to safeguard access to RSN programming in the context of a non-dominant MVPD, they are appropriate in this case *a fortiori.*

Accordingly, DIRECTV urges the Commission to conduct a thorough examination of the threat to competition posed by the Transactions' increased regional monopolization. If the Commission ultimately decides to approve the Transactions, it should impose conditions similar to those imposed in *News/Hughes* to safeguard competition and consumers in the affected MVPD markets. Specifically, and at a minimum, DIRECTV submits that approval must be contingent upon the following two conditions, applicable in such regional markets where the HHI analysis shows that the Transactions increase the likelihood of anticompetitive behavior:

- ***First, neither Comcast nor Time Warner may enter into or continue to maintain an exclusive agreement (including a "cable only" exclusive) with an RSN in any such regional market, nor may they directly or indirectly cause an RSN to refuse to deal with a rival MVPD.***

- ***Second, when negotiations fail to produce a mutually acceptable set of price, terms and conditions for carriage of an RSN in which Comcast or Time Warner holds an attributable interest, an MVPD may choose to submit the dispute to commercial arbitration (with RSN carriage required during the arbitration process).***

The first condition both closes the "terrestrial loophole" in the program access rules and prevents the exercise of market power to split monopoly rents with sports teams. The second condition protects against more insidious types of discrimination, and establishes a right of appeal to a neutral third party when an MVPD is presented with unfair "take it or leave it" terms for RSN carriage. These two conditions are necessary to safeguard MVPD rivals and their subscribers against the increase in market power created by the Transactions.

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COMMENTS OF DIRECTV, INC.

INTRODUCTION

In this proceeding, the nation's two largest cable multiple-system operators ("MSOs"), Comcast Corporation ("Comcast") and Time Warner Cable Inc. ("Time Warner"), seek authority to consummate a series of related transactions (the "Transactions") that will dramatically increase concentration levels in regions across the country. The Transactions involve in part the reallocation of cable systems and subscribers of Adelphia Communications Corporation ("Adelphia") between Comcast and Time Warner. They also include the partitioning of systems jointly held by Comcast and Time Warner through Time Warner Entertainment Company, L.P. ("TWE"), as well as the partial or total abandonment of markets by either Comcast or Time Warner in favor of the other. If approved, these Transactions will create regional monopolies of a size and scope never before approved by the Commission, enhancing the already considerable market power of the country's two largest cable incumbents.

Cable system clustering – which the Application euphemistically refers to as "geographic rationalization" – is not a new phenomenon. Time Warner mentioned its clustering strategy at least as early as its 1996 Annual Report, while Comcast mentioned clustering in the following year's Annual Report.[1] The Commission itself has recognized the significance of clustering as it has regularly tracked cable clusters serving over 100,000 subscribers in its Annual Competition Report, beginning with the report for 1997.[2]

These Transactions, however, present clustering on an unprecedented scale. Comcast would increase the number of subscribers it serves in such clusters by over 2,150,000, while Time Warner's clustered systems would serve 3,640,000 additional subscribers – a 39% increase.

DIRECTV, Inc. ("DIRECTV") operates a Direct Broadcast Satellite ("DBS") system that competes with Comcast and Time Warner in each of the markets they currently control, as well as each of the markets they propose to acquire in the Transactions. It is the nation's leading DBS operator, and thus would be a principal target for anticompetitive activities facilitated by these Transactions. DIRECTV urges the Commission to subject the Transactions to exacting scrutiny – scrutiny not possible based on the information Applicants have provided thus far. The Commission should

[1] *See* Comcast Corporation, 1997 Form 10-K Annual Report, at 5; Time Warner Inc., 1996 Form 10-K Annual Report, at I-23, F2.

[2] *See Annual Assessment of the Status of Competition in Markets for the Delivery of Video Programming*, Fourth Annual Report, 13 FCC Rcd. 1034, 1202 Table E-2 (1998).

also be prepared to impose procompetitive conditions to address the anticompetitive behavior the Transactions will facilitate.

STANDARD OF REVIEW

Section 310(d) of the Communications Act requires the Commission to determine whether the proposed transfer of a radio license would serve the public interest, convenience, and necessity.[3] In making this determination, the Commission must weigh the potential harms to competition[4] of a transaction against the unique public interest benefits that the transaction will create.[5] Applicants must prove by a preponderance of the evidence that the probable benefits of the transaction outweigh the potential harms.[6] In particular, "[t]o find that a [transaction] is in the public interest, . . . the Commission must 'be convinced that it will enhance competition.'"[7] If Applicants cannot carry this burden, the Application must be denied.[8]

The Commission must first examine potential harms from the transaction. Where, as here, a proposed transaction raises a presumption of competitive harm, it will not suffice for the Commission merely to ensure compliance with its various structural ownership and program access rules. The Commission has routinely imposed conditions

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3 47 U.S.C. § 310(d).

4 Among these harms are the enhancement of market power or slowing the decline of market power. *See NYNEX Corp. and Bell Atlantic Corp.*, 12 FCC Rcd. 19985 (1997) ("*Bell Atlantic/NYNEX*").

5 *See, e.g., EchoStar Communications Corp., General Motors Corp., and Hughes Electronics Corp.*, Hearing Designation Order, 17 FCC Rcd. 20559, 20574 (2002) ("*EchoStar HDO*"); *VoiceStream Wireless Corp., Powertel, Inc., and Deutsche Telekom AG*, 16 FCC Rcd. 9779, 9789 (2001).

6 *See EchoStar HDO*, 17 FCC Rcd. at 20574; *see also Media One Group, Inc. and AT&T Corp.*, 15 FCC Rcd. 9816, 9820 (2000)("*AT&T-Media One*").

7 *Time Warner Inc. and America Online, Inc.*, 16 FCC Rcd. 6547, 6555 (2001) (quoting *Bell Atlantic/NYNEX*, 12 FCC Rcd. at 19987).

8 *See Bell Atlantic/NYNEX*, 12 FCC Rcd. at 19987.

on proposed transactions, even where the merged entity would comply with the Commission's rules.[9] Indeed, the Commission concluded in the *News/Hughes* proceeding less than two years ago that neither the Commission's program access rules nor the applicants' commitments to adhere to them were sufficient to protect against the potential harms to consumers and competition that may result from exclusivity in regional programming.[10]

Of course, the Commission's analysis of potential harms extends beyond traditional antitrust analysis.[11] In addition to such concerns, the Commission must consider a transaction's effect on the broader public interest.[12] The Commission must also determine whether the transaction would frustrate implementation or enforcement of the Communications Act and federal communications policy.[13]

The Commission's legal standard is equally exacting with respect to asserted public interest benefits. Not surprisingly, the Applicants have presented a laundry list of the "efficiencies" that they assert will be created by the Transactions. It is the Commission's task to rigorously analyze the merits of these claims and the evidence proffered to support them. Further, when evaluating a transaction, the Commission must

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9 *See, e.g., AT&T-MediaOne*, 15 FCC Rcd. at 9845 (rejecting the applicants' argument that their compliance with "Commission rules, such as program access, program carriage, must carry, leased access, and the channel occupancy rules [would] foreclose their ability to exert excessive programming market power").

10 *See General Motors Corp., Hughes Electronics Corp. and The News Corporation Ltd.*, 19 FCC Rcd. 473, 543 (2004)("*News/Hughes*").

11 *See EchoStar HDO*, 17 FCC Rcd. at 20575 (citing *Satellite Business Systems*, 62 F.C.C.2d 997, 1088 (1977), *aff'd sub nom United States v. FCC*, 652 F.2d 72 (D.C. Cir. 1980) (*en banc*), and *Northern Utilities Service Co. v. FERC*, 993 F.2d 937, 947-48 (1st Cir. 1993)).

12 *See EchoStar HDO*, 17 FCC Rcd. at 20575.

13 *See News/Hughes*, 19 FCC Rcd. at 483-484.

consider only those purported benefits that are both transaction-specific and verifiable.[14] Efficiencies that could be achieved by more competitively neutral means or that will occur regardless of the Transactions cannot be considered procompetitive benefits in this proceeding.[15] Likewise, benefits that are merely speculative or that are predicted to occur in the distant future will be discounted or dismissed from consideration.[16] Again, the weight of verifiable benefits will be considered only net of the costs of achieving them.[17]

DISCUSSION

The Transactions will create – indeed, are designed to create – new and bigger clusters of cable systems. The resulting levels of concentration in many key regional markets far surpasses those that the *Merger Guidelines* presume to create or enhance market power or facilitate its exercise. Such a presumption is especially warranted here, as Comcast and Time Warner have already demonstrated their willingness to engage in anticompetitive practices in regions where they currently enjoy dominant market share.

Applicants have failed to even acknowledge these issues, much less address them. Accordingly, if the Commission is to approve the Transactions, it should impose behavioral constraints on Applicants to address their increased incentive and ability to act anticompetitively.

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14 *See EchoStar HDO*, 17 FCC Rcd. at 20630 (citing *Bell Atlantic/NYNEX*, 12 FCC Rcd. at 20063, and *United States Department of Justice/Federal Trade Commission Horizontal Merger Guidelines* at § 4 ("*Merger Guidelines*")); *see also Ameritech Corp. and SBC Communications Inc.*, 14 FCC Rcd. 14714, 14825 (1999) ("*SBC/Ameritech*").

15 *EchoStar HDO*, 17 FCC Rcd. at 20630.

16 *See id*. at 20630-31; *see also Bell Atlantic/NYNEX*, 12 FCC Rcd. at 20063-64.

17 *See id*. at 20630 (citing *Merger Guidelines* at § 4 ("cognizable efficiencies are assessed net of costs produced by the merger or incurred in achieving those efficiencies")).

I. THE PROPOSED TRANSACTIONS WOULD CREATE REGIONAL MONOPOLIES THAT, LEFT UNCHECKED, WOULD THREATEN COMPETITION IN THE MVPD MARKET

A. Competition Analysis Framework

In considering the competitive impact of numerous merger and consolidation proposals, the Commission has established and applied a consistent analytical framework. Under that framework, and consistent with the *Merger Guidelines* developed by the Department of Justice and Federal Trade Commission, the Commission first performs a structural analysis of the transaction to determine whether it would likely create conditions conducive to anticompetitive behavior.[18] For this analysis, the Commission must identify the relevant product and geographic markets.[19] Next, the Commission must identify market participants, examine market concentration and how concentration will change as a result of the transaction, and consider whether entry conditions are sufficiently easy that new competitors would likely constrain any attempted post-transaction price increase or other anticompetitive behavior.[20] Applying this analytical framework to the Transactions reveals substantial cause for concern.

1. Relevant Product Market

A relevant product market is one that includes all products reasonably interchangeable by consumers for the same purposes.[21] Cable operators compete in two separate but related product markets: (1) the downstream market for the distribution of

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18 *See Merger Guidelines* at § 4.13.

19 A "market" is defined as a product or group of products and a geographic area in which the product or products are produced or sold such that a hypothetical profit-maximizing firm likely would impose at least a "small but significant and nontransitory" increase in price, assuming the terms of sale of all other products are held constant. *See Merger Guidelines* at § 1.0.

20 *See, e.g., EchoStar HDO*, 17 FCC Rcd. at 20605.

21 *See United States v. E.I. du Pont de Nemours & Co.*, 351 U.S. 377, 395 (1956).

multichannel video programming to households (the "distribution market"); and (2) the upstream market for the purchase of video programming (the "programming market").[22] These Comments will focus primarily on direct effects in the programming market, which will have indirect effects in the distribution market as well.

2. Relevant Geographic Market

The Supreme Court has defined a relevant geographic market as the area of effective competition to which purchasers can practicably turn for products and services.[23] Other courts have held that the relevant geographic market selected for analysis must reflect "the commercial realities of the industry."[24]

The relevant geographic market for purposes of analyzing the programming market depends on the programming in question. Some programming networks (such as HBO, for example) offer programming of broad interest and seek a nationwide audience. Others (including RSNs and broadcast stations) are regional or local in scope. Recognizing these differences, the Commission has concluded that "the market(s) that include video programming networks are classic differentiated product markets."[25] Thus, while it is reasonable to use the entire United States as the geographic market for national cable network programming, the geographic markets for regional and local programming are much smaller.

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22 *See, e.g., Implementation of the Cable Television Consumer Protection and Competition Act of 1992 – Sunset of Exclusive Contract Prohibition*, 17 FCC Rcd. 12124, 12139-12140 (2002) ("*Exclusivity Sunset Order*").

23 *See Tampa Electric Co. v. Nashville Coal Co.*, 365 U.S. 320, 327 (1961).

24 *E.g., Arthur S. Langenderfer, Inc. v. S.E. Johnson Co.*, 917 F.2d 1413, 1421 (6th Cir. 1990) (quoting *Brown Shoe Co. v. United States*, 370 U.S. 294, 336-37 (1962)); *RSR Corp. v. FTC*, 602 F.2d 1317, 1323 (9th Cir. 1979).

25 *News-Hughes*, 19 FCC Rcd. at 504.

For RSN programming, the relevant geographic market is regional. Because contracts between each sports team and an RSN limit the distribution of the content to a specific "distribution footprint" outside of which subscribers cannot view the team's games, the Commission in two recent cases found it reasonable to define the relevant geographic market for each RSN as the RSN service area.[26] For purposes of these Comments, DIRECTV will adopt this same market definition.

3. <u>Market Participants</u>

All MVPDs located in the relevant geographic market participate in the programming market. This includes every incumbent cable operator, DBS operator, terrestrial wireless system, and competing wireline provider, if any.[27] Because cable and DBS account for the vast majority of MVPD subscribers, the Commission has focused on those MVPDs alone for purposes of determining market share and other aspects of its competition analysis.[28] DIRECTV will follow the same approach here.

B. The Transactions Result in Concentration Levels that Presumptively Create or Enhance Market Power and Facilitate Its Exercise in Many Regional Programming Markets

With respect to the *national* programming market, Applicants assert that neither Comcast nor Time Warner will achieve sufficient levels of concentration to cause concern. In support of this assertion, they point out that neither MSO will acquire

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[26] *See, e.g., News/Hughes,* 19 FCC Rcd. at 506*; Comcast Corp. and AT&T Corp.*, 17 FCC Rcd. 23246, 23267 (2002) ("*AT&T-Comcast*"). In both cases, the Commission examined the market share across the entire service area covered by the RSN, rather than the "distribution footprint" established by one or more of the teams carried.

[27] *See, e.g., Annual Assessment of the Status of Competition in Markets for the Delivery of Video Programming*, Eleventh Annual Report, 20 FCC Rcd. 2755, 2830 (2005) ("*Eleventh Competition Report*"); *EchoStar HDO,* 17 FCC Rcd. at 20613 (adopting market definition that included "MMDS, SMATV, open video systems, direct-to-home analog and digital satellite offerings, and cable overbuilders").

[28] *See, e.g., News/Hughes*, 19 FCC Rcd. at 500-07.

enough subscribers to exceed a 30% share of all MVPD subscribers nationwide, which was the cap established by the Commission (and subsequently vacated) for national cable horizontal ownership.[29] Whether or not Applicants' assertion is accurate, it is irrelevant to the markets for *regional* programming – markets that Applicants entirely fail to address. As discussed below, the Transactions will create or enhance market power in many such markets around the country.

The increased regional market concentration resulting from the Transactions is indisputable. A widely used and accepted measure of market concentration is the Herfindahl-Hirschman Index ("HHI").[30] Under the *Merger Guidelines*, in highly concentrated markets (post-transaction HHI exceeds 1800) where a transaction produces an increase in HHI of more than 100 points, a presumption arises that the transaction is likely to create or enhance market power or facilitate its exercise.[31]

Exhibit A hereto sets forth the HHI analysis for 29 major RSN markets.[32] As shown there, 10 RSN markets far surpass the thresholds for an adverse presumption, with post-transaction HHIs of at least 2000 and a change of at least 325:

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29 *See* Applications for Consent to the Assignment and/or Transfer of Control of Licenses, Application and Public Interest Statement, MB Docket No. 05-192, at 72 (filed May 18, 2005) ("Application").

30 The HHI is the sum of the squares of the market shares of each firm participating in the market. The HHI can range from nearly zero in an atomistic market to 10,000 in the case of a pure monopoly. Since the HHI is based on squared market shares, it gives proportionally greater weight to entities with large market shares. *See Merger Guidelines* at § 1.5.

31 *Id.* at § 1.51.

32 *See* Statement of Gustavo Bamberger and Lynette Neumann, at Table 3. Since Fox Sports West and Fox Sports West 2 have the same footprint, they have been counted as a single market for these purposes. The Commission's most recent *Competition Report* lists three other RSNs for which DIRECTV does not have sufficient information for analysis. These are Bravesvision, Cowboys TV, and Falconvision, each of which is wholly owned by Comcast. *See Eleventh Competition Report*, 20 FCC Rcd. at 2895-97 Table C-4. Comcast and Time Warner have also announced the formation of a new RSN, Mets Network, that will launch in 2006, but DIRECTV does not yet have information on the RSN's footprint.

RSN	Post-Transaction HHI	Change
C-SET	4,210.6	403.7
Comcast SportsNet Philly	4,156.7	376.9
FSN Florida	2,529.2	580.7
Sun Sports	2,515.2	578.0
FSN Ohio	2,395.7	837.8
FSN West/West 2	2,216.9	740.5
Mid-Atlantic Sports Network	2,168.7	358.6
Comcast/Charter Sports Southeast	2,148.6	325.8
Comcast SportsNet MidAtlantic	2,126.4	390.8
FSN Pittsburgh	2,080.1	576.9

Overall, the adverse presumption will arise in 16 of 29 RSN markets.[33]

The *Merger Guidelines* also specify that significant competitive concerns arise (1) in highly concentrated markets where a transaction increases HHI by more than 50 points, and (2) in moderately concentrated markets (post-transaction HHI between 1000 and 1800) where the transaction increases HHI by more than 100 points.[34] Four additional RSN markets satisfy these criteria.[35]

Thus, in 20 out of 29 RSN markets, the HHI analysis raises serious anticompetitive concerns. In those markets, it is likely that Comcast and Time Warner would be able to exercise market power by denying rivals access to crucial RSN programming[36] and/or raising their costs to acquire such programming, ultimately raising

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33 The other RSNs in this group are Channel 4 San Diego, FSN New England, FSN New York, Madison Square Garden, New England Sports Network, and Yankees Entertainment Sports Net. Table 4 of Exhibit A also includes the HHI analysis for all 210 DMAs, many of which will also experience very large increases in concentration.

34 *Merger Guidelines* at § 1.51.

35 The four additional RSNs are Altitude Sports and Entertainment, FSN Arizona, FSN Cincinnati, and FSN Southwest.

36 Although some RSNs are currently controlled by DIRECTV's affiliate, News Corporation, the Transactions create a significant possibility that this will not be the case in the future. Comcast and Time Warner would be in a position to lure sports teams away from News Corporation's RSNs by enticing them with a share of their monopoly rents. This has already happened in Chicago, where FSN Chicago recently lost all four professional sports teams to CSN-Chicago. Accordingly, the

the prices paid by all MVPD subscribers in those markets. Applicants have provided no basis for the Commission to ignore these clear signs of anticompetitive impact.

C. Increased Regional Market Power Will Give Applicants the Incentive and Ability to Extend a Variety of Anticompetitive Strategies for RSN Programming to Many New Markets

Concentration in regional programming markets is no mere academic concern. To the contrary, a cable operator with sufficient power in the market for RSN programming can exercise that power by denying RSN programming to its rivals or by raising its rivals' costs for such programming. The Transactions, by creating or enhancing regional monopolies across the country, will enable Applicants to engage in a range of foreclosure strategies, all of which distort the MVPD market, impair MVPD competition, and, ultimately, harm consumers.

1. <u>The Transactions Would Create or Enhance Conditions Conducive to Anticompetitive Exclusivity Arrangements in Many New Markets</u>

The Commission has consistently recognized the importance of access to "must have" programming to a healthy and competitive MVPD market. As the Commission has found, there are "no reasonably available substitutes" for RSN programming.[37] Thus, many subscribers choose their MVPD based on the availability and price of such programming. If a cable operator can arrange to withhold RSN programming from, or

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Commission cannot rely on News Corporation's continued control over RSN programming as a check on Applicants' anticompetitive conduct.

[37] *News/Hughes*, 19 FCC Rcd. at 543 ("We base these conclusions, in part, on the limited number of teams and games of local interest that are available and **[REDACTED]**, and on our economic analysis, described below, of the effects of temporary withdrawals of such programming from MVPD subscribers. An additional feature of RSN programming that sets it apart from general entertainment programming is the time-sensitivity of the airing of important local professional sports events, such as opening days or playoffs. As we have previously observed, RSNs are comprised of assets of fixed or finite supply – exclusive rights to local professional sports teams and events – for which there are no acceptable readily available substitutes.").

increase the cost of such programming to, its rivals, it can increase its market share in the distribution market by winning (or keeping) subscribers from those rivals. At the same time, however, such withholding can harm the RSN, which loses revenues from the "foreclosed" rival MVPD. Where the gains to the cable operator of foreclosing rivals outweigh the losses to the RSN programmer, foreclosure is an economically rational strategy.

Foreclosure becomes a more economically rational (and attractive) strategy as a cable operator's market share increases. This is because, as a cable operator controls more MVPD subscribers in a given geographic area, an RSN operating in that area gains more from distribution on the cable system and *loses less* if it denies distribution to the cable operator's rivals.[38]

The HHI analysis set forth in Exhibit A demonstrates that the Transactions will dramatically increase the number of markets in which programming foreclosure is likely to occur. And, as discussed below, the Commission has recognized – and Applicants have engaged in – a number of discriminatory strategies made possible by large market share, including permanent foreclosure, temporary foreclosure, and uniform overcharge pricing.

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38 Expert economists explained this dynamic – and, conversely, why foreclosure would not be economically rational for DIRECTV with its small market share – in the *News/Hughes* proceeding. *See* Charles River Associates, "News Corporation's Partial Acquisition of DIRECTV: Economic Analysis of Vertical Foreclosure Claims," at 17-19, 39-40 (attached as Exhibit B to Opposition to Petitions to Deny and Reply Comments, MB Docket No. 03-124 (July 1, 2003)) ("CRA Analysis").

2. Applicants Have Withheld or Raised the Cost of RSN Programming in Markets They Dominate

Cable operators seeking to foreclose RSN programming from their rivals can do so in a variety of ways. A recent Commission staff paper described these options as follows:

> First, cable operators may be reducing DBS penetration by making unavailable to DBS providers affiliated regional sports networks transmitted terrestrially. Second, cable operators may be able to make unavailable to DBS providers non-vertically integrated regional sports networks, which are not covered by the FCC program access rules, by signing exclusive carriage agreements. Third, the terms of the carriage agreements for some regional sports networks, either affiliated or unaffiliated with cable operators, may make them uneconomical for DBS providers to carry. In other words, the revenue gained through carriage of regional sports networks may not exceed the cost of carrying them, even if not carrying the networks reduces subscribership in some areas.[39]

Real world evidence bears this analysis out. Indeed, Comcast and Time Warner have already demonstrated this entire range of exclusionary tactics in markets where they currently enjoy high concentration levels.

a. *Permanent Foreclosure*

The most obvious way that a regional cable monopoly can harm its rivals is to obtain exclusive rights to RSN programming on a long-term basis.[40] Applicants have engaged in such a "permanent foreclosure" strategy, both with and without vertical integration, in markets where they already enjoy high market share. The Transactions will enable such a strategy in many more markets.

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[39] Andrew Stewart Wise and Kiran Duwad, *Competition Between Cable Television and Direct Broadcast Satellite – It's More Complicated Than You Think*, at 19 (January 2005)(*available at* http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-255869A1.pdf).

[40] *See News/Hughes*, 19 FCC Rcd. at 544 (contrasting permanent and temporary foreclosure).

i. *Exclusivity With Vertical Integration*

The Commission has previously examined the economics of permanent foreclosure and vertical integration on numerous occasions. A vertically integrated firm, the Commission found, "will engage in permanent foreclosure only if the present discounted value of the increased profits it earns in the downstream market as the result of foreclosure exceeds the present discounted value of the losses it incurs from reduced sales of the input in the upstream market."[41] More specifically, with respect to RSN programming:

> If [the vertically integrated programmer] removes its RSN from a rival MVPD it loses the advertising revenues with all of those subscribers. . . . In addition to a loss in advertising revenue, there is also the loss in the affiliate fees paid by the rival MVPD for the right to carry the RSN. The gain to [the vertically integrated programmer] of a permanent withholding strategy is its share of the joint profits earned from the consumers that switch from the rival MVPD, as well as the affiliate fees and advertising revenues those consumers bring with them.[42]

In the *News/Hughes* proceeding, the applicants argued – and the Commission found – that such a strategy would not be profitable where the MVPD in question controls only a relatively small share of the relevant programming markets.[43] This, again, is because the large losses from such foreclosure to the upstream programmer would inevitably outweigh the small gains to the non-dominant downstream MVPD.

Where the MVPD in question controls a larger market share, however, the Commission has repeatedly found that this strategy likely would be profitable:

> The number of subscribers that a vertically integrated [MVPD] serves is of particular importance in calculating the benefits of withholding

[41] *Id.* at 510.

[42] *Id.* at 642.

[43] *See id.* at 520.

> programming from rival MVPDs. The larger the number of subscribers controlled by the vertically integrated cable programmer the larger the benefits of withholding that accrue to that programmer. Other things being equal, then, as the number of subscribers rises, so does the likelihood that withholding would be profitable.[44]

Indeed, Congress enacted program access requirements in the Cable Act of 1992 for these very reasons.[45]

More recently, the Commission cited the same concerns in extending the program access rules' limitations on exclusive agreements between vertically integrated programmers and cable operators.[46] The Commission specifically noted the role of regional clusters as a factor conducive to a foreclosure strategy:

> The concerns outlined above are more pronounced with respect to vertically integrated regional programming distributed within an affiliated cable operator's regional cluster. In addition to noting the growing importance of regional programming services, we have also observed that regional programming tends to be significantly more vertically integrated than are national programming services. In such cases, a programmer foregoes only those revenues associated with DBS's penetration within the cluster, not the revenues associated with DBS subscribers nationwide. In contrast to the national DBS penetration rate of 18 percent, DBS subscriber penetration in various cities where cable MSOs have clusters is much lower. . . . Thus, it appears that the cost to a vertically integrated cable programmer of withholding regional programming would be proportionately lower than the cost of withholding national programming. Moreover, the affiliated cable operator will reap a substantial share of the benefits of withholding programming, since its share of total cable subscribers within the cluster is, presumably, high.[47]

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44 *Exclusivity Sunset Order*, 17 FCC Rcd. at 12140. *See also* CRA Analysis at 17-18.

45 *See, e.g., Implementation of the Cable Television Consumer Protection and Competition Act of 1992*, 10 FCC Rcd. 3105, 3123 (1994) (noting Congressional concern "with market power abuses exercised by cable operators and their affiliated programming suppliers that would deny programming to non-cable technologies").

46 *See Exclusivity Sunset Order*, 17 FCC Rcd. at 12147-12148 and n.173.

47 *Id.* at 12148-12149.

The Transactions will create exactly the incentives that the Commission was trying to combat when it extended the ban on exclusive arrangements.

As Applicants' past behavior demonstrates all too well, the program access rules will not prevent them from acting on these incentives. Comcast owns a majority interest in Comcast SportsNet Philadelphia ("CSN-Philly") – an RSN created in 1996 with exclusive rights to the Philadelphia Phillies, Flyers, and 76ers (the latter two of which were and are controlled by Comcast). Because Comcast already controlled the overwhelming majority of Philadelphia MVPD subscribers in 1996, the cost of withholding CSN-Philly from satellite operators (lost subscriber revenue and lost advertising) would be outweighed by the benefits of such withholding (luring subscribers away from satellite and lowering "churn" from Comcast to satellite). The program access rules, however, were thought to prohibit withholding of such cable-affiliated programming.

Comcast was able to withhold CSN-Philly because of a provision in the law that has since come to be known as the "terrestrial loophole." The program access rules apply to any "satellite cable programming vendor" that is affiliated with a cable operator.[48] To the extent programming is not distributed to MVPDs via satellite, however, it is not subject to the prohibitions on exclusivity. Because Comcast decided to distribute CSN-Philly over fiber optic cables, it has been able to deny that programming to DBS operators without violating the Commission's rules.[49] Comcast continues this practice to

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[48] 47 C.F.R. § 76.1002.

[49] *See Echostar Communications Corp. v. Comcast Corp.*, 14 FCC Rcd. 2089, 2100-2101 (1999); *see also EchoStar Communications Corp. v. Comcast Corp.*, 15 FCC Rcd. 22802, 22807 (2000), *rev. denied sub nom. EchoStar Communications Corp. v. FCC*, 292 F.3d 749 (D.C. Cir. 2002).

this day.[50] Not surprisingly, DIRECTV's market share in the Philadelphia DMA is significantly lower than its market share nationwide.

Other cable operators that enjoy their own Philadelphia-style regional monopolies have copied Comcast's Philadelphia strategy. Cox Communications, for example, offers its Channel 4 San Diego with exclusive rights to San Diego Padres games (including an HD feed, offered on the "4SD" channel) only to cable operators.[51] Again, DIRECTV's market share in the San Diego DMA is significantly lower than its national average. The Transactions will dramatically increase the number of markets in which such an exclusionary strategy would be economically rational – and Comcast has just put in place a nationwide fiber network that could be used to further exploit the terrestrial loophole.[52]

ii. *Exclusivity Without Vertical Integration*

While Congress and the Commission have addressed exclusivity most often in connection with vertical integration, such integration is not a prerequisite for a regional monopoly to foreclose competitors from critical regional programming. If a foreclosure strategy would be profitable for a cable operator and its affiliated programmer, it likely would also be profitable for the two entities in the absence of integration. The only difference is that the cable operator and an unaffiliated programmer must allocate the

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50 Comcast has, on one occasion, offered CSN-Philly to DIRECTV, but its carriage offer was so outrageous as to be functionally indistinguishable from outright withholding.

51 *See* http://www.cox.com/sandiego/coxmedia/exclusive.asp (listing Channel 4 as one of its "Cox Media: Exclusive Products"); http://www.4sd.com/faq.php ("Is Channel 4 San Diego available on Dish or Satellite? No. Channel 4 San Diego is a service available exclusively through your cable provider. Since we only transmit via cable, there is no way to pick up our signal via satellite.").

52 *See* Press Release, "Comcast Extends National Fiber Infrastructure" (Dec. 7, 2004)(*available at* http://www.cmcsa.com/phoenix.zhtml?c=147565&p=irol-newsArticle&t=Regular&id=650959&).

gains from such foreclosure by contract (as opposed to through an intra-company transfer).

Time Warner has shown that such exclusive carriage agreements are indeed possible. A little more than a year ago, the Carolinas Sports and Entertainment Television ("C-SET") network began operation in Charlotte. Billing itself as the "first-ever regional sports and entertainment network to exclusively serve the states of North and South Carolina," C-SET had exclusive rights to 60 games of the NBA's Charlotte Bobcats.[53]

C-SET was, as far as DIRECTV knows, unaffiliated with any MVPD. But Time Warner enjoys substantial market power in C-SET's service area, with 57.6% of MVPD subscribers (and all cable operators collectively have approximately 70% of MVPD subscribers in this service area). With this market share, Time Warner was able to secure the exclusive distribution rights to C-SET, and refuse to allow distribution to DBS competitors.[54] The Transactions would create many more places where such an exclusivity strategy would be economically rational.[55]

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53 *See* http://web.archive.org/web/20040606120046/http://www.c-set.tv/about.htm. C-SET recently announced that it would cease operations effective June 30, 2005. Prior to its demise, C-SET also had exclusive rights to "a range of programming options from throughout the Carolinas, including the . . . [WNBA] Sting, college and high school sports, motor sports, minor league baseball and hockey, outdoor sports, arena football, equestrian and extreme sports." *Id.*

54 *See* http://web.archive.org/web/20040606110520/http://www.c-set.tv/faqs.htm. ("C-SET will not be available via satellite services.").

55 Exclusive programming arrangements, of course, are not *per se* disfavored. *See Implementation of Sections 12 and 19 of the Cable Television Consumer Protection and Competition Act of 1992*, 8 FCC Rcd. 3359, 3384 (1993) (noting that, "[a]s a general matter, the public interest in exclusivity in the sale of entertainment programming is widely recognized"). Where, *in the absence of market power*, an unaffiliated programmer sells its programming to the highest bidder, which in turn uses exclusivity to differentiate itself from entrenched competitors, neither the Cable Act nor any other public policy consideration would counsel against such an arrangement. What distinguishes DIRECTV's arrangement for exclusive carriage of NFL Sunday Ticket® from the RSN exclusives discussed above, then, is one of the most basic of antitrust principles – market power facilitates anticompetitive conduct. More specifically, "[i]t is presumptively exclusionary for a monopolist to extract a supplier's promise

b. *"Soft Exclusivity" for Affiliated RSN Programming*

Exclusive arrangements represent an obvious way for a cable operator to foreclose programming from its MVPD rivals. Sophisticated cable operators seeking to avoid regulatory scrutiny are increasingly resorting to a range of other options short of outright exclusivity that can be used either to achieve *de facto* exclusivity or to significantly raise their rivals' costs.

i. *Uniform Overcharge Pricing*

In the absence of regulation, a cable operator could harm its MVPD rivals by overcharging them for affiliated RSN programming. Rivals would then be put to a Hobson's choice – either overpay for popular programming, or refuse to overpay and cede a *de facto* exclusive to the cable operator. Either way, the cable operator wins and consumers are harmed. This is why the program access rules prohibit discriminatory pricing.

But here, as with the ban on exclusivity, there is a potential loophole. Commenting on the *News/Hughes* merger, the cable industry argued vociferously that a sophisticated vertically integrated RSN could evade this prohibition and harm its affiliate's rivals through a strategy of *uniform* overcharge pricing applicable to both the

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that, notwithstanding its ability to do so, the supplier will not supply any of the monopolist's rivals," Phillip E. Areeda & Herbert Hovenkamp, Antitrust Law, Vol. IIIA, 2d Ed., ¶ 768a5 (2002). On the other hand, a company controlling only a small share of the relevant market would not have the market power necessary for such an exclusive contract to violate the antitrust laws. *See U.S. Healthcare, Inc. v. Healthsource, Inc.* 986 F.2d 589, 597-98 (1st Cir. 1993). Just as importantly, moreover, DIRECTV's carriage of out-of-market NFL games does not preclude carriage of in-market games by local broadcasters. Therefore, while Comcast and Time Warner have required sports fans in "RSN exclusive" markets to subscribe to cable in order to watch their local teams, DIRECTV has not denied any viewer in any local market the continued ability to watch the games of their local NFL team on free, over-the-air television. DIRECTV has not dictated to NFL fans that they must subscribe to DIRECTV in order to see their home team – rather, DIRECTV has offered fans the option to have access to out-of-market games not otherwise broadcast locally.

cable operator and its rivals alike.[56] As one group of cable operators put it, such a strategy would be permissible because, "[i]f [the programmer] obtains artificially *high* prices from [its affiliate], it will not be 'discriminatory' to seek the same prices from non-affiliated distributors."[57] The group explained that, in such a transaction, programmers "don't really lose money in [the] transaction . . . [because] [i]t's money that goes from one pocket into another."[58]

In the *News/Hughes* proceeding, concerns of uniform price increases were merely hypothetical. Here, though, they are not. Applicants have shown that, where they have sufficient market share in a particular region, they are willing to engage in such a strategy. Comcast, for example, recently launched a new RSN, Comcast SportsNet Chicago ("CSN-Chicago"), in cooperation with the Chicago Bulls, Blackhawks, Cubs and White Sox – teams that had previously been carried on FSN Chicago. DIRECTV sought carriage of CSN-Chicago to retain RSN coverage in this important market. Comcast did agree to make this programming available to DIRECTV, but only at a price that is roughly double what DIRECTV paid to carry the very same teams on FSN Chicago immediately prior to CSN-Chicago's launch. Unwilling to forgo this "must have" programming, DIRECTV had no choice but to accede to Comcast's demands.

56 In a further amplification of the *Merger Guidelines*, the Department of Justice noted this same problem with respect to fair dealing provisions. *See* U.S. Dept. of Justice, Antitrust Div., *Antitrust Division Policy Guide to Merger Remedies*, at 24 (Oct. 2004)("In the first instance, if the upstream and downstream firms have merged in such a manner that the sales price to the acquired downstream firm becomes a mere internal accounting factor, the upstream firm could set a high, non-discriminatory price to downstream firms that would nonetheless disadvantage the acquired downstream firm's competitors.").

57 Comments of Advance/Newhouse *et al*. in MB Docket No. 03-124 at 57 (filed June 16, 2003).

58 *Id*.

DIRECTV has no way to confirm that it pays a non-discriminatory price for the CSN-Chicago programming. Even assuming the price increase is *non*-discriminatory, however, Comcast could only sustain this higher price in a market like Chicago, where it controls the vast majority of MVPD subscribers. Only in such markets would an RSN be willing to risk losing subscribers served by its cable affiliate's rivals, because only in such a market is the RSN's potential lost distribution sufficiently small that the cable affiliate would reap more than offsetting gains from subscribers seeking access to "must have" RSN programming.[59] Once again, the Transactions will dramatically increase the number of such markets.

ii. *Threatened or Temporary Withholding*

In the *News/Hughes* transaction, the Commission found that permanent foreclosure would not be a profitable strategy for Fox RSNs, given DIRECTV's small market share (less than 13% at that time) and News Corp.'s minority interest in the company.[60] Nonetheless, the Commission found that *temporary* withholding of vertically-integrated RSN programming could be profitable even where permanent withholding is not.[61] As the Commission explained,

> In markets exhibiting consumer inertia, among other things, temporary foreclosure may be profitable even where permanent foreclosure is not, because, during the period of foreclosure, downstream customers may switch to the integrated firm's downstream product and, due to inertia, then not immediately switch back to the competitor's product once the

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59 If a cable operator has sufficient power in a market to make outright withholding economically rational, then it would be willing to forego programming revenues from rival MVPDs if they are unwilling to pay an inflated price – thereby accomplishing indirectly the exclusive arrangement that it could not accomplish directly under the program access rules.

60 *News/Hughes*, 19 FCC Rcd. at 544, 642-44.

61 *Id.* at 544 ("We also agree with commenters who argue that a temporary foreclosure strategy is likely to be profitable to News Corp. in many instances.").

> foreclosure has ended. . . . Thus, temporary foreclosure may generate profits that continue for a longer period than the period of upstream losses caused by the reduction in demand for the input.[62]

Under this reasoning, even in markets where the Transactions would not create sufficient concentration to make permanent withholding profitable, they may well create sufficient concentration to make temporary withholding profitable. This is even more likely the case here than in *News/Hughes* since Comcast and Time Warner already enjoy high levels of market concentration in many regions.[63]

The Commission also found that temporary withholding (or even just the threat of such withholding) could be used as a weapon for securing higher prices.

> Specifically, by temporarily foreclosing supply of the input to a downstream competitor or by threatening to engage in temporary foreclosure, the integrated firm may improve its bargaining position so as to be able to extract a higher input price from the downstream competitor than it could have negotiated if it were a non-integrated input supplier. In order for an integrated firm successfully to employ temporary foreclosure or the threat of temporary foreclosure as a strategy to increase its bargaining position, the foreclosure strategy must be credible. . . . [B]y temporarily foreclosing certain competitors, the vertically integrated firm may signal to other downstream competitors its willingness to foreclose, which may cause other downstream competitors to agree to a higher price without the vertically integrated firm's having to actually engage in repeated foreclosures.[64]

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62 *Id.* at 511. *See also id.* at 645 (The Commission concludes that temporary foreclosure can be profitable where permanent foreclosure is not because, in its view, temporary foreclosure gives the affiliated MVPD many of the gains of permanent foreclosure (subscriber switching from the foreclosed MVPD) without many of the corresponding losses to the programmer (which regains affiliate and advertising fees from the foreclosed MVPD's subscribers upon restoration of the service)).

63 Moreover, according to the *News/Hughes* analysis, *any* material increase in Comcast's or Time Warner's regional market shares makes temporary withholding less costly to affiliated RSNs in those markets. *See id.* at 645.

64 *Id.* at 511-12.

This, the Commission found, would lead to higher prices and increased disruption to consumers.[65]

The magnitude of this concern is far greater here than in *News/Hughes*, because Comcast and Time Warner start with far greater market share than DIRECTV had in the relevant geographic markets and the Transactions will increase that share substantially. Given that the Commission imposed conditions to address its concerns about withholding by an RSN affiliated with an MVPD that had only about 13% market share, it must surely impose similar conditions where an RSN is affiliated with an MVPD that holds a dominant (and materially increasing) share of the relevant market.

iii. *"Stealth" Discrimination*

Permanent and temporary withholding of RSN programming are serious problems. But they are not the only way that cable operators with sufficient market power can foreclose or raise the costs of their rivals. Recently, for example, cable operators (including Applicants) have begun to devise unusual pricing structures for affiliated programming. These pricing schemes often *appear* non-discriminatory, yet they have the purpose and effect of raising prices for their DBS competitors.

Comcast has recently applied this technique to an affiliated RSN. On November 2, 2004, Comcast launched its newest RSN, Comcast Sports Net West ("CSN-West"), which carries only one men's professional sports team, the NBA's Sacramento Kings.

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65 *See id.* at 547 ("[W]e find that the primary public interest harm that is likely to flow from the combination of RSN programming and nationwide MVPD distribution assets is the competitive harm of across-the-board price increases to MVPDs for carriage of . . . RSNs and/or other carriage concessions, over and above the level of price increases or other concessions that [the RSNs] could otherwise expect to obtain, through the more frequent use of credible threats of withholding or actual withholding of programming. We also find that the transaction would result in secondary public interest harms by depriving subscribers of access to RSN programming during the period of temporary foreclosure or by causing subscribers to change MVPDs to access the foreclosed programming, even where they would otherwise not desire to change providers with greater frequency than today.").

When DIRECTV expressed interest in negotiating a carriage agreement, CSN-West responded with a proposal under which DIRECTV would be required to carry this RSN in a very expansive area, including one in which *the Kings games could not be shown.* Specifically, CSN-West established a three-zone pricing structure – an inner zone (areas in and around Sacramento), an outer zone (extending up to 150 miles from Sacramento), and an "outer outer" zone (covering the San Francisco Bay area). The price per subscriber is highest in the inner zone and lower in zones further out, which is not at all unusual for RSN pricing. What is unprecedented, however, is the fact that CSN-West insisted that DIRECTV carry its programming in the outer outer zone even though the RSN did not have the rights to show Kings games to viewers in that area. Thus, DIRECTV would have to pay a monthly carriage fee for subscribers who could not see the one professional team featured by the RSN.

A bit of context further demonstrates how truly anticompetitive this pricing scheme is. DIRECTV has almost twice as many subscribers in the outer outer zone as it has in the inner and outer zones *combined*. If DIRECTV were allowed to provide CSN-West only to viewers in the inner and outer zones (*i.e.*, those who can view the Kings games), the blended rate for this programming would be comparable to the rate paid by DIRECTV for other RSN programming. Because DIRECTV must provide this RSN to so many subscribers who cannot see the Kings games, however, the effective rate for those who can watch those games is shockingly high – higher than the rate DIRECTV pays for FSN Bay Area (an RSN that carries four professional teams) and nearly the exorbitant rate DIRECTV pays for CSN-Chicago (which also carries four professional teams). This reflects the fact that the price per subscriber in the outer outer zone is no mere pittance – it is more than DIRECTV pays for such top-ten cable networks as TBS, Nickelodeon, MTV, Lifetime, and Fox News Channel.

One might think that the program access rules' non-discrimination requirement would constrain CSN-West from setting its prices in this manner. This is not necessarily the case for two reasons. First, while a DBS service by its nature covers all three RSN zones, cable franchise areas are much smaller. An individual cable system is likely to be located in the inner zone *or* the outer zone *or* the outer outer zone. A cable operator serving the outer outer zone can simply decline to carry the programming at all – and almost certainly would do so, since it could not show the core content of the channel. DIRECTV, by contrast, did not have this option, as it was required to include its subscribers in the outer outer zone in order to provide the programming to subscribers in the other two zones.

Second, to the extent there are larger cable MSOs in the region which can also be required to carry CSN-West in all three zones, the effectiveness of the non-discrimination requirement depends entirely upon their unwillingness to accede to this pricing scheme, which would overcharge them in the same way it overcharges DIRECTV. In this case, Comcast controls 97.1% of all cable subscribers in the San Francisco DMA (which comprises the outer outer zone). Since Comcast also owns 100% of CSN-West, it can accept this unprecedented pricing structure because the overcharge is, for all practical purposes, an intra-company transfer to its programming affiliate.[66] The cost to DIRECTV, by contrast, is real and substantial.

[66] In effect, this is a variation on uniform overcharge pricing. It can, however, be even more pernicious to the extent it allows other cable operators in the inner and outer zones to avoid the overcharge due to the nature/location of their operations.

D. The Available Evidence Indicates That Clustering Leads to Public Interest Harms

Even setting aside the harms described above related to foreclosure of RSN programming, the evidence suggests that clustering leads to higher retail prices, worse customer service, and deterrence of overbuilders. In the *2000 Cable Price Report*, the Commission determined that cable operators that were part of a cluster had, on average, higher monthly rates than operators that were not part of a cluster.[67] In particular, employing a regression that controlled for the number of channels offered, the Commission found that a system that was part of a cluster charged prices that on average were 2.36% higher than non-clustered systems.[68] As summarized by the Commission,

> Using 1999 Price Survey data, we estimated the modified regression equation and the results again showed a positive relationship between clustering and average monthly rates. More specifically, the sign, magnitude, and statistical significance of the coefficient for the cluster variable was similar to the coefficient reported in the *1999 Price Survey Report*. *While clustering may help reduce programming and other costs as claimed by commenters, our findings show that these lower costs are not being passed along to subscribers in the form of lower monthly rates*.[69]

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[67] *See Implementation of Section 3 of the Cable Television Consumer Protection and Competition Act of 1992*, Report on Cable Industry Prices, 16 FCC Rcd. 4346, 4361 (2001)("*2000 Cable Price Report*").

[68] *See id*. at 4376 (Appendix D-1).

[69] *Annual Assessment of the Status of Competition in the Markets for the Delivery of Video Programming*, Seventh Annual Report, 16 FCC Rcd. 6005, 6072-73 (2001) (emphasis added). Cable operators often argue that prices are higher because the number of channels offered is higher, and a better measure is the price charged on a per-channel basis. One might expect the per-channel price to be lower for any system as the number of channels increase, as the additional channels likely cost much less than the core channels that the vast majority of systems carry in common. One might also expect that, to the extent clustered systems offer more channels than non-clustered systems, clustered system operators would have much lower per-channel prices if clustering actually created operating efficiencies that were being passed on to consumers. However, this is also not the case. The Commission's analysis of cable pricing consistently demonstrates that large systems charge about the same per-channel price – or even slightly more – than do smaller systems. *See, e.g., 2000 Cable Price Report*, 16 FCC Rcd. at 4361 ("On a per channel basis, monthly rates for these two groups are similar").

AT&T, a cable operator at that time, criticized the Commission's methodology and suggested changes to the regression analysis. In response, the Commission performed a similar analysis of cable rates that incorporated the factors suggested by AT&T. Notwithstanding its previous findings, the Commission hypothesized that cable rates should be inversely related to the number of subscribers served by an MSO because larger MSOs can capture greater efficiencies.[70] Yet the Commission found once again that higher subscriber counts correlated with higher prices.[71] Other government reports have found a similar correlation between large MSOs and higher cable rates.[72] Thus, even *if* clustering leads to efficiencies (a premise unsubstantiated by the Application), there is no evidence that consumers (rather than Comcast and Time Warner shareholders and management) would be the primary beneficiaries.

Pricing is, of course, not everything. But if clustering *really* led to more advanced service offerings and other non-price benefits, one would expect customer satisfaction to be higher for clustered systems than for non-clustered systems. To the contrary, Comcast and Time Warner – among the most clustered cable MSOs in the country – have consistently underperformed in the customer satisfaction rankings compiled by J.D.

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[70] *See Implementation of Section 3 of the Cable Television Consumer Protection and Competition Act of 1992*, Report on Cable Industry Prices, 17 FCC Rcd. 6301, 6316 (2002)("*2001 Cable Price Report*") ("larger MSOs may have a relative cost advantage over single system operators or smaller MSOs, particularly in programming and financing costs, which may be reflected in lower monthly rates").

[71] *See id.* at 6318 ("Contrary to our hypothesis, the data suggest that as the number of subscribers belonging to the MSO of which the operator is a part increases, the rates charged by that MSO also increase.").

[72] *See, e.g.,* U.S. General Accounting Office Report to Congressional Requesters, "The Effect of Competition From Satellite Providers on Cable Rates," GAO/RCED-00-164 at 7 (July 2000)("GAO Report) ("Cable rates were slightly higher if the owner of a system in a particular franchise area was one of the larger national cable companies"); U.S. General Accounting Office, "Issues in Providing Cable and Satellite Television Services," GAO-03-130 at 45 (Oct. 2002) ("Additionally, cable prices were higher when the cable company was affiliated with 1 of the 10 largest MSOs. This result indicates that horizontal concentration could be associated with higher cable system prices.").

Power and Associates.[73] Similarly, Comcast and Time Warner persistently fall at – and usually below – industry averages found in the American Customer Satisfaction Index ("ACSI").[74] The ACSI Commentary for the first quarter of 2004 puts this in perspective:

> Cable television was added to ACSI in 2000. Since that time, customer satisfaction has gone from bad to worse, and there is no improvement in sight. . . . For the private as well as public sector, including the IRS, this is the lowest level of customer satisfaction of any organization in ACSI. Consumer complaints are also much more common relative to any other measured industry. Almost half of all cable customers have registered complaints about one thing or another. When buyers have meaningful choice alternatives, this level of customer (dis)satisfaction is neither competitive nor sustainable. Cable is the only industry to score below 60 in ACSI. . . . Under normal competitive conditions, there would be mass customer defections. The reason this is not the case for the cable industry is due to local monopoly power, which means that in most markets, the dissatisfied customer has nowhere to go.[75]

Not surprisingly, Applicants present no evidence that cable clustering has led to greater overall MVPD penetration – *i.e.*, the type of increased output associated with a true efficiency. In fact, in both 1997 and 1998 (the only two years for which such data was

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73 *See* Residential Cable/Satellite TV Customer Satisfaction Studies (2000-2004)(*available at* http://www.jdpa.com/studies/search.asp?CatID=3). Interestingly, Adelphia had a higher customer satisfaction score than both Comcast and Time Warner in 2002 – the year it entered bankruptcy.

74 Time Warner has met the average three times and fallen below twice, while Comcast has met the average once and fallen below four times. *See* First Quarter Scores: Utilities; Transportation & Warehousing; Information; Health Care & Social Assistance; Accommodation & Food Services (May 17, 2005)(*available at* http://www.theacsi.org/first_quarter.htm). Established in 1994, the ACSI is a uniform and independent measure of household consumption experience that tracks trends in customer satisfaction. The ACSI is produced by the Stephen M. Ross Business School at the University of Michigan, in partnership with the American Society for Quality (ASQ) and the international consulting firm, CFI Group.

75 ACSI, Q1 2004: Transportation/Communications/Utilities and Services: Industry and Company Results, Commentary by Professor Claes Fornell (June 3, 2004)(*available at* http://www.theacsi.org/scores_commentaries/commentaries/Q1_04_comm.htm).

reported), Comcast had significantly higher penetration in *non-clustered* markets than it did in clustered markets.[76]

There is also evidence that clustering deters competitive entry by overbuilders. As the Commission and other federal agencies have repeatedly found, cable prices are markedly lower in markets that are also served by another wireline MVPD system.[77] A recent study concluded that clustering creates a "fortress" that tends to deter entry by overbuilders. Specifically, the study concluded that

> *ceteris paribus*, an increase in the size of the cluster value for a given area significantly decreases the likelihood that an overbuilder enters that area. This empirical finding has an important application to the evaluation of cable mergers. If a merger increases the cluster value for consumers in a given locality, then the threat of entry by an overbuilder is reduced. To the extent that cable pricing is constrained by the threat of entry, the merger would increase cable prices.[78]

Once again, Applicants' assumption that clustering leads inevitably to public interest benefits has not been borne out.

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The Transactions, then, will create extraordinary concentration in many regional markets. Armed with increased market share, Comcast and Time Warner will be able to engage in a wide variety of exclusionary strategies, ranging from permanent foreclosure of affiliated programming to exclusive deals for unaffiliated programming to a host of

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76 *See* Comcast Corp., 1997 Form 10-K Annual Report at 5 (59.6% penetration in clustered markets vs. 70.1% in non-clustered markets); Comcast Corp., 1998 Form 10-K Annual Report at 5 (59.3% vs. 67.3%). Comcast discontinued its practice of reporting these figures after 1998.

77 *See, e.g., 2001 Cable Price Report*, 17 FCC Rcd. at 6311, Table 6 (average monthly cable rate for areas with wireline overbuilder was 9.1% lower than in non-competitive areas); GAO Report at 28-32 (Tables 3 and 4) (presence of an overbuilder reduced cable rates between 7% and 9.8%).

78 H.J. Singer, "Does Clustering by Incumbent Cable MSOs Deter Entry by Overbuilders?" at p. 4 (May 2003)(*available at* http://ssrn.com/abstract=403720).

"soft exclusivity" tactics. Moreover, clustering has been associated with higher prices, lower customer satisfaction, and deterrence of new entry. All of this will result in fewer choices (and higher prices) for consumers seeking alternatives to Comcast and Time Warner. This, DIRECTV submits, would patently disserve the public interest.

II. THERE ARE NO MITIGATING FACTORS THAT OVERCOME THE PRESUMED ANTICOMPETITIVE EFFECT OF THE PROPOSED TRANSACTIONS

Under the *Merger Guidelines*, there are three ways to rebut the presumed anticompetitive effects of a proposed transaction. First, an applicant can show that competitive entry would be timely, likely, and sufficient to deter or counteract anticompetitive effects. Second, an applicant can show that, but for the transaction, either party would be likely to fail, causing its assets to exit the market (the so-called "failing firm" argument). Third, an applicant can show that the efficiencies to be gained by the transaction outweigh the presumed anticompetitive effects.[79] In this case, Applicants have failed to make any of these showings.

A. Entry by New Competitors Will Not Be Sufficient or Timely Enough to Deter or Counteract the Transactions' Anticompetitive Effects

To begin, this is not a case where timely new entry is likely to remedy an otherwise unacceptable transaction.[80] Generally, only those committed entry alternatives that can be achieved within two years from the initial planning to significant market impact will be considered timely.[81] The Commission has repeatedly found that the MVPD industry is highly concentrated and characterized by substantial barriers to entry

79 *See generally Merger Guidelines* at §§ 0.2, 3.0, 4.0, and 5.0.

80 A transaction is not likely to create or enhance market power or to facilitate its exercise if entry into the market can be expected to be timely, likely, and sufficient in its magnitude, character and scope to deter or counteract the competitive effects of concern. *See id.* at §3.0.

81 *See id.* at § 3.2.

by new competitors.[82] Nonetheless, Applicants assert that the MVPD market is subject to new entry – in particular, by large, well-financed telephone companies (the regional Bell Operating Companies, or "RBOCs"). This, Applicants argue, is "extra protection" against any anticompetitive harms the Commission might anticipate from the Transactions.[83]

As the Commission is aware, this is not the first time that RBOCs have announced plans to enter the MVPD market.[84] Those past forays into video services failed when the RBOCs encountered unexpected obstacles. There is reason to believe that obstacles will continue to prevent the RBOCs from entering many MVPD markets in a manner sufficient and timely enough to have the "significant market impact" required under the *Merger Guidelines* to remedy the concentrating effect of the Transactions.[85]

For example, despite attempts to override the franchising requirements in several states and at the national level,[86] RBOCs still must apply for a local franchise agreement

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82 *See, e.g., Cable Horizontal and Vertical Ownership Limits*, 20 FCC Rcd. 9374, 9437 (2005); *Exclusivity Sunset Order*, 17 FCC Rcd. at 12144 ("Among these barriers is the strategic behavior by incumbent cable operators designed to raise rivals' costs, *e.g.*, limiting the availability to rivals of certain popular programming and equipment").

83 *See, e.g.*, Application at 56.

84 *Compare Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, Tenth Annual Report, 19 FCC Rcd. 1606, 1677-80 (2004)(recounting history of RBOC video announcements, including video dialtone, OVS, and cable franchises) *with Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, Eighth Annual Report, 17 FCC Rcd. 1244, 1291 (2002)("ILECs have largely exited the video business").

85 *See Merger Guidelines* at § 3.2. Indeed, Steven Burke, Chief Operating Officer of Comcast, has opined that "[t]he Bells are not likely to have video until 2006 or 2007." *See* A. Van Duyn, *The Change Sweeping Through a Cable Giant*, Financial Times, July 12, 2005, at 14.

86 *See, e.g.*, Bill McConnell, *Bad News Bells – Help from Congress won't be enough*, Broadcasting & Cable, July 11, 2005, at 12 (discussing reasons why bills to eliminate local franchising requirements are too controversial for Congress to deal with quickly).

in every town or city they target for service.[87] One RBOC has stated that, while its service area comprises more than 10,000 franchise areas, it has obtained only five or six franchise agreements after a year's worth of effort.[88] Even assuming that the franchising process speeds up as RBOCs gain familiarity with it, there is little prospect that they will be able to obtain the required agreements and launch video service in the majority of their service areas within the next two years.

In addition, RBOCs face operational obstacles in rolling out an MVPD service based on new technology. Almost inevitably, any attempt to introduce a new mass-market service using untested technology is bound to encounter snags along the way. Not surprisingly, technological issues have arisen over the past few months that have led to revised timetables for the deployment of RBOC video services.[89]

Even setting aside these licensing and technological obstacles, most markets affected by the Transactions would not have an RBOC video competitor within the next two years. First, as evidenced by the maps supplied in the Application, Comcast and Time Warner will provide service in many areas that are served by a phone company other than an RBOC.[90] For those areas, new entry is not even a glimmer on the horizon.

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87 *See* 47 U.S.C. § 541.

88 *See Are Policy-Makers Passing The Video Franchise Buck?*, 3 Telecom Policy Report 23, June 13, 2005.

89 *See, e.g.*, *Microsoft's Lightspeed in Slo-Mo*, Business Week, June 9, 2005 (recounting delays) (*available at* www.businessweek.com/print/technology/content/jun2005/tc2005069_0146_tc024.html); *MS's IPTV Strategy in Tatters*, Faultline, June 1, 2005 (SBC and Verizon planning to use Microsoft IPTV product)(*available at* http://www.paidcontent.org/pc/arch/2--5_06_01.shtml#014045); *Swisscom IPTV Stall Sends Shivers*, Light Reading, May 27, 2005 (problems with Microsoft IPTV software force postponement of service launch for at least six months)(*available at* http://www.lightreading.com/document.asp?doc_id=74648&site); Leslie Cauley, *Potential Trouble Looms for SBC's Net Based TV*, USA Today, June 8, 2005 at 5B (SBC launch delayed from late 2005 to early 2006).

90 *See* Application at Exhibits CC and FF.

Second, given the time necessary to roll out a sophisticated new video offering and the thousands of cable franchise areas within the RBOC territories, it is clear that the RBOCs will only be able to offer video service in a fraction of their footprint within the relevant time frame.[91]

Even with respect to the relatively few markets that the RBOCs actually enter over the next two years, it is unlikely that such entry would be sufficient to counteract the Transactions' anticompetitive effects. According to industry analysts, RBOCs will find it difficult to generate a reasonable rate of return on their "gigantic," "Armageddon"-like capital expenditures.[92] The prices that the RBOCs would have to charge in order to remain profitable thus would not constrain cable pricing. Indeed, "[t]he most cynical cable and Wall Street executives believe that the noise about [RBOC] video is aimed primarily at Washington, intended at projecting an image that will create new competition."[93]

Lastly, as new entrants with no market share, the RBOCs are the most likely targets for abuse by dominant incumbents such as Applicants. A cable operator with a regional monopoly would have the economic incentive to withhold affiliated RSN programming from an RBOC and would have to pay little compensation to an unaffiliated RSN to forgo the minimal affiliate and advertising revenues associated with

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91 Indeed, by virtue of the Transactions, Comcast and Time Warner may well play an increasingly important role in determining where the RBOCs choose to deploy. As discussed above, clustering creates fortress markets that deter new entrants. In these circumstances, the clustering of cable systems created and enhanced by the Transactions could become a pivotal factor in determining where RBOCs chose to enter the video business.

92 John M. Higgins, *Cable Braces for Telco Invasion into TV; Are the phone companies for real this time?*, Broadcasting and Cable, April 4, 2005, at 14 (cited in Application at nn. 60, 130).

93 *Id.*

the RBOC's relatively few subscribers. For all of these reasons, RBOC entry is unlikely to be timely and sufficient to offset the presumed anticompetitive effects of the Transactions in most of the markets they would affect.

B. Other Alternatives for Disposition of the Adelphia Bankruptcy Proceeding Present Fewer Competitive Concerns

Although it never uses the phrase, the Application impliedly makes a variant of the "failing firm" argument as a justification for the Transactions.[94] This argument, however, plainly does not apply to these Transactions. The mere fact that the Transactions would provide capital to a bankrupt firm does not mean that the firm itself is "failing," and cannot be said to justify what would otherwise be an unacceptable transaction. Under the *Merger Guidelines,* a "failing firm" argument applies only where the firm "has made unsuccessful good-faith efforts to elicit reasonable alternative offers of acquisition," which are defined as "any offer[s] to purchase the assets of the failing firm for a price above the liquidation value of those assets."[95]

Adelphia clearly does not qualify as a failing firm under this analytical framework, as it has received numerous offers above liquidation value. Any one of those offers would enable creditors to reclaim at least some of the value of Adelphia's debt, would ensure that Adelphia's assets did not exit the market, and would avoid the anticompetitive effects posed by the Transactions with Comcast and Time Warner. Indeed, Adelphia could emerge from bankruptcy itself through the reorganization process.

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[94] Applicants argue, for example, that if the Transactions are not approved, Adelphia would have to repeat the expensive and time-consuming process of remarketing its assets or devising a standalone plan of reorganization in unknown market conditions – with unknowable results. *See, e.g.,* Application at 60-62.

[95] *Merger Guidelines* at § 5.1 and n.39.

Nor can more generic bankruptcy concerns justify the Transactions. While resolving Adelphia's bankruptcy may serve the public interest, other alternatives for disposition of Adelphia's assets present fewer competitive concerns. Indeed, to the extent the Transactions provide maximum value to creditors by sharing with them the anticipated monopoly rents that will inure to Comcast and Time Warner, such benefit comes at the expense of the affected consumers in the relevant markets.

While the Commission has an obligation to consider the national policies underlying the bankruptcy laws, including the interests of creditors,[96] that obligation does not supersede the Commission's duty under Section 310(d) to ensure that the proposed transaction serves the "public interest, convenience and necessity."[97] To the contrary, the Commission *cannot* approve the sale of a bankrupt firm's assets when such a transaction conflicts with the Commission's mandate to ensure that licenses are used and transferred consistently with the Communications Act.[98]

C. The Purported Benefits of the Proposed Transactions Have Not Been Substantiated and Are Not Transaction-Specific

The anticompetitive effects of the Transactions cannot be swept aside by claims of "new entry," nor can they be excused on the basis that Adelphia is a failing firm. Applicants must therefore show that public interest harms are *outweighed* by public interest benefits associated with the Transactions. Where, as here, potential harms to the public interest appear "both substantial and likely, the Applicants' demonstration of claimed benefits also must reveal a higher degree of magnitude and likelihood than [the

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[96] *See Adelphia Communications Corp.*, 17 FCC Rcd. 24544, 24546 (2002).

[97] 47 U.S.C. § 310(d).

[98] *See LaRose v. FCC*, 494 F.2d 1145, 1148 (D.C. Cir. 1974).

Commission] would otherwise demand."[99] In order to approve the Transactions, the Commission must find that they will result in significant, offsetting, transaction-specific public interest benefits that cannot be achieved in any other way. The Applicants do not even come close to such a showing, as the benefits they claim are unproven, non-cognizable, and/or not transaction-specific.

1. Applicants Have Failed to Explain How the Swap of Systems Between Comcast and Time Warner Will Serve the Public Interest

Applicants' primary public interest benefit claim rests upon the assertion that they will provide better service than Adelphia. Applicants point in particular to the advanced services that will be made available "[b]y taking the Adelphia cable systems out of bankruptcy and placing them under the operation of either Comcast or Time Warner Cable – two of the nation's most stable, respected, and technologically advanced cable operators."[100]

The Transactions, however, also involve nearly 1,800,000 subscribers being "swapped" between Comcast and Time Warner.[101] This represents approximately 25.8% of all subscribers involved in the Transactions. Such subscribers have nothing whatsoever to do with Adelphia. Some of the swaps, moreover, involve the wholesale transfer of huge system clusters. For example, Comcast proposes to transfer to Time Warner systems serving 580,000 subscribers in Dallas, 485,000 subscribers in Los

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99 *EchoStar HDO*, 17 FCC Rcd. at 20631. *See also Merger Guidelines* at § 4 ("The greater the potential adverse competitive effect of a merger . . . the greater must be cognizable efficiencies in order for the Agency to conclude that the merger will not have an anticompetitive effect in the relevant market. When the potential adverse competitive effect of a merger is likely to be particularly large, extraordinarily great cognizable efficiencies would be necessary to prevent the merger from being anticompetitive.").

100 Application at i.

101 *See* Exhibit A, Table 1.

Angeles, and 93,000 subscribers in Cleveland. For its part, Time Warner proposes to transfer to Comcast systems serving over 247,000 subscribers in Minneapolis/St. Paul and 200,000 in Memphis.[102]

These are *not* systems that have been starved for cash while being run by "an operator that has lagged behind Time Warner Cable and Comcast" for the last two years.[103] Rather, each of these systems has been operated by one of the Applicants themselves, and each constitutes a cluster in its own right. Applicants nowhere assert that these swaps are necessary to improve service to *Adelphia* customers, or to improve lagging performance of these systems in the hands of either Comcast or Time Warner (or both). Indeed, Applicants fail to specifically address the public interest benefits of these swaps at all.

2. Applicants' Claims of Improved Services are Not Transaction-Specific

The Application devotes a great deal of time to discussing Adelphia's "lagging performance" and suggesting that Comcast and Time Warner can be expected to remedy Adelphia's shortcomings.[104] The Application compares Adelphia to Comcast and Time Warner with respect to five service aspects: (1) telephone customers;[105] (2) high-speed data ("HSD") penetration; (3) video-on-demand ("VOD") availability; (4) high definition

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[102] *See* Letter from Arthur H. Harding to Marlene H. Dortch, MB Docket 05-192 (June 21, 2005).

[103] Application at 45.

[104] *See, e.g., id.* at 45-49.

[105] The number of telephone subscribers is a particularly curious metric to choose for comparison, given that any Adelphia subscriber who has access to broadband service also has access to third-party VoIP providers such as Vonage, Skype, and Net2Phone. Applicants fail to explain why the public interest is better served when cable operators offer communications service themselves than when independent companies offer communications service over cable facilities.

television ("HD") subscribers; and (5) digital video recorder ("DVR") subscribers.[106] Given that Adelphia has been in bankruptcy for nearly three years – and that Applicants themselves chose the metrics for comparison[107] – it is not surprising to find that the comparison favors Applicants. Yet one would expect that any solvent operator would achieve better results than one mired in bankruptcy. Indeed, similar claims could be made by any number of non-bankrupt operators that would replace Adelphia – including the other parties who bid in the bankruptcy court's asset auction. Unless Applicants are claiming that they will offer better service to Adelphia subscribers *than other bankruptcy bidders*, it is hard to see how these asserted benefits are dependent on the Transactions. Certainly, they are not cognizable under Commission precedent – which recognizes only asserted benefits that could not be achieved in another way.[108]

Applicants, of course, do not claim that they will offer Adelphia customers better service than would other bankruptcy bidders. Nor could they. Neither Comcast nor Time Warner has achieved service metrics notably better than those of other operators. For example, the Commission's *2004 Cable Price Report* shows that, as of January 2004, the average HSD penetration rate was 26.1% – a figure higher than the penetration rates of both Comcast (18.3%) and Time Warner (20.8%).[109] Other large cable system operators (including Cablevision, a bidder in the Adelphia bankruptcy proceeding) meet or exceed

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[106] *See id* at 47.

[107] For example, the summary table does not include availability of HSD services, where Adelphia nearly matches Comcast and Time Warner (96.2% vs. 99%) despite its bankrupt status. *Id.* at 46. And while the Application compares the raw number of DVR subscribers, it does not calculate DVR penetration – where Adelphia would best Comcast, 2.52% to 2.2%. *See id.*

[108] *See News/Hughes*, 19 FCC Rcd. at 610; *EchoStar HDO*, 17 FCC Rcd. at 20630.

[109] *Implementation of Section 3 of the Cable Television Consumer Protection and Competition Act of 1992*, Report on Cable Industry Prices, 20 FCC Rcd. 2718, 2730 (2005)("*2004 Cable Price Report*").

Applicants' performance in their chosen metrics, as well as other performance measures.[110] For that matter, in evaluating claims of increased service quality, it is worth remembering that Comcast and Time Warner have consistently underperformed their cable peers in the customer satisfaction rankings compiled by J.D. Power and Associates. At least on the evidence available, it appears that any number of other parties would likely be able to offer Adelphia subscribers the same outlook for improvement that Applicants do – *without* creating or enhancing regional monopolies.

In a related argument, Applicants also cite their ability to provide capital to fund upgrades to Adelphia systems as a public interest benefit.[111] Here again, however, this "benefit" is not unique to Applicants because Adelphia had other options for exiting bankruptcy. As the Commission recently put it,

> [t]o the extent that access to capital is a problem, however, it could be ameliorated through other means that pose fewer competitive risks than the proposed transaction . . . . Thus, since the capital structure could be improved through other means that pose fewer competitive risks, this claimed benefit is not transaction-specific.[112]

Accordingly, access to capital is not a cognizable benefit for purposes of the Commission's analysis in this proceeding.

The Commission will recognize a claimed benefit only if it is "likely to be accomplished as a result of the [transaction] *but unlikely to be realized by other means*

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[110] *See* Cablevision Systems Corporation, 2004 Form 10-K Annual Report, at 4 (66.7% basic penetration, 30.4% HSD penetration, 272,700 VoIP customers, 100% VOD availability as of Dec. 31, 2004); Cox Communications, Inc., 2004 Form 10-K Annual Report, at 5 (59.5% basic penetration, 24.6% HSD penetration, 1,305,365 VoIP customers as of Dec. 31, 2004).

[111] *See* Application at 48.

[112] *News/Hughes*, 19 FCC Rcd. at 621.

that entail fewer anticompetitive effects."[113] Here, the claimed benefits are just as likely to be realized by other means that are not likely to harm consumers. For this reason, none of the claimed benefits related to improved service for current Adelphia subscribers are transaction-specific.

3. Applicants Have Failed to Show That Clustering Is Necessary to Achieve Asserted Public Interest Benefits

Applicants repeatedly assert that clustering – which they euphemistically refer to as "geographic rationalization" – will enhance competition and provide pro-consumer efficiencies.[114] Despite nearly a decade of clustering data upon which to draw, however, Applicants have failed to present any empirical evidence to support their contention that clustering generates public interest benefits.

Although the Application asserts at length the accomplishments of Comcast and Time Warner in rolling out new and advanced services, it presents no evidence to support the proposition that clustering contributes to (much less is a prerequisite for) the introduction of such services. Both Comcast and Time Warner operate numerous systems that are part of a cluster and others that are not part of a cluster. Yet Applicants have submitted no evidence to show that subscribers served by clustered systems predictably receive better, more advanced services more quickly than do those served by non-clustered systems. Were this the case, for example, one would expect total MVPD penetration to increase with concentration. But the evidence from Comcast's own annual reports suggests otherwise.[115] Applicants have submitted no evidence that taking a large

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[113] *Id*. at 610 (emphasis added); *EchoStar HDO*, 17 FCC Rcd. at 20630.

[114] *See*, *e.g.*, Application at 21.

[115] *See* footnote 76 above.

cluster and making it even larger will result in greater efficiencies. Nor have they submitted evidence that the benefits of these efficiencies can be expected to flow to subscribers rather than to the shareholders and management of Comcast and Time Warner.[116]

This would be a material shortcoming in any application, given that every applicant bears the burden of demonstrating that a proposed transaction will serve the public interest. In this case, however, the lack of evidence on this point is a particularly notable deficiency – both because clustering is one of the Transactions' primary purposes and because the available evidence suggests that clustering harms consumers through higher retail prices, worse customer service, and deterrence of overbuilders.

4. <u>The Partial Divestiture of Comcast's Interest in TWE and Time Warner Is Not a Cognizable Benefit of the Transactions</u>

Applicants assert that the Transactions will "achieve a long-standing Commission public interest goal" and "reduce . . . media ownership concerns" by allowing Comcast to divest its ownership interests in Time Warner and TWE.[117] These "benefits" are not cognizable for several reasons. First, they are not transaction-specific, as there are any number of other ways in which Comcast could divest these interests – and do so without anticompetitive effects.

[116] Moreover, to the extent Applicants expect to capture operating efficiencies from clustered systems, they have failed to quantify them. The Application is not even accompanied by a rudimentary declaration of a corporate officer quantifying asserted efficiencies, let alone the more substantial showing required under the Commission's rules to substantiate claimed benefits. *Compare* Declaration of Robert Pick, attached as Appendix 9 to Applications and Public Interest Statement of AT&T Corp. and Comcast Corporation, MB Docket No. 02-70 (filed Mar. 29, 2002)(summarizing and quantifying asserted synergies and efficiencies of proposed transaction) *and EchoStar HDO*, 17 FCC Rcd. at 20633-37 (discussing applicants' detailed projections of cost savings and efficiencies).

[117] *See* Application at 63-67.

Second, divestiture is not a free-standing public interest objective, but rather a pre-existing obligation imposed on Comcast in order to "avoid potential harm to competition and diversity in video programming" that would otherwise have resulted from its acquisition of AT&T.[118] Thus, unlike an undertaking to roll out service on a particular schedule or to deploy a new technology in a particular area, this obligation is purely prophylactic – guarding against harm rather than ensuring a benefit.[119]

Lastly, the Transactions would not divest Comcast of its direct voting interest in Time Warner, which will remain subject to the trust and divestiture requirements.[120] Thus, the Transactions will not, as the Application asserts, "obviate the need for the ongoing series of reporting and monitoring conditions, thereby reducing burdens that have been placed on both the Applicants and the Commission."[121] In sum, Comcast's partial divestiture of its interests in Time Warner and TWE would not result in benefits cognizable in this proceeding.

III. THE COMMISSION SHOULD NOT GRANT THE APPLICATION WITHOUT IMPOSING PROCOMPETITIVE CONDITIONS TO LEVEL THE PLAYING FIELD

In this proceeding, the nation's two largest cable incumbents propose Transactions that will enhance and extend their market power and facilitate its exercise with respect to RSN programming in many regional markets. Applicants, moreover,

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118 *AT&T-Comcast*, 17 FCC Rcd. at 23330.

119 DIRECTV also notes that the Commission has already determined (at Comcast's urging) that the existing trust mechanism through which these interests are held is sufficient for the time being to address public interest concerns with respect to media concentration (*see id.* at 23275-76) – further undercutting Applicants' claim that addressing this issue would be yet another public interest benefit of the Transactions. *See* Application at 67.

120 *See* Application at 4 n.8. In addition, a 50-50 joint venture (the Texas and Kansas City Cable Partners, L.P.) that owns cable systems serving approximately 1.5 million subscribers will remain subject to the trust agreement. *See* Application at 9-10 and n. 20.

121 *Id.* at 67.

have already (and repeatedly) engaged in anticompetitive behavior in markets where they already possess such power. In the *News/Hughes* proceeding, which presented the issue of potential RSN withholding by an MVPD with no distribution market power, the Commission concluded that behavioral conditions were necessary to safeguard competition. *A fortiori*, the same conclusion must also apply here.

Among the many conditions imposed in *News/Hughes* to safeguard access to programming for all MVPDs were the following three:

- News Corp. will not offer any of its existing or future national and regional programming services on an exclusive basis to any MVPD and will continue to make such services available to all MVPDs on a non-exclusive basis and on non-discriminatory terms and conditions.

- DIRECTV will not enter into an exclusive distribution arrangement with any Affiliated Program Rights Holder, defined to include an entity in which News Corp. or DIRECTV holds a non-controlling attributable interest and an entity that knowingly holds a non-controlling attributable interest in a programmer through News Corp. or DIRECTV.

- When negotiations fail to produce a mutually acceptable set of price, terms and conditions for carriage of an affiliated RSN, an MVPD may choose to submit the dispute to commercial arbitration in accordance with specified procedures.[122]

These conditions apply uniformly in all markets across the United States, since DIRECTV's service is national in scope.

Comcast and Time Warner do not provide service nationally. Nonetheless, as discussed above and set forth in Exhibit A, the HHI analysis demonstrates that the Transactions (1) presumptively will create or enhance market power and facilitate its exercise in numerous regional markets across the country, and (2) raise warning flags in

[122] *See News/Hughes*, 19 FCC Rcd. at 675-77.

additional regional markets.[123] In light of that evidence – as well as Applicants' own exclusionary conduct in the past – Applicants' future behavior in those markets must be constrained in order to safeguard a competitive environment for the benefit of consumers and rival MVPDs.

Specifically, DIRECTV submits that, if the Commission decides to grant the Application, it should at a minimum impose the following two conditions based on those applied in the *News/Hughes* proceeding, where competition concerns were far less compelling. These conditions would not apply nationally, but would instead apply in such regional markets where the HHI analysis shows that the Transactions increase the likelihood of anticompetitive behavior:[124]

- ***First, neither Comcast nor Time Warner may enter into or continue to maintain an exclusive agreement (including a "cable only" exclusive) with an RSN in any such regional market, nor may they directly or indirectly cause an RSN to refuse to deal with any rival MVPD.***

- ***Second, when negotiations fail to produce a mutually acceptable set of price, terms and conditions for carriage of an RSN in which Comcast or Time Warner holds an attributable interest, an MVPD may choose to submit the dispute to commercial arbitration (with RSN carriage required during the arbitration process).***

The first condition both closes the "terrestrial loophole" in the program access rules (*e.g.*, Comcast in Philadelphia) and also prevents the exercise of market power to split monopoly rents with sports teams (*e.g.*, Time Warner in Charlotte). The second condition protects against the more insidious types of discrimination and establishes a

[123] Because the transaction in *News/Hughes* did not involve a combination of horizontal assets, the Commission did not conduct an HHI analysis in that proceeding.

[124] For purposes of these conditions, the trigger would be an HHI increase of at least 100 points in a moderately concentrated market (HHI between 1000 and 1800) or an HHI increase of at least 50 points in highly concentrated markets (HHI greater than 1800).

right of appeal to a neutral third party when an MVPD is presented with unfair, "take it or leave it" terms.

These two conditions are very similar to the conditions found appropriate to address RSN-related issues in the *News/Hughes* proceeding, but have been tailored to this proceeding in light of the Transactions' enhancement of regional market power. Imposing them here will safeguard Applicants' MVPD rivals and their subscribers against the anticompetitive effects arising from the Transactions.

CONCLUSION

By design, the Transactions will create or enhance concentration in regional markets across the country. Standard antitrust analysis demonstrates that the resulting market power will presumptively lead to anticompetitive effects with respect to regional programming, and Applicants have failed to substantiate any offsetting public interest benefits. Less than two years ago, without any finding of market power in the distribution market, the Commission imposed conditions to assure continued access to "must see" RSN programming. In this proceeding – which involves parties with market power and a history of exclusionary conduct – the threat to competition is far greater. In order to approve the Transactions the Commission should, at a minimum, impose similar conditions to safeguard competition and consumers in the MVPD market against easily anticipated anticompetitive effects.

Respectfully submitted,

DIRECTV, INC.

By: __/s/_______________________
Susan Eid
Vice President, Government Affairs
Stacy R. Fuller
Vice President, Regulatory Affairs
DIRECTV, INC.
444 North Capitol Street, N.W.
Suite 728
Washington, DC 20001
(202) 715-2330

William M. Wiltshire
Michael Nilsson
Amy Richardson
HARRIS, WILTSHIRE & GRANNIS LLP
1200 Eighteenth Street, N.W.
Washington, DC 20036
202-730-1300

Counsel for DIRECTV, Inc.

July 21, 2005

DECLARATION

I, Daniel Fawcett, do hereby declare and state under penalty of perjury as follows:

1. I am Executive Vice President, Business and Legal Affairs, for DIRECTV, Inc. My business address is 2230 E. Imperial Highway, El Segundo, CA 90245. My telephone number is 310-964-0123.

2. I have read the foregoing Comments. To the best of my personal knowledge, information, and belief formed after reasonable inquiry, the statements made in these Comments other than those of which official notice can be taken, are well grounded in fact.

7/20/05
DATE

Dan Fawcett
DANIEL FAWCETT

CERTIFICATE OF SERVICE

I hereby certify that, on this 21st day of July, 2005, a copy of the foregoing Comments of DIRECTV, Inc. was sent by hand delivery to:

Philip L. Verveer
Michael H. Hammer
Francis M. Buono
Willkie Farr & Gallagher LLP
1875 K Street, N.W.
Washington, DC 20006

Aaron I. Fleischman
Arthur H. Harding
Seth A. Davidson
Craig A. Gilley
Fleischman and Walsh, L.L.P.
1919 Pennsylvania Avenue, N.W.
Washington, DC 20006

Joseph W. Waz, Jr.
James R. Coltharp
Comcast Corporation
2001 Pennsylvania Avenue, N.W.
Washington, DC 20006

and by e-mail to:

Best Copy and Printing, Inc.
Portals II
445 12th Street, S.W.
Room CY-B402
Washington, DC 20554
www.bcpiweb.com

Wayne McKee
Media Bureau
Room 4-C737
Federal Communications Commission
445 12th Street, S.W.
Washington, DC 20554
Wayne.McKee@fcc.gov

Barbara Esbin
Media Bureau
Room 3-C458
Federal Communications Commission
445 12th Street, S.W.
Washington, DC 20554
Barbara.Esbin@fcc.gov

Jim Bird
Office of the General Counsel
Room 8-C824
Federal Communications Commission
445 12th Street, S.W.
Washington, DC 20554
James.Bird@fcc.gov

Tracy Waldon
Media Bureau
Room 3-C488
Federal Communications Commission
445 12th Street, S.W.
Washington, DC 20554
Tracy.Waldon@fcc.gov

Jeff Tobias
Wireless Telecommunications Bureau
Room 3-A432
Federal Communications Commission
445 12th Street, S.W.
Washington, DC 20554
Jeff.Tobias@fcc.gov

Royce Sherlock
Media Bureau
Room 2-C360
Federal Communications Commission
445 12th Street, S.W.
Washington, DC 20554
Royce.Sherlock@fcc.gov

JoAnn Lucanik
International Bureau
Room 6-A660
Federal Communications Commission
445 12th Street, S.W.
Washington, DC 20554
JoAnn.Lucanik@fcc.gov

Marcia Glauberman
Media Bureau
Room 2-C264
Federal Communications Commission
445 12th Street, S.W.
Washington, DC 20554
Marcia.Glauberman@fcc.gov

Kimberly Jackson
Wireline Competition Bureau
Room 5-C142
Federal Communications Commission
445 12th Street, S.W.
Washington, DC 20554
Kimberly.Jackson@fcc.gov

/s/
Jennifer Anselmo