realities of the marketplace. In effect, they are saying, vertical and horizontal integration were necessary for the industry to survive in the face of rising costs and increased competition from new technologies.[38]

As this process unfolded, the impact was felt in more than just access to audiences. The leverage that the vertically integrated core of the industry acquired also dramatically changed the terms of trade between the independents and vertically integrated conglomerates. With a small number of vertically integrated buyers and a large number **of** much smaller product sellers, the core oligopoly gains monopsony power. They can impose onerous terms on the supplier, appropriating maximum surplus. With all of the major distribution channels under their control, the vertically integrated oligopoly can slash the amount they are willing to pay for independent product.

MARKET STRUCTURAL IMPACTS OF HORIZONTAL CONCENTRATION AND VERTICAL INTEGRATION

The pattern of behavior and structural changes in the industry should raise red flags for public policy. One major concern about vertical mergers is that the industry undergoes a rush to integration and consolidation. Being a small independent firm at any stage renders a company extremely vulnerable to a variety of attacks.

> Oligopolies often settle down into behavioral patterns in which price competition atrophies, even though some or all sellers suffer from excess capacity. Non-price rivalry then becomes crucial to the distribution **of** sales. One form of nonprice competition is the acquisition of downstream enterprises, which all else (such as prices) being equal will be purchased from their upstream affiliates. If acquisition of this sort deflects significant amounts of sales, disadvantaged rivals are apt to acquire other potential customers in self-defense, and reciprocal fear of foreclosure precipitates a bandwagon effect in

[38] Bielby William T. and Denise D. Bielby, "Controlling Prime Time: Organizational Concentration and Network Television Programming Strategies," ***Journal of Broadcasting & Electronic Media,*** 47: 4 (2003), p. 585.

which the remaining independent downstream enterprises are feverishly

> If there are 10 nonintegrated firms and only one of them integrates, then little affect on competition might occur. But if this action induces the other **9** to do the same, the ultimate impact of the first "triggering" move may be large. Any increase in market power is magnified.[40]

A second. related concern about vertical integration that arises from the observed behaviors is that it can create or reinforce barriers to entry into the industry. By integrating across stages of production, incumbents may force potential competitors to enter at both stages, making competition much less likely. "[V]ertical mergers may enhance barriers to entry into the primary industry if entrants must operate at both stages in order to be competitive with existing firms and if entry at both stages is substantially more difficult than entry at one stage".[41]

Capital market hurdles are only one of the barriers to entry that vertical integration and conglomeration can create. Such mergers can also foreclose input markets to competitors.

> When all production at a level of an industry is "in-house," no market at all exists from which independent firms can buy inputs. If they face impediments or delays in setting up a new supplier, competition at their level will be reduced. The clearest form of this **is** the rise in capital a new entrant needs to set up at both levels.[42]

The experience in the video product space over the *two* decades in which the vertically integrated oligopoly emerged suggests that vertical integration increased barriers to entry into the television sector.

> [B]ecause the vertically integrated structure creates such a barrier to entry.,. it is not necessary for these executives to collude.... The complexity has made it

[39] Scberer and Ross, pp. 526-527.
[40] Shepherd, p. 290.
[41] Perry, p. 241.
[42] Shepherd, pp. 289-290.

almost impossible for new players to enter the market, because they have to do so on so many levels – production, distribution, cable outlets, and so forth.[43]

Compared to recorded music, production costs in television are astronomical, creating substantial barriers to entry to new program suppliers and creating incentives to the networks to demand greater control over costs.. .. In **the** increasingly deregulated business environment, the enhanced market power of the corporations that control access to channels of distribution has made it more difficult for independent suppliers of new television series to survive in the industry, Moreover, the high cost of producing episodic television makes it extremely difficult to operate through channels of distribution outside of network television, such as first run syndication or cable (especially when those off-network venues are increasingly controlled by the same corporations).[44]

FAVORING AFFILIATES

The gatekeeper role translates into leverage because "with increased vertical integration, independent producers have less access to audiences, or they must align themselves with studios or networks to get their shows on the air."[45] Einstein concludes that integration favors internally produced product.

Given vertical integration and the combined network/programming departments, all things being equal, an internally produced show is going to get an airing over one in which the network does not have an interest. It is also more likely to get a better time slot and be kept on the air longer. While it is possible that some shows of lesser quality are given preference over those produced by outsiders, this is a situation that is not likely to be sustained.[46]

Producers claim that with the demise of the Fin-Syn Rules, networks have used their enhanced market position in several ways to gain unfair advantage over outside program suppliers. First, they claim that when selecting **series** for the prime-time schedule and deciding between a **series** from an outside producer versus one of comparable or even less quality produced in-house by the network or by a **network** joint venture, the network will favor the ***series*** in

---

[43] Einstein, p. **217.**
[44] Bielby and Bielby, p. 341
[45] Einstein, pp. 180-181.
[46] Einstein, p. 194-195.

which it has a financial interest. Moreover, many producers perceive that this kind of favoritism has intensified in recent years.[47]

Exclusive and preferential deals for the use of facilities and products compound the problem

> The first firms to integrate into neighboring stages reduce the number of alternative sources for other firms at either stage. This "thinning" of the market can increase the costs of market or contractual exchange. Subsequent integration by other firms then becomes more likely.[48]

Concerns arise that not only will the dominant firm in the industry gain the leverage to profitably engage in anti-competitive conduct, but also the dynamic processes in the industry will clearly shift toward cooperation and coordination rather than competition. **The** issue is not simply collusion, although that is clearly a concern.

> The ***Guidelines*** do recognize three major competitive problems of vertical mergers in concentrated industries. First, forward mergers into retailing may facilitate collusion at the manufacturing stage by making it easier to monitor prices or by eliminating a "disruptive buyer." [49]

Beyond collusion, a mutual forbearance and reciprocity occurs as spheres of influence are recognized and honored between and among the small number of interrelated entities in the industry.

> Now we consider the big picture, rather than market-by-market effects. Imagine an extreme situation, with five big diversified firms extending into all major sectors. They coexist in parallel, touching one another in hundreds of markets. Whatever their effects on each market might be, they pose a larger problem of spheres of interest, or diplomatic behavior replacing competition ...
>
> Reciprocity is an exchange of favors. Reciprocal buying is one form of it. At its simplest, firm A buys from firm B because of some purchase that B makes from A ...

---

[47] Bielby and Bielby, p. 581.

[48] Perry, Martin, "Vertical Integration: Determinants and Effects," in Richard Schmalensee and Robert D. Willig (Eds.) ***Handbook of Industrial Organization*** (New **York** North-Holland, 1989), p. 247.

[49] Perry, p. 247.

> Reciprocity: The large conglomerate may have numerous opportunities for reciprocal buying arrangements.
>
> Mutual forbearance: More generally (it is sometimes claimed) large firms treat each other with deference, avoiding competitive confrontation whenever possible.[50]

Einstein and others identify a number of ways in which vertical integration affects the flow of programming. Clearly inferior shows are aired primarily because the vertically integrated media conglomerate owns them, although there is a difference of opinion on how prevalent this outcome is.

> There are already many examples of network-produced programs that have failed miserably. Shows that were put on the schedule for no other reason than the network studio produced them.[51]
>
> There is definitely favoritism for internally produced shows over those produced out of house.. . There are limits to this.. .. To the extent that they won't put on a bad show that's produced internally over a good show that's not, but certainly if two shows are of **equal** value the internally produced show will get the nod.[52]
>
> Indeed, according to one producer, a network financial **stake** in a proposed series "practically guarantees" a slot in the prime-time schedule.. . "Without question, if I know that I am gonna **lose,** I just want to know that at the end **of** the day the shows that beat me out did so because they are better shows and not just because they're co-owned by the network.[53]

More generally, owned-programming gets an inside track and is chosen when there are close calls.

> [I]t appears the incentives introduced into the program selection process by the repeal of the Fin-Syn rules have clearly affected the program selection process within broadcast networks. Specifically, the networks have an incentive to

---

[50] Asch, Peter and Rosalind Senaca, ***Government and the Marketplace*** (Dryden Press, Chicago: 1985), p. **248.**
[51] Einstein, p. 194-195.
[52] Einstein, p. **217.**
[53] Bielby and Bielby, p. 581.

select programs produced in-house because of both financial and political reasons.[54]

[I]t is important to note here that internally produced programming has the so-called home court advantage when it comes to being selected for the prime-time schedule.. .. 'If you put the network person in charge of both sides of the fence.. . It's impossible to ask the network person to have that much objectivity.[55]

Owned programming is given better time slots.

What is less known is that the networks are selling time periods, giving the best time slots on the schedule to those who make the best deal with the network.[56]

Owned programming is kept on the air longer.

Shows are also being maintained on the schedule for longer than they might be if the network did not have an ownership interest in the show.[57]

Owned programming clogs syndication.

A new issue has arisen in the syndication market that is adversely affecting producers to the benefit of the networks and their parent companies. Due to increased vertical integration, more and more companies are selling programs within their own company rather than going out into the marketplace to sell a show. For instance, a network that has its own production company will sell a hit show to its cable network at a below-market rate without opening the show to bidding by other outlets, cable or broadcast. Though this is **very** lucrative for the company, **it is** detrimental to the profit participants in the show—the producers, the actors and so forth. If the vertically integrated company sells the show internally, it is at a heavily discounted price, which means that the profit participants are cheated out of their rightfully earned money. By selling internally, the companies have almost created a new form of warehousing. Rather than keeping a show off the market, they are keeping the show off the market to competitors.[58]

The pattern of acquisition of shows and movies discussed in the previous chapter also suggests that when the oligopolists are not self-supplying, they engage in reciprocal dealing,

[54] Einstein, pp. 180-181.
[55] Einstein, **p.** 187.
[56] Einstein, **p.** 217.
[57] Einstein, p. 192.
[58] Einstein, pp. 198-199.

buying shows from one another. Interviews with independent producers conducted in preparing this study indicate that, with the vertical integration of studios into the core of the oligopoly, the problem afflicts the movie segment as well. The field is simply not level.

The interviews with independent movie producers suggest that the problems that afflict independents in syndication are somewhat different for producers of series and movies. The literature on independent producers of series shows that when independents were squeezed out of the prime time series market, they simply did not have product to sell into syndication, since they were literally put out of business. To some extent, producers of movies were similarly affected, since they did not have larger budget movies to sell into syndication, though they managed to remain in the movie business. Their theatrical releases were squeezed in the syndication space as the vertically integrated entities came to dominate syndication. The squeeze was two-pronged they found it more difficult to get placement and the license fees and other terms deteriorated.

MONOPSONY POWER

The final area of concern identified in the analytic framework is the exercise of monopsony power. The gatekeeper problem is at the core of monopsony power concerns in the video content industry.[59] The harm in the exercise of monopsony power is the reduction of prices paid to suppliers and therefore a reduction of the quantity or quality of the product supplied.

[59] Curtin, John J., Daniel L. Goldberg and Daniel S. Savrin, "The EC's Rejection of the Kesko/Tuko Merger: Leading the Way to the Application of a 'Gatekeeper' Analysis of Retailer Market Power Under U.S. Antitrust Law," 40 *B.C. L. Rev.* 537 (1999).

> By reducing its demand for a product, a monopsonist can force suppliers to sell to it at a lower price than would prevail in a competitive market... If the price is suppressed they will reduce output to a level that once again equals their marginal costs. In any event, both price and output will fall below the competitive level when the buyer is a monopsonist. Some productive assets will he assigned to products that would have been the supplier's second choice in a competitive market. As a result, monopsony allocates resources inefficiently just as monopoly does.[60]

This problem is evident in tne TV video space as well. Broadcasters have the leverage to extract equity shares for shows not developed internally

> [I] in recent years, the networks seem to have refined their strategy even further – recognizing that when series with high potential do appear from outside producers, they can use their market power to extract an ownership stake after the pilot has been produced.
>
> Secondarily, if the show is not internally produced, then the ability to have equity ownership in an externally produced show is expected for inclusion on the prime-time schedule.[61]
>
> Even shows in which the networks did not originally have an interest have had their financing restructured to allow the network to become a financial partner for a show to stay on air, particularly in the ever-important fifth year. ... "'Shakedown is probably too strong a word, but they should not have the right to insist on ownership just to provide real estate on the airwaves."'
>
> Giving a piece of the show to the network has become a normal way of doing business since the repeal of the Fin-Syn rules, because access to the airwaves depends on giving the networks a financial interest in the program. Sometimes these requirements are subtle, like requesting that a producer create their show with their studio's production facilities, and sometimes they are quite blatant – your money or your show.[62]
>
> Of even greater concern to these producers than the perceived favoritism towards in-house production and joint ventures is an increasingly common practice by the networks of commissioning pilots from independent producers

[60] Hovenkamp, Herbert, ***The Law of Antitrust: An Integrated Handbook,*** Hornbook Series (West Group, St. Paul, 2000), p. 14.
[61] Einstein, pp. 180-181.
[62] Einstein, p. 192.

then demanding a financial stake as a condition of picking up a series for the prime time schedule.[63]

Networks gain market power to meddle with the content offered by independents

The argument being advanced here is that the increase in in-house production following the demise of the Fin-Syn Rules created a conflict of interest as business executives from the networks are placed in a position to meddle in the creative process. Under the Fin-Syn Rules, it is argued that independent producers and those affiliated with tha majbr studios were insulated from this kind of interference.[64]

Interviews with the independent film producers underscore **the** problem of monopsony power. The pervasive control over distribution channels on TV allows the integrated firms to dictate terms and conditions that squeeze the independents. These include license **fees** that do not cover the costs, given the quality that is demanded, extremely long license periods, and claims to back end-rights – home video, foreign sales and digital distribution -- that limit the ability of independents to make up for the inadequate license fees. The exercise of this monoposony power has gone so far as to allow the buyers to repurpose content to "higher" value" distribution channels without additional compensation for the independent producers. By taking a product that was purchased at terms and conditions designed for a lower value outlet and re-using it on a much higher value outlet, the vertically integrated company extracts much greater value (profit), without compensating the producer.

This exercise of monopsony power is akin to a practice that the vertically integrated companies had applied in the **series** space. In that space, the vertically integrated firms take a high value product and **sell** it at very low prices to a lower value outlet, in essence under stating the value of the product, to which independent participants might have a claim.

---

[63] Bielhy and Bielby, p. 581.
[64] Beilby and Bielby, p. 580.

> A new issue has arisen in the syndication market that is adversely affecting producers to the benefit of the networks and their parent companies. Due to increased vertical integration, more and more companies are selling programs within their own company rather than going out into the marketplace to **sell** a show. For instance, a network that has its own production company will sell a bit show to its cable network at a below market rate without opening the show to bidding by other outlets, cable or broadcast. Though this is very lucrative for the company, it is detrimental to the profit participants in a show – the producers, the actors and so forth.[65]

It should be evident from these examples that the existence of multiple cable outlets does not alter the already restricted television landscape because the networks have captured a substantial hold over the most important cable networks

> One way that networks are ensuring a faster return on investment is by having a secondary distribution channel usually in the form of a general entertainment cable channel. These channels are used as a secondary outlet through which they can distribute their programs.. .. Each of these networks present programming on the broadcast network that is then re-presented (or repurposed) on the secondary outlet. This will lead to **more** redundant programming and less new content through more outlets. Networks are also making their prime time programming available through video-on-demand and DVD collections.[66]

> Another increasingly popular business strategy implemented by the big four and emerging networks also offsets the impact of expanding channels of distribution. "Repurposing" involves exhibiting each episode of a **series** on an affiliated broadcast or cable network immediately after the initial network broadcast.[67]

[65] Epstein, pp. 198-199.
[66] Einstein, pp. 218-219, on the latter point Einstein cited Adalian, 2002.
[67] Beilby and Bielby, p. 592.

VI. THE DEBATE OVER QUALITY

QUALITATIVE OBSERVATIONS

The question of the relationship between vertical integration and declining quality has been hotly debated. The exercise of monopsony power is clearly affecting the structure of the industry. Two effects have been noted.

First, the number of entities engaged in the process has been reduced sharply because the distribution of risk and rewards has been shifted in favor of the networks.

> [T]he statistical patterns summarized above include instances in which the networks have used their enhanced market power to negotiate ownership shares in series pilots brought to them by outside suppliers. In these situations, the program supplier, not the network, absorbs development costs, while the network acquires a share of the back end profits if the series eventually becomes a hit and goes into syndication. From the program suppliers' perspective, the costs of development for new series remain the same, but to reach the prime-time schedule, the supplier has to agree to forgo a share of the future revenues. According to some in the industry, this revenue squeeze on independent program suppliers is the primary reason that a number of them have exited the business of prime-time series development.[68]

> So far, the most visible impact of deregulation has been a reduction in the number of organizational settings in which those who create television series are employed, and an increase in corporate control over the circumstances under which they practice their craft.[69]

The second effect is to eliminate the creative tension that once existed between the producer and the distributor of product.

> Vertical integration is seen as eliminating a valuable step in the development process. First, developing programming is a creative process. When one entity created the programming and another would select it, the two companies could argue and disagree and out of those discussions, the show would often be improved... [T]he process did favor internal shows and eliminated much of the

[68] Beilby and Bielby, p. 590.
[69] Beilby and Bielby, p. 593.

development process altogether. Producers also stated that this process was detrimental to the overall quality of network programming.[70]

One aspect of the debate over quality that is intriguing but little studied is the potential relationship between integration, declining quality and declining ratings. **As** Bielby and Bielby note:

> In 1999, *Advertising Age* editorialized that ABC was "auctioning" its most desirable prime-time time slot to the program supplier willing to give the network a financial stake, part of a trend that is making it "increasingly clear the broadcast networks are more interested in financial deals than putting the best shows they can find on the air." **The** trade publication warned that **the** ratings decline experienced by the networks would accelerate if "financial packages rather than program quality determine what **gets** on the schedule."[71]

The ratings decline certainly did continue, **as** integrated ownership of program dng increased. **As** is frequently the case in this sector, many other things were changing that could account for the decline in ratings, but the correlation is notable.

Waterman sees some evidence of the latter effect on the studio side of the business.

> [E]xcessive movie budgets and an over reliance on sequels or derivative movies have also been associated unfavorably with conglomerate organization and the mentality of the top executive in charge.[72]

Waterman also notes that the claimed efficiency benefits of conglomeration have come into question

> When merger plans are announced, industry analysts often cite efficiencies, such as workforce combinations, or marketing advantages, such as the ability to cross-promote movies using television, magazines or other media assets also owned by the conglomerate. **Also** commonly mentioned are **the** advantages of vertical integration, such **as** the ownership of television or cable networks that can serve as guaranteed outlets for movies produced by the conglomerate's studio branch. **A** related benefit is the ability to consolidate exploitation of a single story idea or character through books, magazines, television shoes, music publishing, Internet web sites, or other media within a single

[70] Einstein, p. **194-195.**
[71] Bielby and Bielby, p. 581
[72] Waterman, p. **30.**

corporation. The economic advantages of such operating efficiencies (often called economies of scope) are plausible. However, real multimedia exploitation within the same conglomerate is apparently infrequent and other efficiency claims have come into recent disrepute – notably in the cases of AOL-Time Warner and the ABC-Disney mergers.?'

What we may be left with are the market power advantages of a tight oligopoly in the video entertainment space, which do not yield efficient gains while imposing a heavy price in terms of diversity and quality.

QUANTITATIVE MEASURES OF QUALITY

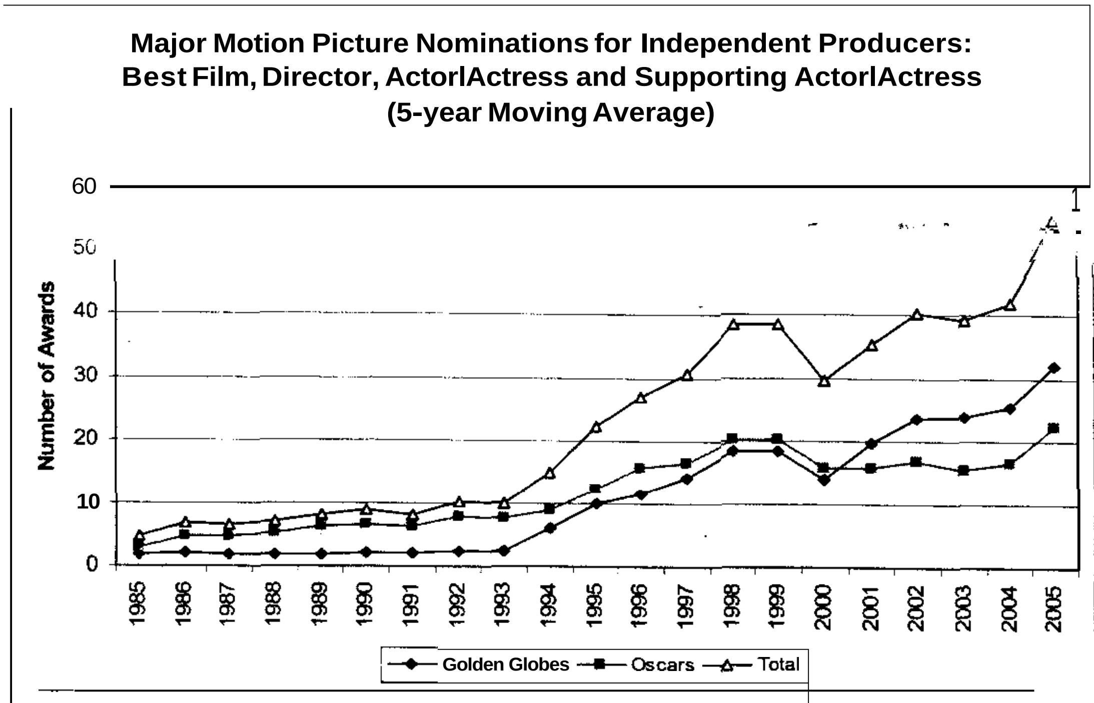
Claims that programming decisions reflect the efficient choice of the best available product are difficult to support in light of this description of the changes in behavior as well as the patterns in the data. These changes and patterns are more consistent with the argument that the vertically integrated oligopoly favors it own content and prefers to deal within the oligopoly.

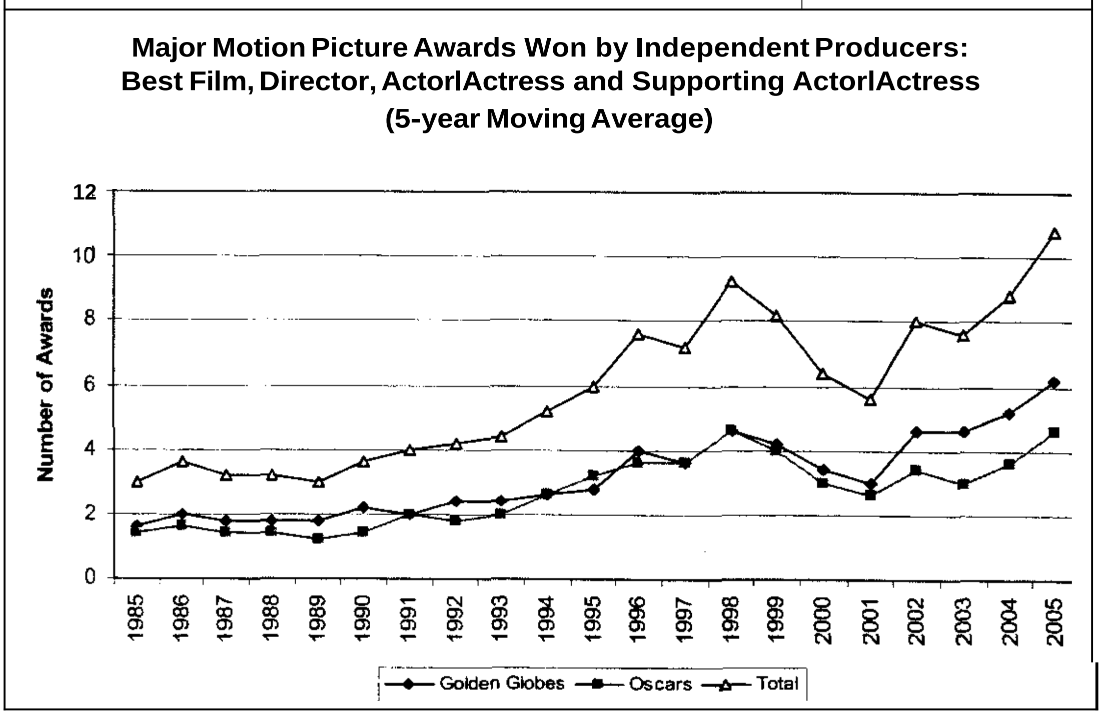
Movies

Objective measures of quality in product in the entertainment space are notoriously difficult to come by. In the movie space, analysts frequently turn to the annual awards ceremonies. The Oscars and Golden Globe Awards contradict the claim that independents suffered some sort of collapse in the 1990s. In fact, their share of awards has been constant, if not rising (see Exhibits VI-1 and VI-2).

[73] Waterman, p. 30; Peltier, Stephanie, "Mergers and Acquisitions in the Media Industries: Were Failures Predictable," *Journal of Media Economics*, 17(4), 2004.

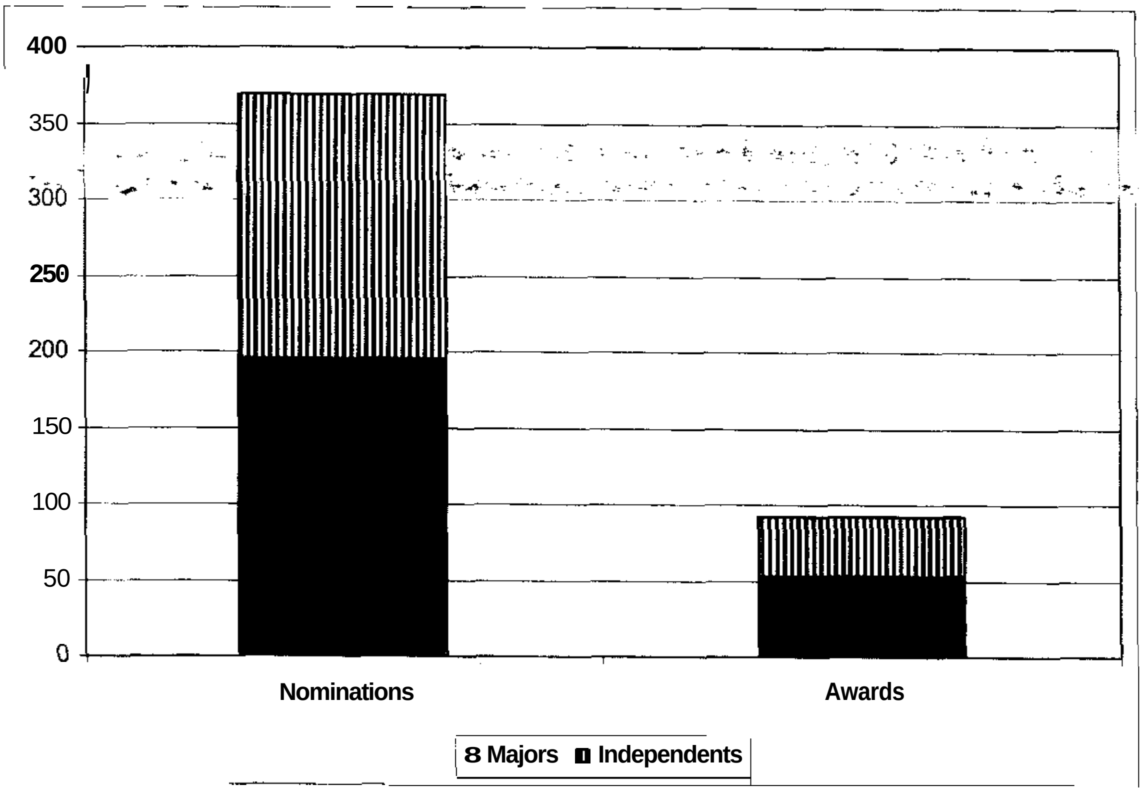
Exhibit VI-1:
Major Categories, Golden Globes and Oscars: Majors v. Independents





Source: Box Office Mojo.com

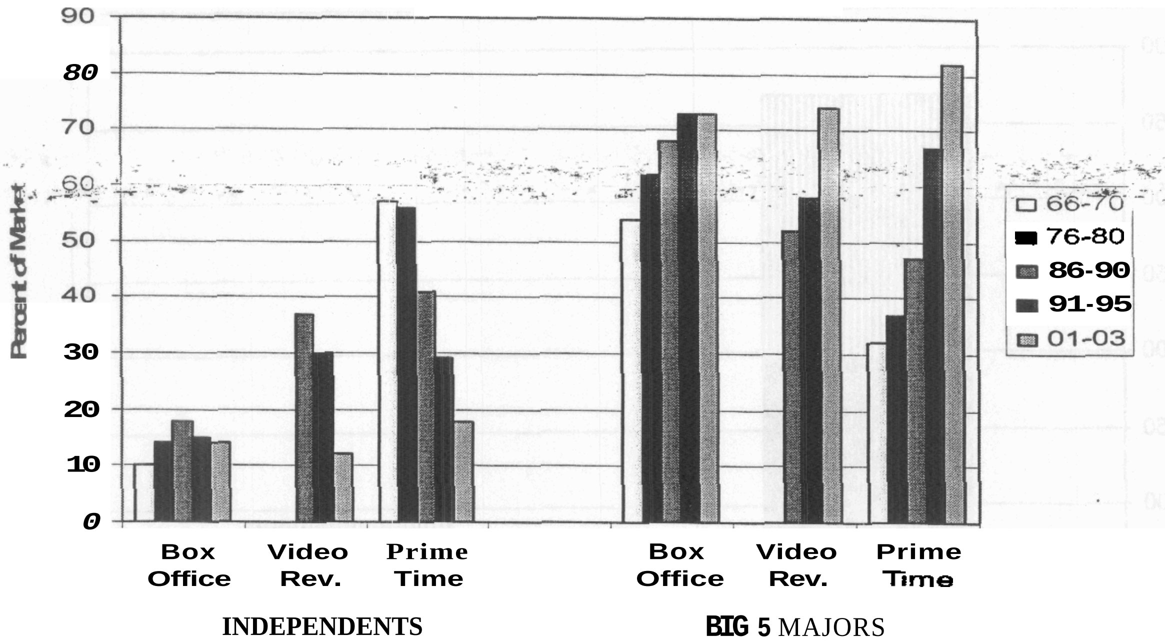
Exhibit VI-2:
Oscar Nominations and Awards 2001-2005:
Majors v. Independents



Source: **Box** Officemojo.com

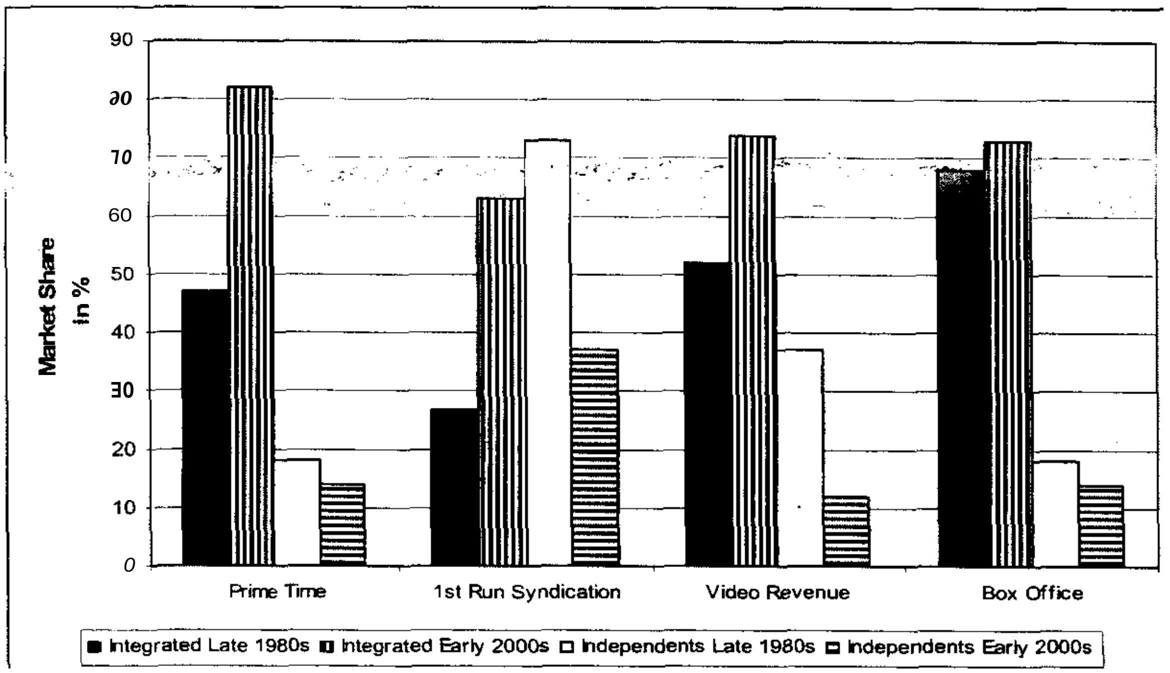
Arguably, a second measure of quality is success. For movies, box office is the predominant measure, although success at the box office reflects many things beyond simple quality, such as the advertising budget. For comparative purposes across time and distribution channels, the market shares in Exhibits VI-3 and **VI-4** make a simple point. Independents held their market share in the **Box** Office much better than they did in the other distribution channels where vertical leverage was most directly exercised.

Exhibit VI-3:
The Shares of Independent Producers in Box Office, Video Revenue and Prime Time Hours Late 1960s to Early 2000s



Sources. Box Office and Video Revenue are five year averages from David Waterman, ***Hollywood's Rood to Riches*** (Cambridge: Harvard University Press, 2005), pp. 21, 25, **86-90** and **01-03.** Big Five **Majors are** the studios that have been acquired by major TV programmers – Disney/ABC; Fox/20th Century Fox; NBC/Universal; Wamer Bros.; CBS/paramount. Other majors (not shown) **are** MGM/UA and Columbia. Independents are what Waterman calls "the residual." Prime Time is percent of hours in 1989, and ***2002*** from Mara Einstein, ***Program diversity and the Program Selection Process on Broadcast Network Television*** (Washington D.C.: Federal Communications Commission, September 2003), pp. ***26.*** First-run syndication is from C. Puresell and C. Ross, "Vertical Integration and Syndication," ***Electronic Media,*** 22(1): 2003, for **1993** and **2002.** It includes only vertical integration and not internal dealing among the big ***5.***

Exhibit VI-4:
Growth of Big 5 Market Share and Vertical Integration in Domestic Markets: Late 1980s to Early 2000s



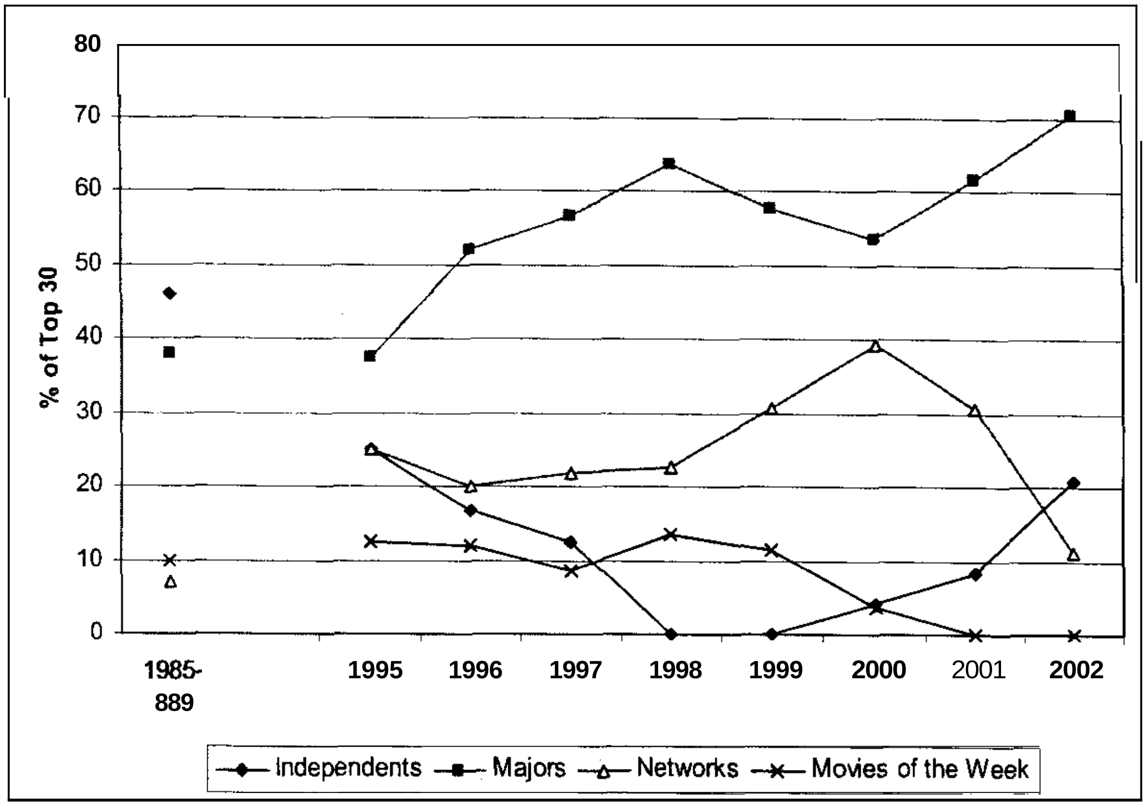
Sources. Box Office and Video Revenue are five year averages from David Waterman, *Hollywood's Road to Riches* (Cambridge: Harvard University Press, 2005), pp. 21, 25, 86-90 and 01-03. Big Five Majors are the studios that have been acquired by major TV programmers – Disney/ABC; Fox/20th Century Fox; NBC/Universal; Warner Bros.; CBS/paramount. Other majors (not shown) are MGM/UA and Columbia. Independents are what Waterman calls "the residual." Prime Time is percent of hours in 1989, and 2002 from Mara Einstein, *Program diversity and the Program Selection Process on Broadcast Network Television* (Washington D.C.: Federal Communications Commission, September 2003), pp. 26. First-run syndication is from C. Puresell and C. Ross, "Vertical Integration and Syndication," *Electronic Media,* 22(1): 2003, for 1993 and 2002. It includes only vertical integration and not internal dealing among the big 5.

Television

The quantitative analysis of the quality of television is even more complex. Independents were virtually eliminated from prime time and have little opportunity to bring new product to that space, so before and after comparisons tell us little, other than the fact that they were excluded. Moreover, there is no box office to count. The essential point here is that given the opportunity to appear in the exhibition space, independents held their own.

Exhibit VI-5 compares the source origin of the top thirty shows **for** two periods: 1985-1989, which is the base period I have been using for the Fin-syn era, and 1995 to 2002 for the post Fin-syn period. Ratings are the closest equivalent to **Box** Office. 1 start with the popularity measure because it tells us about the pattern of types of shows. I have included all non-news shows that appeared in the top 30. I have used the same coding approach as in the earlier analysis of all shows on TV. Thai is, where a major studio is listed

Exhibit V1-5:
Producers of Top 30-Rated TV Shows.



Source: Tim Brooks and Earle Marsh, *The Complete Directory to Prime Time Network and Cable TV Shows: 1946 - Present,* (New York: Ballantine, 2003), Appendix 3; Beta Study System database.

in a co-production, it is considered the producer. Where the producer uses both the name of a network and a major studio, it is counted as the major. The details of the counts might change somewhat with a different approach, hut the basic patterns would he clear.

Prior to the repeal of Fin-syn, independents and major studios dominated the top shows. The networks did not ever pull their weight. They were somewhat underrepresented in these ratings. After the repeal of Fin-Syn, the vertically integrated oligopoly completely dominates the space. There are very few independents and no non-integrated majors in the top 30 shows. When the independents do return to the top **30** in the early 2000s, it is with reality shows, not scripted entertainments.

I have included the category of Movies of the Week, although I do not have the producers for the actual movies for two reasons. First, **as** we have seen, in the broader market share analysis, these were almost always independents and majors prior to the repeal of Fin-Sin; afterwards, they almost entirely had vertically integrated majors as producers. Second, the nature of prime time movies changed. Movies of the Week were big events with large budgets and appeared in the top 30 shows consistently, accounting for about 10 percent of the total, until the end of the 1990s. They then dropped quickly out of sight. This was the period of the expansion **of** Basic cable movies

The pattern of popularity helps to provide background for the analysis of awards – the Emmys. There are a very large number of categories across many different types of shows. The categories also change over time. **A** separate category for Made for TV Movies was not added until the 1990s, so there is no baseline. For the purposes of this analysis, I focus on the Emmys for Best Comedy and Drama. These are series of scripted shows, **for** which awards were consistently given, that most parallel movies and were available to independents.

Over the course of the 1980s there were 20 such awards given for each genre (see Exhibit VI-6). The distribution of the awards closely reflected the market share of the different types of producers. The point here is that if these awards represented an independent measure of quality, the independents held their own. The vertical restriction did not cause "inferior" product?, to be aired. With the repeal of Fin-Syn, independents were banished from these two categories of television entertainment and disappeared from the awards. **As I** have noted, their presence in prime time is now largely restricted to reality shows. The pattern **of** awards is similar to the other data we have seen: as Fin-Syn was under attack in the early 1990s the independents declined and were subsequently eliminated after repeal.

Exhibit VI-6:
Emmys for Best Comedy and Drama

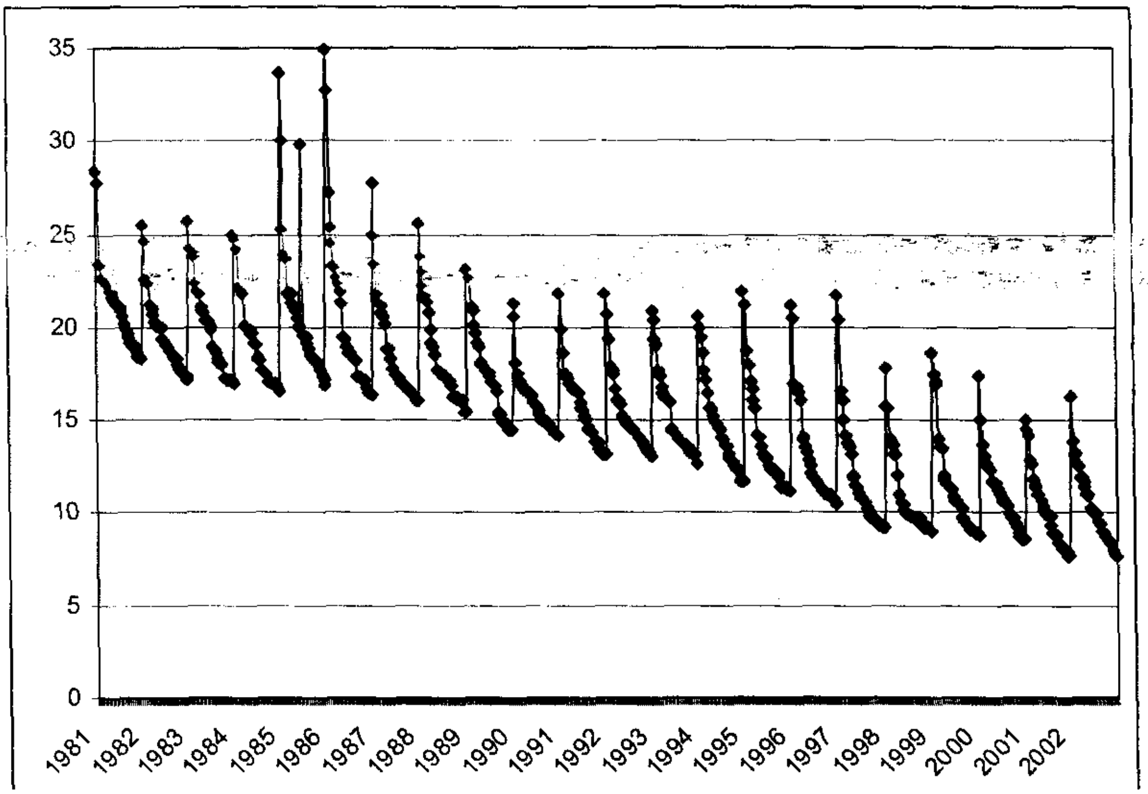
Producer	80-84	85-89	90-94	95-99	00-04
Independents	*70*	40	20	0	**0**
Networks	20	40	50	100	60
Majors	**10**	20	30	***0***	40

Source: Tim **Brooks** and **Earle Marsh,** ***The Complete Directory to Prime Time Network and Cable TV Shows: 1946- Present,*** **(New York** Ballantine, 2003), **Appendix** 3; Beta **Study System database.**

CONCLUSION

The debate over the impact of vertical integration on quality is difficult to resolve, as many factors were affecting the industry. Still, the pattern of declining ratings observed over a twenty year period is consistent with the claim that self-dealing had an impact (see Exhibit VI-7). The Exhibit shows the average rating of the top 30 shows **for** each year. There are *two*

Exhibit VI-7: Declining Ratings of the Top 30 TV Shows



Source: Tim **Brooks and** Earle **Marsh,** ***The Complete Directory to Prime Time Network ond Cable TV Shows:*** *1946* ***– Present,*** **(New York Ballantine, 2003), Appendix 3;** Beta **Study System database.**

shifts downward – one in the early 1990s, as the Fin-Syn rules came under attack one in the late 1990s and early 2000s as the integration of major studios took place. The correlation with the changing pattern of program acquisition discussed earlier is clear. While the quantitative and qualitative evidence on quality cannot prove that vertical integration was the culprit in the decline of quality, it makes a strong case that independents were eliminated not because of an inability to produce high quality and popular content, but rather as a result of a poorly run marketplace for production

VII. CONCLUSION:
PUBLIC POLICY HAS UNDERMINED SOURCE DIVERSITY, WILL THE INTERNET CHANGE ANYTHING?

VERTICAL INTEGRATION TRUMPS TECHNOLOGY

This paper has shown that the policies adopted by the FCC and Congress in the 1990s lead to a dramatic decline in source diversity on broadcast television. In the early and mid 1990s, the Broadcast networks were given three huge advantages in the television video product space. First, they were given camage rights on cable networks (1992). Second, the Financial Interest and Syndication Rules were repealed (1995). Finally, they were allowed to own multiple stations in a single market (1996). They used this leverage to extend their control over the video content product space vertically – by merging with studios – and horizontally – by self-supplying content in broadcast prime time and expanding distribution on cable.

A tight, vertically integrated oligopoly now dominates the broadcast, cable and theatrical space in America. Promises that prime time would not become dominated by the networks, and theories that claimed competition would prevent it, have proven misguided. Hopes that cable and its expanding capacity would create vibrant competition have been dashed as the incumbent broadcaster networks extend their reach over cable's viewers by demanding camage and extending their brand control into the new space. Wile the purpose of this paper is to document what happened and why, it is clear that if policymakers still believe in source diversity, then a change in policy to promote it would he in order.

Previous technological changes have not been able to deconcentrate the product space. It bas taken policy changes to break the stranglehold on distribution. Whether theaters in the

1940s or broadcasters in the 1970s, gate keeping has long been a powerful force in the industry.

Because of the high cost of producing movies and other video content, the aggregation of audiences remains a critical function. With such a powerful hold on all forms of video distribution, it will be extremely difficult to dislodge the dominant players. They are the established brands and continue to gain momentum in the premium, large audience outlets.

THE INTERNET AND DIGITAL BROADCAST PLATFORMS

While the history of the video entertainment product space is clear, as is the basis for adopting policies that promote source diversity, there is no doubt that policymakers who contemplate adopting such policies will be bombarded with claims that, even though the policies that affect the traditional video distribution channels have been disastrous, **we** need not be concerned because 'the Internet changes everything.'

This claim should be viewed with a great deal of skepticism. In fact, the more likely question that policy makers in this area should ask is "Do the Internet and the new digital era change anything?"

The best assessment at present is that "only a few small experiments in altering the movie-release paradigm have been conducted to date."[74] While the role of the Internet is currently unclear, one thing is certain. It is another distribution platform that the vertically integrated conglomerates are moving to dominate. Whether it will be able to de-concentrate the video exhibition space described in this section remains subject to debate. However,

---

[74] Thompson, **Anne,** 'Independent Producers and Distributors," *Hollywood **Reporter,*** August 1,2006,p.l.

without sufficient regulation that provides equal access to all, the Internet will fall subject to the same fate as broadcast television, premium cable television, and finally basic cable television: domination by the vertically integrated oligopoly created by the regulatory changes of the last decade.

As we have seen, in a world with limited shelf space, placement is everything. If you cannot get on the shelf, the audience cannot find you. In a world of infinite shelf space, placement is *still* everything. When there is such a cacophony of outlets, the audience cannot find you unless you have prominent placement. Whether it is simultaneous release on multiple platforms or widespread digital distribution, the key challenge remains "finding a way to brand a movie." In the end, says producer Jim Stark, "Nothing beats five weeks in a theater."[75]

One need only review the critique of the launches of new Internet-based distribution platforms to see the problem in clear relief. The central questions are: what do their libraries look like? What are the majors doing with respect to the platform? If the majors are not there, the platform is deemed to have dim prospects. When the majors and networks are there, they tend to get the best placement and the best deals. Little has changed. They are the most prominent and have the resources to preserve that prominence. This is clearly reflected in the reporting on the announcement of Apple's "video streaming gadget code-named ITV"[76]

> Apple's competition included the movie studios themselves plus many other ambitious firms such as Amazon, which recently unveiled its Unbox download service.
>
> TV shows are also starting to turn up the online service for Microsoft's Xbox…

---

[75] Thompson, p. 1.
[76] Ward, Mark, "Apple Video Divides Industry," *BBC News, September 13,* 2006, p. 1.

> Apple pre-announced its ITV box in a bid to convince potential partners that its ambitions are serious.. . it hoped to build "momentum" and get movie makers and broadcasters talking about putting content on the Apple service. For example, Amazon's Unbox offers movie downloads from 20th Century **Fox,** Paramount, Sony, Universal and Warner Bros. So **far,** only Disney movies are available from Apple.[77]

The quote from Les Moonves of CBS above, which touted **the** advantages that broadcasters have, was actually given in response to claims that the Internet was displacing the networks. Responding to **the** claim that broadcast share would shrink, Moonves said **"If** you want 30 million people, you can't get that anywhere else.. .Television will hold and the Internet will augment what we do."[78]

Dana Walden of 20th Century Fox TV echoes this view. "In the digital space, the extensions seem to come after the fact. **We're** trying to create brands on the (broadcast) networks that are enhanced by digital opportunities."[79]

While the potential and prospects are unclear, the reaction to a new technology is predictable and the studios and networks will **seek** to extend their gatekeeper function. Already, as one recent article observed, "studio business affairs executives now were insisting that this exclusivity [in rights to distribute] include the Internet as well."[80]

Thus, the Internet has not done much to break the **grip** of the vertically integrated oligopoly on the video revenue streams in the video entertainment product space. **As** the independent producers emphasized in the interviews, these firms control **the** TV outlets and syndication, have the output deals for domestic and foreign theatrical releases, and have a

[77] Ward, p. **2.**
[78] Fabrikant and Carter, p. C1 1.
[79] "A TV Navigation Guide," *Hollywood Reporter,* September 13,2006, p. **2.**
[80] Hlestand, Jesse, "Profit Anticipation," *Hollywood Reporter,* June *6,2006,* p. 1.

huge advantage in foreign TV deals. They control the branding process with their access to audiences that is being leveraged into dominance of commercial distribution on the Internet.

Given the history of gate keeping in the industry and these observations on the impact of lntemet distribution, the advent of digital TV, which will increase the number of channels the broadcasters control as much a i si:: fold, does not hold much promise to deconcentrate the TV sector. Broadcasters, who have leveraged a series of favorable policies into domination of the video entertainment product space, will now have more resources to strengthen their position, enrich their brands and repurpose their content across another distribution channel. Technological change and an increase in distribution capacity have repeatedly failed to restrict the gate keeping power of vertically integrated entities in this product space.

CONCLUSION

If policymakers value source diversity, which they should, structural restraints on the market power of the vertically integrated companies will have to be imposed. These structural restraints will have to apply to both the broadcast and cable distribution channels because public policy created the leverage that broadcasters have used to dominate the cable distribution platform. The restraints should also apply to the Internet and all other developing distribution technologies.