Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
	)	MB Docket No. 07-198
Review of the Commission's Program Access	)	
Rules and Examination of Programming Tying	)	
Arrangements	)	
	)	

REPLY COMMENTS

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I. INTRODUCTION AND SUMMARY

The record in this proceeding reflects a sharp divide. On one side are the media conglomerates, programmers and broadcasters. On the other are smaller distributors and the consumers they serve, most often in smaller markets and rural areas.

Not surprisingly, programmers and broadcasters defend current wholesale programming and retransmission consent practices. They argue that current wholesale practices are necessary to preserve their business models and expand distribution of, and payment for, their programming, regardless of demand, or lack thereof. Oddly, however, they also defend current wholesale practices as in the best interests of *consumers*. Essentially, they argue that consumers are better off paying for channel packages bloated with undesired channels, and that consumers served by smaller distributors somehow benefit because smaller distributors must pay much more than large distributors for the very same channels. Programmers and broadcasters insist that any change to the wholesale status quo threatens a range of awful outcomes. Finally, they argue that even if current wholesale practices harm the public interest, the Commission has no authority to do anything about it.

The record also contains extensive input from smaller distributors, more than 1,500 companies represented by ACA and other groups. These small companies describe a wholesale market rife with "take it or leave it" tying and bundling, tier placement and distribution obligations, and widespread price discrimination, all imposed by programmers and broadcasters with overwhelming market power. Moreover, <u>price discrimination in retransmission consent transactions is rapidly escalating to unprecedented levels</u>.

The record shows that wholesale programming and retransmission consent practices restrict the ability of small and medium-sized cable companies to offer more choice at retail, while at the same time, significantly increasing their costs. Smaller distributors call for the Commission to act and alleviate the harms resulting from current wholesale practices. To this end, ACA has proposed minor adjustments to the program access and retransmission consent regulations that would help address the problems with the current wholesale market, and help smaller cable companies deliver more choice and better value at retail.

The record presents the Commission with a clear choice. The Commission can act to mitigate the harms of current wholesale practices, or the Commission can do nothing and accept the status quo. ACA advocates the former. The proposals set forth in ACA's comments provide a restrained and measured approach, and the Commission should adopt them.

These Reply Comments address the following six issues:

The Commission must act to constrain sharply escalating retransmission consent price discrimination. The magnitude of retransmission consent price discrimination against smaller distributors has reached unprecedented – and unconscionable – levels. <u>Broadcast licensees are exploiting their market power to extract fees from smaller distributors up to twenty times higher than paid by larger MVPDs</u>. As former FCC Chief Economist William P. Rogerson concludes, <u>no economic rationale or discernable public policy supports this price discrimination</u>. Rather, retransmission consent price discrimination represents sheer abuse of market power by powerful broadcast groups and networks. This conduct raises costs for rural distributors and consumers and impedes broadband deployment. The Commission should not allow this to continue. As stated by Professor Rogerson:

> Higher retransmission consent fees are passed through to subscribers in the form of higher subscription fees. The government has granted commercial broadcasters with valuable spectrum and provides a range of legal and regulatory protections to help ensure the availability of broadcast television to the public. <u>The use of some of those legal and regulatory protections to extract substantially higher fees from smaller distributors and their customers raises policy questions that the Commission should consider carefully</u>.
>
> <u>I think that the Commission should carefully consider whether adjustments to regulations that would spread this burden more equally across all MVPD subscribers would be more consistent with the Commission's public policy objectives</u>.

The record confirms that current wholesale programming and retransmission consent practices harm broadband deployment. The record corroborates ACA's findings that current wholesale practices impede broadband deployment, especially in smaller markets. To advance the important policy goal of ubiquitous broadband, the Commission must curtail wholesale programming and retransmission consent practices that substantially increase costs for video services and divert resources from rural broadband deployment.

The record confirms that smaller distributors face "take it or leave it" wholesale tying and bundling, tiering and distribution obligations, and price discrimination. Programmers and broadcasters claim that they routinely offer channels on a standalone basis and provide flexible "menus" of "options." The record shows the wholesale market described by programmers and broadcasters is a fantasy land, at least for small and medium-sized cable companies. Smaller distributors uniformly describe how "take or leave it" tying, bundling, tiering and distribution obligations, and price discrimination predominate their transactions with programmers and broadcasters.

ACA's proposed adjustments to Commission regulations fully accommodate programmer and broadcaster concerns with a prohibition on bundled offerings. Programmers and broadcasters raise several objections to a blanket prohibition on wholesale channel packages. ACA's proposals fully accommodate those objections. Rather than prohibit wholesale bundles, the Commission should obligate programmers and broadcasters to also offer channels on a standalone basis, on reasonable prices, terms and conditions. This change would not *restrict* wholesale offerings, it would *expand* them, with concomitant benefits at the retail level.

Additionally, programmers claim they already offer channels on a standalone basis, so they should have no objection to codification of this practice.

Concerning retransmission consent, ACA's proposals would help protect consumers from non-cost based price discrimination. Professor Rogerson concludes that regulations like those proposed by ACA could alleviate the harms of retransmission consent price discrimination "in a workable and fairly simple fashion."

The record confirms the need for a standstill provision in program access and retransmission consent complaint regulations. Smaller distributors consistently describe how the current program access and retransmission complaint processes do not provide effective remedies. As the Commission has repeatedly found, and as this record affirms, when a smaller cable system is involved, the threat of temporary withdrawal of a must have channel overwhelmingly skews a negotiation in favor of the programmer or broadcaster. The Commission should adjust its regulations to permit continued carriage of a channel while a program access or retransmission consent complaint is pending.

The record validates that the Commission has authority to adopt the regulations proposed by ACA. Programmers and broadcasters argue that the Commission does not have authority to address the public interest harms caused by current wholesale practices. The record reflects ample input to the contrary.

The record in this proceeding demonstrates the incentive and ability of powerful programmers and broadcasters to use wholesale practices to reduce choice and raise costs at retail, harming the public interest, especially in markets served by small and medium-sized cable companies. Consumers in those markets need some help from the Commission. The record in this proceeding provides ample basis for the Commission to act.

II. THE COMMISSION MUST ACT TO ADDRESS THE HARMS OF RAPIDLY ESCALATING RETRANSMISSION CONSENT PRICE DISCRIMINATION.

As described in ACA's comments, wholesale price discrimination against small and medium-sized cable companies predominates in the marketplace.[1] Programmers and broadcasters routinely charge smaller companies substantially higher per-subscriber fees than they charge large companies, with little or no basis in cost. The public interest harms from this wholesale practice are manifest. Wholesale price discrimination: (i) increases costs for consumers, especially in the smaller markets served by ACA members;[2] (ii) hurts competition by undercutting smaller companies' ability to compete on price;[3] and (iii) impedes broadband deployment in rural markets by

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[1] *In the Matter of Implementation Review of the Commission's Program Access Rules and Examination of Programming Tying Arrangements*, Report and Order and Notice of Proposed Rulemaking, MB Docket No. 07-198, Comments of the American Cable Association at 17-18 (filed Jan. 3, 2008) ("*ACA Comments*").

[2] *In the Matter of General Motors Corporation and Hughes Electronic Corporation, Transferors, and The News Corporation Limited, Transferee, For Authority to Transfer Control*, Memorandum Opinion and Order,19 FCC Rcd. 473, ¶ 209 (2004) ("*News Corp. Order*") ("News Corp.'s use of market power to extract artificially high levels of compensation from MVPD rivals, or other carriage concessions, could make rival MVPDs less viable options for consumers, thus limiting consumer choice."); *In the Matter of Carriage of Digital Television Broadcast Signals*, First Report and Order and Further Notice of Proposed Rulemaking, 17 FCC Rcd. 6441, ¶ 35 (2001) (acknowledging small cable operators concerns about unregulated retransmission consent demands and its effect).

[3] *ACA Comments* at 19 ("Price discrimination combined with tying, bundling, tiering and distribution obligations all raise the wholesale cost of cable and undercut the ability of smaller companies to compete on price.").

diverting resources from infrastructure investment.[4] These public interest harms provide ample basis for the Commission to constrain this price discrimination by adopting the regulatory adjustments proposed by ACA.[5]

Based on the record in this proceeding and additional information gathered by ACA, the problem is much worse than previously reported. <u>Broadcasters are rapidly escalating retransmission consent price discrimination to unprecedented – and unconscionable – levels</u>. Small and medium-sized cable companies are facing per-subscriber fees many times higher than what larger MVPDs pay for the exact same broadcast stations. As analyzed by Professor William Rogerson in the report accompanying these reply comments, <u>no economic rationale or discernable public policy basis exists for retransmission consent price discrimination of this magnitude</u>.[6] This price discrimination results solely from unconstrained abuse of market power by broadcasters against smaller distributors.

A. Broadcasters are now demanding that small and medium-sized cable companies pay retransmission consent fees up to twenty times higher than larger MVPDs pay for the same stations.

A review of retransmission consent pricing information in the record and elsewhere shows that price discrimination against smaller distributors is escalating to unprecedented levels.

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[4] *Id.* at 20 ("The ever-escalating pressure on cost and bandwidth from programmers and broadcasters can delay and even prevent very small systems from upgrading to provide broadband.").

[5] *Id.* at 20-26.

[6] William P. Rogerson, *The Economic Effects of Price Discrimination in Retransmission Consent Agreements*, at 3 and 12 (filed Feb. 12, 2008) (attached as Appendix A) ("*Rogerson Report*").

We start with the data submitted in the *Eisenach Report*.[7] Therein, we learn that affiliate groups, including Sinclair and Nexstar, are, on average, charging cable operators and DBS providers between $0.13 and $0.25 per month per subscriber for network stations.[8] The recent retransmission consent analysis by the Congressional Research Service reports similar findings.[9] At the same time and for the very same broadcast stations, <u>smaller MVPDs are being charged between $0.50 and $1.00 per subscriber per month</u>.[10] Put another way, <u>broadcasters are charging smaller MVPDs per-subscriber rates that are, on average, ***four to seven*** times higher than paid by larger MVPDs</u>.

But that is just part of the picture. It gets worse when we consider the largest MVPDs and their retransmission consent deals. The *Eisenach Report's* estimates of retransmission consent fees likely include recently concluded long-term agreements with Comcast and Time Warner, for which little, if any, cash consideration was paid.[11] A very generous estimate of the per-subscriber cash value of the Sinclair/Comcast and Sinclair/Time Warner transactions falls in the range of $0.05 – $0.10 per subscriber per

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[7] *In the Matter of Implementation Review of the Commission's Program Access Rules and Examination of Programming Tying Arrangements*, Report and Order and Notice of Proposed Rulemaking, MB Docket No. 07-198, Comments of the Walt Disney Company, Exhibit A, Jeffery A. Eisenach, *Economic Implications of Bundling in the Market for Network Programming* (filed Jan. 4, 2008) ("*Eisenach Report*").

[8] *Id.*, ¶¶ 82, 84.

[9] Charles B. Goldfarb, *CRS Report for Congress*, *Retransmission Consent and Other Federal Rules Affecting Programmer-Distributor Negotiations: Issues for Congress*, at 31-34, 40-53 (July 9, 2007) ("*CRS Retransmission Consent Report*").

[10] *CRS Retransmission Consent Report* at 36 ("Industry observers had differences of opinion on the terms of the agreements; some thought CBS was receiving 50 cents per subscriber per month…or even more…."); *In the Matter of Implementation Review of the Commission's Program Access Rules and Examination of Programming Tying Arrangements*, Report and Order and Notice of Proposed Rulemaking, MB Docket No. 07-198, Comments of the National Telecommunications Cooperative Association at 22 (filed Jan. 4, 2008) ("*NTCA Comments*") ("Broadcasters seek additional revenues by charging small and medium rural video providers rates as high as $1.00 per subscriber per month to carry a broadcast station in-DMA signal/channel.); *Rogerson Report* at 11, n.11.

[11] *CRS Retransmission Consent Report* at 50-53.

month. From this, it becomes readily apparent that broadcasters are charging smaller MVPDs retransmission consent fees between ***ten and twenty times*** higher than what the largest distributors pay.

And the magnitude of this price discrimination is growing geometrically. ACA has recently received reports of one major broadcast network demanding retransmission consent fees of $1.65 per subscriber per month from small cable operators, all for the same station where DBS and the largest cable operators pay between $0.00 and $0.15.

As analyzed by Professor Rogerson, there is no economic rationale or discernable public policy supporting retransmission consent price discrimination, and the Commission should consider adjusting its regulations to address the problem:

> In some markets, price discrimination can have the desirable effect that it provides firms with the incentive and ability to serve more customers by allowing them to simultaneously serve customers with a low ability/willingness to pay for the good at low prices while still serving customers with a higher ability/willingness to pay for the good at higher prices. No such economic rational applies in the case of retransmission consent. Obviously, local broadcasters would still provide their signals to the major MVPDs if they were not allowed to charge even higher prices to small and rural MVPDs. Therefore the main effect of price discrimination in this case, is simply to allow broadcasters to charge higher prices to MVPDs with less bargaining power.[12]
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> * * *
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> Higher retransmission consent fees are passed through to subscribers in the form of higher subscriber fees….The government has granted commercial broadcasters with valuable spectrum and provides a range of legal and regulatory protections to help ensure the availability of broadcast television to the public. The use of some of those legal and regulatory protections to extract substantially higher fees from smaller distributors and their customers raises policy questions that the Commission should consider carefully.[13]

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[12] *Rogerson Report* at 12 (emphasis added).

[13] *Id.* at 13-14 (emphasis added).

* * *

> I think that the Commission should carefully consider whether adjustments to regulations that would spread this burden more equally across all MVPD subscribers would be more consistent with the Commission's public policy objectives.[14]

Retransmission consent price discrimination is escalating for one principal reason – broadcasters are ratcheting up their abuse of market power over smaller cable companies. This should come as no surprise; the Commission has repeatedly recognized that small and medium-sized cable companies are especially vulnerable to withdrawal of must have programming.[15] Professor Rogerson's analysis confirms this.[16] Exploiting this vulnerability, broadcasters have now made price discrimination their business plan.

Looking ahead, Sanford Bernstein satellite analyst Craig Moffett offers the following ominous observation: "Two trends are clear from 2007: retrans consent generates cash and smaller operators . . . will bear the brunt of the pain."[17]

Mr. Moffett gets it half right. As the Commission has repeatedly recognized, when broadcasters and programmers use the threat of withdrawal to extract higher rates, smaller cable companies *and* consumers will feel the pain.[18]

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[14] *Rogerson Report* at 4 (emphasis added).

[15] *News Corp. Order*, ¶ 176 ("[W]e agree with ACA to the extent that it argues that small and medium-sized MVPDs may be at particular risk of temporary foreclosure strategies aimed at securing supra-competitive programming rate increases for 'must have' programming….."), ¶ 204 ("[T]he *ability* of a television broadcast station to threaten to withhold its signal, even if it does not actually do so, changes its bargaining position with respect to MVPDs, and could allow it to extract higher prices, which ultimately are passed on to consumers.); *Implementation of the Cable Television Consumer Protection and Competition Act of 1992 – Development of Competition and Diversity in Video Programming Distribution: Section 628(c)(5) of the Communications Act: Sunset of Exclusive Contract Prohibition*, Report and Order and Notice of Proposed Rulemaking, 22 FCC Rcd. 17,791, ¶ 120 (2007) ("*Program Access Order and NPRM*").

[16] *Rogerson Report* at 6-9.

[17] Mike Farrell, *Retrans on the Rise*, MULTICHANNEL NEWS, Jan. 7, 2008, at 30 (emphasis added).

B. Retransmission consent price discrimination harms consumers.

It is well-settled that increased retransmission consent fees, especially of the magnitude broadcasters are demanding of small and medium-sized cable companies, directly lead to higher costs for consumers.[19] Even network owner NBC concedes this.[20] In the case of retransmission consent price discrimination, the public interest harm is more concentrated. One class of viewers – those served by smaller distributors – bears the burden of higher costs. As Professor Rogerson concludes, retransmission consent price discrimination results in an unwarranted cost disparity between viewers of the same programming.

> MVPDs pass higher programming costs back to their subscribers in the form of higher subscriber fees. <u>Therefore, the main effect of price discrimination in retransmission consent agreements is simply that different groups of viewers are being charged different prices to view the same programming</u>.[21]

In the face of this, the record contains a peculiar assertion by broadcasters – that *consumers* are the main benefactors of retransmission consent price discrimination.[22]

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[18] *News Corp. Order*, ¶ 176, 204; *Program Access Order and NPRM*, ¶ 120.

[19] *News Corp. Order*, ¶ 209 ("If News Corp. can…charge higher fees…these fees are unlikely to be absorbed solely by the MVPDs, but would be passed on to consumers in the form of higher rates.").

[20] *In the Matter of Implementation Review of the Commission's Program Access Rules and Examination of Programming Tying Arrangements*, Report and Order and Notice of Proposed Rulemaking, MB Docket No. 07-198, Comments of NBC Universal, Inc. and NBC Telemundo License Co., at 54 (filed Jan. 4, 2008) ("*NBC Comments*") ("In addition to higher per-subscriber fees…which would be passed through to subscribers….").

[21] *Rogerson Report* at 13 (emphasis added).

[22] *In the Matter of Implementation Review of the Commission's Program Access Rules and Examination of Programming Tying Arrangements*, Report and Order and Notice of Proposed Rulemaking, MB Docket No. 07-198, Comments of the Fox Entertainment Group, Inc. and Fox Television Holdings, Inc., at 12-16 (filed Jan. 4, 2008) ("*Fox Comments*"); *In the Matter of Implementation Review of the Commission's Program Access Rules and Examination of Programming Tying Arrangements*, Report and Order and Notice of Proposed Rulemaking, MB Docket No. 07-198, Comments of the National Association of Broadcasters at 27-30 (filed Jan. 4, 2008) ("*NAB Comments*").

At least for consumers served by small and medium-sized cable companies, broadcaster claims of "consumer benefit" collapse under minimal scrutiny.

Broadcasters first assert that higher retransmission consent fees benefit consumers by increasing investment in local and network programming.[23] Broadcasters fail to support this statement with any evidence of any increase in local programming. And for good reason, the evidence does not exist. In reality, <u>while broadcasters are raising retransmission consent fees, they are reducing local programming</u>.[24] Further, ACA members report that <u>affiliate groups like Sinclair, Nexstar and others are eliminating smaller market local news operations</u>, while at the same time raising the price of retransmission consent for smaller companies. In short, the current retransmission consent process harms consumers by raising costs and reducing local programming.

In the same vein, the networks argue that retransmission consent benefits consumers by supporting investment in quality network programming.[25] But if this were the case, that investment would lead to more consumers watching broadcast networks. The truth is exactly opposite; consumers continue to watch less and less of the broadcast networks.[26] Again, the facts fail to support broadcaster assertions that consumers "benefit" from current retransmission consent practices. And in markets

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[23] *NAB Comments* at 27.

[24] *CRS Retransmission Consent Report* at 22; *DPI Report* at 78 (the majority of what local television stations provide is <u>not</u> locally-produced content).

[25] *In the Matter of Implementation Review of the Commission's Program Access Rules and Examination of Programming Tying Arrangements*, Report and Order and Notice of Proposed Rulemaking, MB Docket No. 07-198, Comments of the Walt Disney Company at i (filed Jan. 4, 2008) ("*Disney Comments*"); *Fox Comments* at 14 ("[G]iving broadcasters the 'opportunity to be compensated for retransmission consent should increase the incentives to provide attractive programming.'").

[26] *CRS Retransmission Consent Report* at 22 ("[T]he four major broadcast networks lost 2.5 million viewers during the spring of 2007.").

served by ACA members, the consumer harm from retransmission consent price discrimination is manifest.

C. The record shows that for small and medium-sized cable companies retransmission consent "negotiations" are most often "take it or leave it."

In the face of escalating retransmission consent price discrimination, broadcaster filings offer Pollyanna descriptions of a rosy world of retransmission consent. For example, NAB claims "broadcasters, typically, offer a menu of consideration options"[27] and cash payments occur only "rarely."[28] Maybe this describes retransmission consent negotiations between broadcasters and the largest MSOs.[29] But for small and medium-sized cable operators, the reality of retransmission consent is one-sided, abusive, and costly.

The following excerpts from the record describe the real world of retransmission consent for more than 1,500 small and medium-sized cable companies.

From NTCA:

> Retransmission consent has become "a skewed playing field where broadcasters control all elements of price, terms and conditions of negotiations with MVPDs."[30]

* * *

> Retransmission consent "is especially harmful to the interests to small independent and rural MVPDs and their customers. Many MVPDs must pay

[27] *NAB Comments* at 2.

[28] *Id.* at 16.

[29] *CRS Retransmission Consent Report* at 10 ("Content providers and programmers are taking advantage of structural market changes favorable to them to pressure MVPDs to make cash payments for programming that until now was available either for free or for non-cash considerations (or, where cash payments have been made in the past, to make higher cash payments). Some MVPDs have had sufficient countervailing market power to resist, or limit these changes….").

[30] *NTCA Comments* at 22.

whatever rate the in-DMA market broadcaster charges and may not look to neighboring markets for better deals."[31]

From the Digital Policy Institute:

"It is fallacious to call this retransmission consent process 'negotiation.' [Smaller] cable companies are unable to negotiate. Their only option is to accede to the broadcaster's requests or go without the channel."[32]

From OPASTCO et al.:

Current broadcaster fee demands on small MVPDs have "become debilitating….Broadcasters presently have insufficient incentive to provide retransmission consent to smaller video providers at reasonable rates." [33]

From Liberty Cablevision of Puerto Rico:

Out-of-state companies impose "cash payments" and impose "programming to the local public" without any regard to local markets.[34]

These descriptions of retransmission consent negotiations, along with those submitted by ACA,[35] show that the divide between large and small is clear and growing. So long as broadcasters' exercise of market power goes unconstrained, price discrimination and the harm to consumers will continue to escalate.

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[31] *Id.* at 23.

[32] *NTCA Comments*, Ball State University Digital Policy Institute, *Retransmission Consent, Must Carry and the Public: Current Economic and Regulatory Realities of Multichannel Video Providers*, at 77 (filed Jan. 4, 2008) ("*DPI Report*").

[33] *In the Matter of Implementation Review of the Commission's Program Access Rules and Examination of Programming Tying Arrangements*, Report and Order and Notice of Proposed Rulemaking, MB Docket No. 07-198, Comments of the Organization for the Promotion and Advancement of Small Telecommunications Companies; the Independent Telephone and Telecommunications Alliance; the Western Telecommunications Alliance; and the Rural Independent Competitive Alliance, at 11 (filed Jan. 4, 2008) ("*OPASTCO et al. Comments*").

[34] *In the Matter of Implementation Review of the Commission's Program Access Rules and Examination of Programming Tying Arrangements*, Report and Order and Notice of Proposed Rulemaking, MB Docket No. 07-198, Comments of Liberty Cablevision of Puerto Rico, Ltd. at 1 (filed Jan. 4, 2008) ("*Liberty Cablevision Comments*").

[35] *ACA Comments* at 7-9.

D. To mitigate the harms of retransmission consent price discrimination, the Commission should adjust its regulations as proposed by ACA.

ACA's comments include proposed adjustments to the retransmission consent regulations that would help moderate price discrimination. In short, these regulations would prohibit non-cost based price discrimination and would allow an aggrieved MVPD to petition the Commission for relief. To be clear, these regulations would not restrict a broadcaster's ability to seek and obtain consideration for retransmission consent. The regulations would merely provide a check on the ability of a broadcaster to charge a small cable company much higher rates simply because it is small.

This principal of non-discrimination springs directly from the program access regulations. As analyzed by Professor Rogerson, these regulations, after which ACA's retransmission consent proposals are patterned, would address the harms of retransmission consent price discrimination in a relatively workable and simple fashion:

> [T]he current program access regulations provide a model showing that it is possible for the Commission to implement this more complex sort of regulatory requirement in a relatively workable and simple fashion. In particular, current program access regulations require cable network programmers that are vertically integrated with a cable system to make their programming available to non-affiliated MVPDS at the same terms and conditions that it is made available to their own affiliated cable systems. The regulation is enforced by allowing aggrieved parties to file complaints with the Commission that are then investigated. The threat that complaints can be filed, and that the subsequent investigation would be costly and time consuming for all parties, then provides programmers with some incentive to avoid violations of the rules in the first place. While this system undoubtedly does not work perfectly, I note that the Commission has been satisfied enough with its performance to renew these regulations a number of times.[36]

By incorporating the nondiscrimination standard into retransmission consent

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[36] *Rogerson Report* at 14-15.

regulations, the Commission can efficiently alleviate the consumer harm caused by broadcasters' current practices, especially the rapidly escalating price discrimination against small and medium-sized cable companies.

ACA also proposes regulatory adjustments that would create the right for cable systems subject to effective competition to offer, and customers to choose, increasingly costly retransmission consent stations on a separate tier,[37] exactly like DBS subscribers can do today. Broadcasters currently mandate distribution of retransmission consent stations to all subscribers, leaving customers with no choice but paying escalating retransmission consent fees.

The record also reflects continuing support among smaller distributors for a "right to shop" for out-of-market stations,[38] as proposed in ACA's *Petition for Rulemaking*.[39] This change would provide a market mechanism to moderate retransmission consent prices.

III. THE RECORD SHOWS THAT CURRENT WHOLESALE PROGRAMMING AND RETRANSMISSION CONSENT PRACTICES HURT BROADBAND DEPLOYMENT, ESPECIALLY IN SMALLER MARKETS.

ACA's comments identify the substantial public interest harms of current wholesale programming and retransmission consent practices, including the harm to

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[37] *ACA Comments* at 25 ("[S]ystems subject to effective competition should have the flexibility to offer increasingly costly network broadcast stations on a separate tier.").

[38] *NTCA Comments* at 23 ("Because many rural video providers cannot shop in neighboring DMAs for lower rates, rural providers are at the mercy of all broadcasters operating in their DMA….NTCA urges the Commission to rule on the *ACA Petition for Rulemaking*…"); *OPASTCO Comments et al.* at 11, n.37 ("The solution [proposed in the *ACA Petition for Rulemaking*] would allow the marketplace, rather than one entity, to determine the price small video providers should pay for content if their original supplier chooses to require additional payment for retransmission consent.").

[39] American Cable Association Petition for Rulemaking, *In the Matter of Petition for Rulemaking to Amend 47 CFR 76.64, 76.93 and 76.103 Retransmission Consent, Network Non-Duplication, and Syndicated Exclusivity*, MB Docket No. RM-11203, at 34 (filed Mar. 2, 2005) ("In short, all that we request is this: When a broadcaster seeks a "price" for retransmission consent, a small cable company has the ability to "shop" for lower cost network programming for its customers.").

broadband deployment.[40] The comments of groups representing hundreds of rural cable operators and small telcos corroborate ACA on this point.

Commenters representing rural cable systems and small telcos describe how fair and reasonable access to popular channels is critical to upgrading networks and offering broadband. OPASTCO aptly describes this as "the intrinsic link between the availability of video services and broadband deployment."[41] Several commenters underscore how current wholesale programming and retransmission consent practices undercut the ability to offer a competitive video product, impeding broadband deployment.

> *From NTCA*:
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> "The ability to offer a quality video product to customers is…a key driver of broadband deployment in rural areas and is essential to the long-term viability of rural communications providers."[42]
>
> *From CA2C*:
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> "Investment in broadband infrastructure can be especially challenging in sparsely populated, high-cost rural areas. The link between broadband penetration and video services has been demonstrated for both urban and in particular, rural markets."[43]
>
> *From OPASTCO et al.*:
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> The current wholesale market "restricts consumer choice and impedes entry into the MVPD market. This, in turn, impedes additional broadband investment, making Commission action imperative."[44]

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[40] *ACA Comments* at 18-20.

[41] *OPASTCO et al. Comments* at ii.

[42] *NTCA Comments* at 2.

[43] *In the Matter of Implementation Review of the Commission's Program Access Rules and Examination of Programming Tying Arrangements*, Report and Order and Notice of Proposed Rulemaking, MB Docket No. 07-198, Comments of The Coalition for Competitive Access to Content, at 20 (filed Jan. 4, 2008).

[44] *OPASTCO et al. Comments* at 19.

From Bend Broadband et al.:

"Our customers seek choices that offering a broad variety of channels provides, but they also seek improved broadband speeds and advanced service that are jeopardized by coerced carriage of bandwidth-consuming tied and bundled channels."[45]

As the Commission has repeatedly recognized, promoting broadband deployment is a national communications policy goal of the highest priority.[46] As the record in this proceeding shows, in many rural markets, the wholesale practices of programmers and broadcasters undercut this goal.

IV. THE RECORD SHOWS THAT SMALLER MVPDS FACE WIDESPREAD WHOLESALE TYING, BUNDLING, TIERING OBLIGATIONS, AND PRICE DISCRIMINATION - ALL ON A "TAKE IT OR LEAVE IT" BASIS.

ACA's comments, along with those of other smaller distributors, describe a wholesale market rife with "take it or leave it" tying, bundling, tiering obligations and price discrimination.[47] The record also includes descriptions of the wholesale

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[45] *In the Matter of Implementation Review of the Commission's Program Access Rules and Examination of Programming Tying Arrangements*, Report and Order and Notice of Proposed Rulemaking, MB Docket No. 07-198, Comments of the Small Cable System Operators for Change, at 4-5 (filed Jan. 4, 2008) (*"Bend Broadband et al. Comments*").

[46] *See, e.g., In the Matter of Implementation of Section 621(a)(1) of the Cable Communications Policy Act of 1984 as amended by the Cable Communications Policy Act of 1984 as amended by the Cable Television Consumer Protection and Competition Act of 1992*, Report and Order and Further Notice of Proposed Rulemaking, 22 FCC Rcd. 5101, ¶ 4 (2007); *In the Matter of Exclusive Service Contracts for Provision of Video Services in Multiple Dwelling Units and Other Real Estate Developments*, Report and Order and Further Notice of Proposed Rulemaking, 22 FCC Rcd. 22,235, ¶ 1 (2007); *In the Matter of Implementation of Section 224 of the Act; Amendment of the Commission's Rules and Policies Governing Pole Attachments*, Notice of Proposed Rulemaking, 22 FCC Rcd. 20,195, ¶ 36 (2007).

[47] *In the Matter of Implementation Review of the Commission's Program Access Rules and Examination of Programming Tying Arrangements*, Report and Order and Notice of Proposed Rulemaking, MB Docket No. 07-198, Comments of the Rural Iowa Independent Telephone Association, at 3 (filed Jan. 4, 2008) ("Large content providers have been adding increasing amounts of additional programming requiring substantial excess fees."); *NTCA Comments* at 16 ("In order to gain access to the 'must have' programming, programmers typically require MVPDs to pay for additional content for which there is limited or no demand and put it on a basic tier of service. Despite programmer assertions to the contrary, the contracts are offered on a "take it or leave it" basis, leaving MVPDs with no viable alternative."); *OPASTCO et al. Comments* at 9 ("'[C]arriage negotiation' in today's marketplace for small MVPDs is largely a misnomer. Oftentimes there are no negotiations to speak of for these providers."); *Bend Broadband et al Comments* at 2 ("The Small Cable System Operators increasingly face 'take-it-or-leave-it'

marketplace by programmers and broadcasters. Programmers and broadcasters describe a sanguine world of flexibility and accommodation,[48] where "must-have" programming does not exist,[49] and even it if did, programmers would not leverage it,[50] all because programmers and broadcasters do not have market power.[51] At best, these assertions appear carefully crafted for Commission consumption. More to the point here, for small and medium-sized cable companies, programmers and broadcasters describe a world so attenuated from the reality of actual transactions as to approach fantasy. We encourage the Commission not to be fooled. We again suggest that the Commission require programmers to provide actual contracts, both for large and small distributors, to get behind the rhetoric and see the reality of tying and bundling, distribution obligations and price discrimination.

A few of the assertions of programmers and broadcaster warrant brief responses here.

<u>On the subject of standalone channel offers</u>:

What programmers and broadcasters say:

Channels are routinely offered on a standalone basis at reasonable prices.[52]

What small distributors say:

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programming deals, which feature costly provisions for the tying and bundling of channels."); *ACA Comments* at 5-18.

[48] *In the Matter of Implementation Review of the Commission's Program Access Rules and Examination of Programming Tying Arrangements*, Report and Order and Notice of Proposed Rulemaking, MB Docket No. 07-198, Comments of Viacom, at 11-14 (filed Jan. 4, 2008) ("*Viacom Comments*"); *Disney Comments* at 45; *Fox Comments* at 21-26; *NBC Comments* at 38-42.

[49] *NBC Comments* at 46-50.

[50] *Id.* at 45.

[51] *Disney Comments* at 37-39; *Fox Comments* at 3-4; *NBC Comments* at 42-43.

[52] *Disney Comments* at 44; *Fox Comments* at 21; *NBC Comments* at 36.

From NTCA:

"Stand alone" offers are false alternatives.[53]

From OPASTCO et al.:

"Forced tying arrangements are rampant…impeding consumer choice and broadband deployment."[54]

* * *

"Although in some cases alternatives are allegedly offered, the prices or conditions are so onerous as to leave rural MVPDs no realistic choice but to accept the programmers' pricing and tiering requirements."[55]

From Bend Broadband et al.:

"The simple fact is that these 'stand alone' prices are typically set at unreasonably high levels – often many times the price of the entire tied or bundled price – with no inherent cost justification, thereby effectively forcing carriage of tied and bundled programming."[56]

For smaller distributors, programmers' "standalone" offers are illusory because they are priced at levels that coerce purchase of the bundle.

If programmers believe their standalone channel offers are genuine and reasonably priced, then they should not object to ACA's proposals. ACA's proposals would merely codify what programmers claim they do now.

[53] *NTCA Comments* at 18 ("Those few members who have been able to gather information about 'stand alone' programming report that it would be more expensive to carry just the one desired program than to take the entire group of programs – a 'false alternative.'").

[54] *OPASTCO et al. Comments* at ii.

[55] *Id.* at 10.

[56] *Bend Broadband et al Comments* at 3-4.

On the subject of forcing carriage of channels on the most widely-distributed tiers:

What programmers and broadcasters say:

Wholesale terms do not dictate carriage on tiers at retail.[57] Programmers merely "offer incentives for wider distribution."[58]

What smaller distributors (and Dish Network) say:

From OPASTCO et al.:

"Small MVPDs are routinely left with the choice of paying what the programmers dictate and accepting forced carriage of channels in specified tiers, or lose customers due to lack of must-have content."[59]

From Dish Network:

Contractual obligations to distribute channels on the "most widely distributed package" restrict how packages are sold at retail.[60] Contractual restrictions "affect significantly the flexibility of MVPDs to offer creative and alternative programming packages."[61]

From Bend Broadband et al.:

"The terms of carriage dictated by large programmers often require…carrying a program service in the operator's most widely viewed tier of service…prohibiting carriage of a channel in a different tier…linking retransmission consent to the carriage of other costly programming or placement in a specific tier."[62]

As stated in ACA's comments and as widely corroborated on the record, the wholesale practices of requiring channel distribution on specified tiers or to high

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[57] *NBC Comments* at 7.

[58] *Id.* at 39.

[59] *OPASTCO et al. Comments* at 9.

[60] In the Matter of Implementation Review of the Commission's Program Access Rules and Examination of Programming Tying Arrangements, Report and Order and Notice of Proposed Rulemaking, MB Docket No. 07-198, Comments of the Dish Network at 3 (filed Jan. 4, 2008) ("*Dish Network Comments*").

[61] *Id.* at 14.

[62] *Bend Broadband et al Comments* at 2.

percentages of subscribers leave cable operators little to no flexibility in how they package programming.[63] Contrary to NBC's claim of offering "incentives for wider distribution," ACA members face mandatory distribution obligations as conditions of access. These practices reduce choice and raise costs to consumers.

On the subject of programmers' and broadcasters' "take it or leave it" approach to smaller distributors:

What programmers and broadcasters say:

We never "condition retransmission consent on carriage of additional channels."[64] Smaller operators typically receive a "menu" of consideration options.[65]

What smaller distributors say:

From OPASTCO et al.:

81% of OPASTCO members surveyed report "take it or leave it offers" from programmers and broadcasters.[66]

* * *

"Small MVPDs are routinely left with the choice of paying what the programmers dictate and accepting forced carriage of channels in specified tiers, or lose customers due to lack of must-have content."[67]

From the Digital Policy Institute:

"It is fallacious to call this retransmission consent process 'negotiation.' [Smaller] cable companies are unable to negotiate. Their only option is to accede to the broadcaster's requests or go without the channel."[68]

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[63] *ACA Comments* at 14-17.

[64] *Fox Comments* at 16.

[65] *Disney Comments* at 48-49; *Fox Comments* at 16-18; *NAB Comments* at 18; *NBC Comments* at 37-38.

[66] *OPASTCO et al. Comments* at 10.

[67] *Id.* at 9.

[68] *DPI Report* at 77.

From Bend Broadband et al.:

> Small system operators "increasingly face 'take-it-or-leave it' programming deals, which feature costly provision for the tying and bundling of channels."[69]

On this issue, smaller distributors speak with a single voice – programmers and broadcasters routinely offer programming and retransmission consent terms on a "take it or leave it basis," using market power over must have programming to impose additional carriage obligations at discriminatory prices.

On the subject of market power over must have programming:

What programmers and broadcasters say:

> The concept of "must have" programming is nonsense.[70] The Commission is wrong in considering it.[71] Programmers do not use must have programming as leverage in negotiations.[72]

To these assertions, we think Les Moonves, CEO of broadcaster and programmer CBS, Inc., provides the definitive rebuttal:

> "Try running a cable operation without the Super Bowl, the Grammys, CSI, the Final Four, Survivor, David Letterman."[73]

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[69] *Bend Broadband et al. Comments* at 2.

[70] *NBC Comments*, Exhibit B, Bruce M. Owen, *Wholesale Packaging of Video Programming*, at 2 (filed Jan. 4, 2008) ("*Owen Report*").

[71] *NBC Comments* at 47.

[72] *Owen Report* at 29.

[73] John Higgins, CBS Braces for Cable Showdown, BROADCASTING AND CABLE, Mar. 27, 2006 (emphasis added).

V. ACA'S PROPOSED ADJUSTMENTS TO COMMISSION REGULATIONS ACCOMMODATE PROGRAMMER AND BROADCASTER WORRIES OVER A PROHIBITION ON WHOLESALE BUNDLING.

Programmers and broadcasters present a panoply of objections to a prohibition on wholesale bundling. Their professed concerns range from constitutional issues[74] to Commission jurisdiction questions[75] to public policy.[76] Some programmers even express concern about the potential impact on cable operators and cable customers.[77]

Whatever the merit of these concerns, ACA's proposals fully accommodate them. At bottom, programmers and broadcasters object to a prohibition on bundling. The minor adjustments to Commission regulations proposed by ACA would not restrict bundling. Therefore, by adopting ACA's proposals, the Commission would not implicate programmers and broadcasters objections.

For example, programmers and broadcasters want to be free to offer wholesale channel bundles. Under ACA's proposals, they would remain free to do so. They would simply need to also offer channels on a standalone basis on reasonable prices, terms and conditions. Rather than *restrict* wholesale offerings, ACA's proposals would *expand* them.

In the same vein, many programmers say they already offer channels on a standalone basis.[78] ACA's proposals would simply codify this practice, and give a

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[74] *Disney Comments* at 72-83; *NBC Comments* at 30-32.

[75] *Viacom Comments* at 18, 23-32; *Fox Comments* at 32-38.

[76] *NBC Comments* at 55 ("Commission regulation prohibiting wholesale packaging, retail tiering or both will certainly diminish programming diversity and choice.").

[77] *Id.* at 53 ("[I]f the Commission were to prohibit programmers from negotiating for subscriber levels and/or tier placement in their carriage agreements with MVPDs, programmers, operators and subscribers would all be adversely affected.").

[78] *Viacom Comments* at 2 ("First and foremost, Viacom offers all of its programming networks for sale on a standalone basis").

remedy in case standalone channels were not offered on reasonable terms. As programmers and broadcasters claim they already do this, they should have no legitimate objection to the Commission incorporating this into its regulations.

ACA's proposals do go a step further and would constrain the wholesale practice of conditioning access to a channel to specific tiering or distribution obligations.[79] At the same time, ACA's proposals would not restrict programmers from offering incentives for wider distribution. Professor Owens states that programmers currently do offer incentives for wider distribution of programming.[80] Here too, ACA's proposals would merely codify what programmers claim is their current practice, along with providing a remedy in cases where a programmer unreasonably restricts the ability to offer programming on a tier of the operator's choice.

VI. THE RECORD SHOWS THE CLEAR NEED FOR A STANDSTILL PROVISION IN COMPLAINT PROCEEDINGS, ESPECIALLY THOSE INVOLVING SMALLER MVPDS.

ACA's proposals include revising the program access and retransmission consent complaint procedures to include a standstill provision.[81] This would codify the conditions from the *News Corp. Order* that have worked effectively to bring a measure of balance to negotiations with a powerful broadcaster and programmer. Without a right of carriage during a complaint proceeding, the threat of withdrawal of a must-have channel overwhelmingly skews negotiations in favor of the broadcaster and programmer, eviscerating the utility of the complaint process.

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[79] *ACA Comments* at 22, 25.

[80] *Owen Report* at 37.

[81] *ACA Comments* at 23-24, 26.

The record contains widespread support for this adjustment to Commission regulations, especially in cases involving small and medium-sized distributions. As stated by OPATSCO et al., "[t]emporary foreclosure may impair settlement negotiations and discourages parties from filing complaints…The Commission should implement a 'standstill' requirement in order to protect customers and MVPDs from the anticompetitive actions of programmers."[82] NTCA and Verizon similarly support the standstill approach to complaint resolution.[83] As stated by Dish Network, "[t]emporary foreclosure is almost as damaging as an outright refusal to deal."[84] As described by a small cable operator, Liberty Cablevision of Puerto Rico, only with a standstill provision would it be able to justify "the administrative burdens and costs of a contested case before the Commission."[85] Otherwise, it would still "be faced with the threat of losing local broadcast signals."[86]

It is axiomatic that there is no genuine right without a remedy.[87] And without a standstill provision, the Commission program access and retransmission consent

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[82] *OPASTCO Comments* at 17-18.

[83] *In the Matter of Implementation Review of the Commission's Program Access Rules and Examination of Programming Tying Arrangements*, Report and Order and Notice of Proposed Rulemaking, MB Docket No. 07-198, Comments of Verizon, at 15 (filed Jan. 4, 2008) ("A standstill requirements would ensure that the customers being served by the MVPD alleging a violation of the program access rules can continue to enjoy the programming they are currently receiving while the Commission considers the merits of the provider's allegations."); *NTCA Comments* at 34 ("The Commission should adopt a procedure similar to the 'standstill' in Appendix B(2)(c) of the *Adelphia Order*.").

[84] *Dish Network Comments* at 5.

[85] *Liberty Cablevision Comments* at 3.

[86] *Id.* at 2.

[87] *See, e.g.*, *Franklin v. Gwinnett County Public Schools*, 503 U.S. 60, 66, 112 S.Ct. 1028, 1033 (U.S.Ga., 1992), *citing Marbury v. Madison*, 5 U.S. 137, 163 (1803) ("[Our Government] has been emphatically termed a government of laws, and not of men. It will certainly cease to deserve this high appellation, if the laws furnish no remedy for the violation of a vested legal right.").

complaint processes do not offer a realistic remedy, at least for small and medium-sized cable companies.

VII. THE RECORD VALIDATES THAT THE COMMISSION HAS AUTHORITY TO ADOPT THE REGULATIONS PROPOSED BY ACA.

ACA's requested relief is very limited. ACA does <u>not</u> advocate a prohibition on tying and bundling – ACA advocates only that broadcasters and programmers be required to offer standalone channels on reasonable rates, terms and conditions, and that the Commission prohibit non-cost-based price discrimination. ACA does not ask for a ban on tiering and penetration provisions – it asks only that programmers be required to provide reasonably-priced alternatives. Similarly, ACA's recommended adjustments to the retransmission complaint process are finely-honed. Comments arguing that the Commission does not have the authority to preclude bundling are inapposite.[88] ACA does not request so extensive a remedy.

As shown in ACA's comments, the Commission has ample authority to adopt the limited revisions to the Commission's regulations that ACA proposes.[89] The record in this proceeding confirms the Commission's authority.[90]

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[88] *See, e.g.*, *Disney Comments* at 4-16.

[89] *ACA Comments* at Appendix 2.

[90] *See, e.g., NTCA Comments* at 19; *Dish Network Comments* at 18-20; *AT&T Comments* at 11-13; *Broadband Service Providers Association Comments* at 7-8, 14-15.

VIII. CONCLUSION

The Commission has before it ample evidence that current wholesale programming and retransmission consent practices result in substantial public interest harms. The adjustments to Commission regulations proposed by ACA would ameliorate those harms in a restrained and narrowly-tailored way, and the Commission should adopt them.

Respectfully submitted,

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APPENDIX 1

The Economic Effects of Price Discrimination in Retransmission Consent Agreements, William P. Rogerson, Professor of Economics, Northwestern University

Before the
Federal Communications Commission
Washington, DC 20554

In the Matter of	)	
	)	
Review of the Commissions' Program	)	MB Docket 07-198
Access Rules and Examination of	)	
Program Tying Arrangements	)	

THE ECONOMIC EFFECTS OF PRICE DISCRIMINATION IN RETRANSMISSION CONSENT AGREEMENTS

by

William P. Rogerson
Professor of Economics
Northwestern University

February 12, 2008

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INTRODUCTION AND SUMMARY

The retransmission consent framework put into place by the 1992 Cable Act[1] allows broadcasters to negotiate compensation from MVPDs in return for providing them with permission to broadcast their signals. Current regulations do not require broadcasters to make their signals available on the same terms to all MVPDs in their broadcast area and there is considerable evidence that broadcasters do, in fact, engage in extensive amounts of price discrimination. In particular, it appears that small and medium-size MVPDs are often required to pay fees that are at least four to five times as high as the fees that large MVPDs pay for permission to retransmit exactly the same broadcast signal. The American Cable Association (ACA) has asked me to provide an analysis of the economic causes and consequences of these discriminatory practices. In particular, they have asked me to consider if the case can be made that allowing such discriminatory practices could potentially result in economic efficiencies of some sort or whether the main effect of these practices is simply that different groups of subscribers are essentially being charged different prices to view the same programming. I have also been asked to consider the feasibility and cost of implementing regulations designed to restrict such discriminatory practices.

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[1]Cable Television Consumer Protection and Competition Act of 1992,PUb. L. No. 102-385, 106 Stat. 1460. *See also* 47 C.F.R. 76.64. This original act applies only to cable system operators. In 1999 Congress enacted the Satellite Home Viewer Improvement Act, Pub. L. NO. 106-113, 114 Stat. 1501, which allows DBS companies to offer local broadcast channels to their subscribers and allows broadcasters to negotiate compensation for providing them with retransmission consent. *See also,* Satellite Home Viewer Extension Reauthorization Act ("SHVERA"), Pub. L. No. 108-447, 118 Stat. 2809 (2004).

My main conclusions are as follows:

1. The main economic cause of price discrimination in retransmission consent agreements is simply that small and medium-size MVPDs are in a considerably worse bargaining position than their larger brethren, because the share of the audience they provide to a typical broadcast station is small enough that the loss of this audience will not generally have any significant impact on the station's advertising revenue.

2. In some markets, price discrimination can have the desirable effect that it provides firms with the incentive and ability to serve more customers by allowing to them to simultaneously serve customers with a low ability/willingness to pay for the good at low prices while still serving customers with a higher ability/willingness to pay for the good at higher prices. No such rationale applies in the case of retransmission consent. Obviously, local broadcasters would still provide their signals to the major MVPDs if they were not allowed to charge even higher prices to small and medium-size MVPDs. Therefore the main effect of price discrimination in this case, is simply to allow broadcasters to charge higher prices to MVPDs with less bargaining power.

3. Higher retransmission consent fees are ultimately paid for by the subscribers to MVPDs in the form of higher subscription fees.

4. While there may be a good public policy rationale to require MVPD subscribers to make

modest payments that help support the programming efforts of local broadcasters, the rationale for requiring the customers of small and medium-size MVPDs to make higher payments than the customers of large MVPDs is much less apparent. The government has granted commercial broadcasters with valuable spectrum and provides a range of legal and regulatory protections to help ensure the availability of broadcast television to the public. The use of some of those legal and regulatory protections to extract substantially higher fees from smaller distributors and their customers raises policy questions that the Commission should carefully consider. I think that the Commission should carefully consider whether adjustments to regulations that would spread this burden more equally across all MVPD subscribers would be more consistent with the Commission's public policy objectives.

5. Since retransmission consent fees are projected to continue to rise rapidly, the inequities generated by these discriminatory practices will continue to grow.

6. The current program access regulations provide a model showing how the Commission could implement non-discrimination requirements for retransmission consent fees in a relatively simple and workable fashion

The paper is organized as follows. A brief summary of my qualifications follows this introduction. Then Section 1 describes the factors that affect the bargaining power between MVPDs and broadcasters and explains why smaller MVPDs have considerably less bargaining power than do larger MVPDs. Section 2 very briefly reviews some of the evidence that small and medium-size MVPDs do, in fact, pay significantly higher retransmission consent fees than larger MVPDs. Section 3 considers the possibility that allowing this price discrimination might somehow enhance economic efficiency and concludes that the normal economic reason why we might expect price discrimination to be efficiency-enhancing in some circumstances does not apply in this case. Section 4 concludes that the main economic effect of allowing price discrimination in this case is simply that different viewers are charged different prices to view the same programming. It also suggests that Commission should carefully consider whether this outcome is consistent with its own policy objectives. Section 5 briefly describes the manner in which current program access regulations prohibit price discrimination by vertically integrated cable programmers and suggests that the same approach could be used to implement nondiscrimination requirements for retransmission consent fees. Finally Section 6 draws a brief conclusion.

QUALIFICATIONS

My name is William P. Rogerson. I am a Professor of Economics at Northwestern University. In 1998-99 I served as Chief Economist at the Federal Communications Commission ("Commission"). I have published numerous academic articles on industrial organization, regulation, the economics of contracts, and telecommunications and I am an elected fellow of the Econometric Society. I have served as Chairman of the Department of Economics at Northwestern University and am currently Co-Director of Center for the Study of Industrial Organization and Director of the Program in Mathematical Methods in the Social Sciences at

Northwestern. I am also a Senior Fellow at the Searle Center on Law, Regulation, and Economic Growth at Northwestern and Director of the Searle Research Program on Regulation and Antitrust. Since my term as Chief Economist at the Commission, I have served as an economic expert to both government agencies and private parties on a number of regulatory issues involving the multi-channel video programming and delivery (MVPD) industry. This includes serving as the economic expert for the Federal Trade Commission in its review of the Time Warner AOL merger and serving as the economic expert for the Association of State Attorney Generals to support their analysis of the DirecTV EchoStar merger. A copy of my curriculum vitae is appended to this paper.

1. SMALL AND MEDIUM-SIZE MVPDS HAVE CONSIDERABLY LESS BARGAINING POWER THAN LARGE MVPDS

The negotiating strength between a local broadcaster and an MVPD is affected by the relative harm that each party would suffer if the MVPD were not to carry the signal of the local broadcaster. The potential harm to the broadcaster is that its viewership would decline and that this would have a negative impact on its ability to earn advertising revenues. The potential harm to the MVPD is that it would have less desirable programming and that it would therefore lose customers to other MVPDs that still carry the signal and/or that it would have to lower its subscription prices to retain customers.

There is widespread agreement among industry participants, policy-makers, and economists and financial analysts that study this industry that the relative balance of negotiating strength between a local broadcaster and MVPD is dramatically different in the case of most small and medium-size MVPDs than it is in the case of the largest cable system operators or the two large DBS providers. This is primarily because the potential harm that a broadcaster will suffer if the MVPD does not retransmit its signal is dramatically different in each case. In particular, a local broadcaster will typically face the situation where the vast majority of its customer base is located in more urban areas served by one or two very large cable systems and a much smaller faction of its customer base is located is less developed areas typically served by a much larger number of small cable systems. Of course, the two major DBS providers, DirecTV and Echostar, will also generally make their services available throughout the viewing area. As a result, when a local broadcaster calculates the share of its viewers that subscribe to the various MVPDs that serve its viewing area, it finds that one or two large cable systems typically provide service to the vast majority of its viewers, that the two DBS firms provide service to a smaller but still significant proportion of its viewers and that the share of its viewers that subscribe to any other MVPD is almost too minuscule to calculate. Losing carriage on one of the major cable systems would therefore represent a major loss of viewers for the broadcaster that would likely have immediate and severe repercussions for its advertising revenues. Losing carriage on one of the two DBS providers would create a smaller but still significant revenue loss for the broadcaster. However, losing carriage on a small cable system would not necessarily even be an event that most advertisers would notice.

A recent report by the Congressional Research Service[2] describes the negotiating environment between local broadcasters and MPVDs and its effect on the levels of compensation

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[2]Goldfarb, Charles B. *Retransmission Consent and Other Federal Rules Affecting Programmer-Distributor Negotiations: Issues for Congress,* Congressional Research Services Report for Congress, July 9, 2007 (“CRS Report”).

that broadcasters are able to negotiate with different types of MPVDs in great detail and provides a much more detailed and in-depth picture of the situation than I am able to do in this short paper. I recommend that the interested reader consult this report directly. However I will extract a few particularly relevant quotations from this report. The report contrasts the situation between small and medium-size cable companies versus the major DBS providers as follows.

> "Small and mid-size cable companies often face direct competition from the two major satellite companies, DirecTV and DISH Network. These cable companies have fewer subscribers than the major satellite companies and thus when negotiating with programmers typically do not pose a serious risk to the programmers if there is an impasse and the programming is not carried; a programmer's forgone per subscriber fees from these cable companies and foregone advertising revenues would not be substantial. By contrast, a programmer's revenues could be significantly reduced if one of the satellite companies discontinued carriage, since each of the satellite carriers have more than 13 million subscribers. [footnote omitted] Moreover, many of the smaller cable companies have limited or no ability to offer bundled video/telephone/broadband services that tend to foster customer retention even when favored programming is no longer carried. Thus, if an impasse were to occur, a smaller cable company would face significant risk of losing subscribers to satellite companies. In fact, where a smaller cable company has had an impasse with a programmer, sometimes the programmer – or a satellite operator that has an agreement with the programmer and is competing with the cable company – has offered a "bounty" of upwards of $200 to households to switch to the satellite service, with these offers marketed over the programmer's network while the programmer-cable company negotiations are still on-going. [footnote omitted]"[3]

It also points out that large cable operators are in an even stronger negotiating position than the DBS providers.

> "The very large cable companies appear to have been more successful than the two large satellite companies in resisting cash payments, for several reasons. Their strategy to cluster their systems in a limited number of local markets has given them high subscriber penetration in those markets, which helps in negotiations with local broadcast stations. Also, their ability to offer bundles of video, voice, and data services reduces the likelihood that subscribers will change provider based solely on the loss of a particular

[3] CRS Report at 12.

video program." [4]

Analysts that follow this industry and industry publications routinely note the same factors. For example the New York Times quotes Sanford Berstein analyst Craig Moffet as stating:

> "it is one thing to wring big fees out of small cable operators, but if CBS goes dark on Comcast, CBS's distribution would plummet overnight. Comcast may end up paying something , but it is hard to see how it is all that material."[5]

The industry publication MultiChannel News reports the same analyst as stating that

> "two trends are clear from 2007: retrans generates cash and smaller operators, with less leverage than larger cable companies, will bear the brunt of the pain." [6]

2. SMALL AND MEDIUM-SIZE MVPDS PAY SIGNIFICANTLY HIGHER RETRANSMISSION CONSENT FEES THAN LARGE MVPDS

The almost universal use of non-disclosure clauses in retransmission consent agreements limits the amount of publicly available evidence on the magnitude of retransmission consent fees and how they vary between MVPDs of different sizes. However, the available evidence, which consists largely of media reports and analyst reports, consistently and uniformly suggests that the independently owned affiliates of the four major broadcast networks and the owned and operated affiliates of CBS[7] are now charging fees in the neighborhood of $.50 per subscriber per month to

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[4]CRS Report at 13

[5]See *Slow and Steady No More*, New York Times, October 19, 2007.

[6]See *Retrans on the Rise*, Multichannel News, January 7, 2008.

[7]The situation is more complicated for the owned and operated(O&O) affiliates of NBC, ABC, and Fox. These networks all produce significant amounts of their own cable network

small and medium-size MVPDs and $.10 to $.15 per subscriber per month to the two major DBS providers. Exact figures for the fees that the largest cable operators are paying are more difficult to come by but there is a strong consensus that the fees are certainly no higher than those paid by the DBS providers and may, in fact, be substantially lower.

Some of this evidence has actually been presented in the record of this proceeding in an economic expert report filed by Disney, which is, of course, the owner of one of the four major networks, ABC.[8]   Citing a report by Bernstein Research[9] the Disney expert report states that

> "Although some of the smaller cable operators may be paying cash for retransmission rights, the major cable operators have resisted such initiatives[cite to Bernstein Report]. In contrast, satellite operators are already paying cash for retransmission consent, on the order of $0.10 to $0.15 per subscriber per month[cite to Berstein Report]."[10]

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programming and the retransmission consent deals they negotiate with MVPDs on behalf of their O&O's tend to be negotiated as part of larger packages where the MVPDs agree to purchase various cable networks at specified prices. In these cases one would have to calculate the implicit premium that small and medium-size MVPDs are paying for retransmission consent by comparing the prices of the over-all packages of programming that the MVPDs purchase, and I am not aware of any news reports that have attempted to conduct this more involved sort of calculation.

[8]See "Economic Implications of Bundling in the Market for Network Programming," by Jeffrey Eisenach, January 4, 2008, ("Disney Expert Report")submitted by The Walt Disney Company as part of "Coments of the Walt Disney Company," *MB Docket No.07-29, MBDocket No. 01-198,* January 4, 2008.

[9]Berstein Research, *U.S. Media: Cash for Retrans A net Poitive for TV Stations, But Full Financial Benenfit Will Likely Require Large Patience*, Mar. 2006, ("Berstein Report").

[10]See Disney Expert Report at

Numerous news stories by major national newspapers as well as industry publications report retransmission consent fees paid by smaller cable operators in the range of $.30 to $.50.[11] The ACA and other representatives of smaller MVPDs report that many of their members are now charged between $.50 and $1.00 per subscriber per month in retransmission consent fees for each of the four major networks. The ACA also reports that one of their members recently received a rate card seeking $1.65 per subscriber per month as the retransmission consent fee for an affiliate of the one of the major four networks.

As I mentioned above, virtually all retransmission consent agreements contain non-disclosure clauses that prohibit MVPDs from disclosing the terms of these agreements. I think that if the FCC determines that it needs more information about the magnitude and extent of price discrimination before it takes any action on this issue, that it could and should require broadcasters to make systematic information available on the terms of the retransmission agreements that they negotiated with different MVPDs.

It is also worth noting that retransmission consent fees have been rising dramatically over the last few years and that most industry participants and observers are projecting that they will

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[11] *See Channel Change - Television's Power Shift: Cable Pays for Free Shows; Broadcasters Want Cash to Carry Their Signal; Super Bowl is Hostage*, Wall Street Journal, February 5, 2007, page A1 (reporting that Sinclair Broadcasting was asking for retransmission consent fees of $.50 per subscriber per month from cable operator Suddenlink and that it likely got close to what it was asking for); *Commisso: 'Industry Has Major Issues,* Multichannel News, February 5, 2007 ("Mediacom may have agreed to pay as much as 50 cents per subscriber per month for each of clair's stations according to one party close to the company. The Wall Street Journal Monday put the payments in the range of 30-50 cents."); *CBS Reaches Deals With 9 Cable operators for Compensation to Carry its Programs*, New York Times February 23, 2007 ("[Mr. Moonves] previously predicted at investor conferences that CBS could gain 50 cents a subscriber from these agreements. That amount was widely speculated to be exactly what CBS did secure from at least some of the nine systems involved.")

continue to rise rapidly over the next few years. For example, Kagan research is reported to have projected that retransmission consent revenues will rise from their current level of $230 million per year to a level of $1 billion per year in 2010.[12] Thus, the financial significance of retransmission consent fees to both MVPDs and their customers is going to continue to grow in importance over the next few years.

3. ALLOWING PRICE DISCRIMINATION IN RETRANSMISSION CONSENT AGREEMENTS DOES NOT EXPAND THE MARKET

In some markets, price discrimination can have the desirable effect that it provides firms with the incentive and ability to serve more customers by allowing to them to simultaneously serve customers with a low ability/willingness to pay for the good at low prices while still serving customers with a higher ability/willingness to pay for the good at higher prices. No such rationale applies in the case of retransmission consent. Obviously, local broadcasters would still provide their signals to the major MVPDs if they were not allowed to charge even higher prices to small and medium-size MVPDs. Therefore the main effect of price discrimination in this case, is simply to allow broadcasters to charge higher prices to MVPDs with less bargaining power.

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[12]See *Dueling for Dollars,* Multichannel News, March 5, 2007.

4. THE MAIN ECONOMIC EFFECT OF ALLOWING PRICE DISCRIMINATION IN RETRANSMISSION CONSENT AGREEMENTS IS THAT DIFFERENT GROUPS OF VIEWERS ARE BEING CHARGED DIFFERENT PRICES TO VIEW THE SAME PROGRAMMING

MVPDs pass higher programming costs back to their subscribers in the form of higher subscription fees. Therefore the main effect of price discrimination in retransmission consent agreements is simply that different groups of viewers are being charged different prices to view the same programming.

In a sense, the retransmission consent regime essentially allows local broadcasters to indirectly charge MVPD subscribers a fee for the right to view local broadcasts' signals through their MVPD provider, even though the same signals are provided free over the air. The goal of policy makers when they instituted this policy was to strengthen the financial viability of local broadcasters and to provide them with both the incentive and financial resources to increase the quality of their programming. While there may be a good public policy rationale to require MVPD subscribers to make modest payments that help support the programming efforts of local broadcasters, the rationale for requiring the customers of small and medium-size MVPDs to make higher payments than the customers of large MVPDs is much less apparent. I think that the Commission should carefully consider whether adjustments to regulations that would spread this burden more equally across all MVPD subscribers would be more consistent with the Commission's public policy objectives.

The government has granted commercial broadcasters with valuable spectrum and provides a range of legal and regulatory protections to help ensure the availability of broadcast television to the public. The use of some of those legal and regulatory protections to extract substantially higher fees from smaller distributors and their customers raises policy questions that the Commission should carefully consider.

5. PROGRAM ACCESS REGULATIONS PROVIDE A WORKABLE MODEL FOR IMPLEMENTING REGULATIONS THAT WOULD RESTRICT PRICE DISCRIMINATION IN RETRANSMISSION CONSENT AGREEMENTS

A potential difficulty in implementing regulations that would restrict the ability of broadcasters to price discriminate in their retransmission consent agreements is that the agreements in many cases involve more complex terms that a simple cash payment. In particular, as mentioned above, many of the retransmission consent agreements negotiated by the major networks on behalf of their owned and operated affiliates require the MVPDs to carry additional cable network programming produced by the network in return for receiving retransmission consent. If all compensation took the form of stand-alone cash payments, price discrimination could be prevented simply by requiring all broadcasters to publish a rate card which made the same prices available to all MVPDs. Such a requirement would be very simple and easy to enforce. However, because retransmission consent contracts are often more complex, a no-discrimination requirement would have to be implemented by the more general requirement that broadcasters would have to make the same terms available to all MVPDs. This more complex requirement would obviously be somewhat more difficult to verify and enforce.

However, the current program access regulations already provide a model showing that it is possible for the Commission to implement this more complex sort of regulatory requirement in a relatively workable and simple fashion. In particular, the current program access regulations require cable network programers that are vertically integrated with a cable system to make their programing available to non-affiliated MVPDS at the same terms and conditions that it is made available to their own affiliated cable systems. The regulation is enforced by allowing aggrieved parties to file complaints with the Commission that are then investigated. The threat that complaints can be filed, and that the subsequent investigation would be costly and time consuming for all involved parties, then provides programmers with some incentive to avoid violations of the rules in the first place. While this system undoubtedly does not work perfectly, I note that the Commission has been satisfied enough with its performance to renew these regulations a number of times.

6. CONCLUSION

There is considerable evidence that small and medium-size MPVDs are charged significantly higher fees for retransmission consent than large MVPDs are charged. The primary explanation for this is simply that small and medium-size MVPDs have considerably less bargaining power in their negotiations with broadcasters. Higher retransmission consent fees are passed through to subscribers in the form of higher subscription fees. The government has granted commercial broadcasters with valuable spectrum and provides a range of legal and regulatory protections to help ensure the availability of broadcast television to the public. The use of some of those legal and regulatory protections to extract substantially higher fees from smaller distributors and their customers raises policy questions that the Commission should carefully consider.

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1990 - Present	Professor of Economics, Northwestern University
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1998-1999	Chief Economist, Federal Communications Commission (while on leave from Northwestern)
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1984-1990	Associate Professor of Economics, Northwestern University
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HONORS, AWARDS, RESEARCH GRANTS

Keynote Speaker at European Institute for Advanced Studies in Management (EIASM) Workshop on Accounting and Economics, Bergen, Norway, June 22-23, 2006.

Searle Fund For Policy Research, Research Grant, “Regulation of Interconnection Between Telecommunications Carriers in the Emerging Competitive Environment,” June 2002-May 2004.

Elected Fellow of the Econometric Society, 1999.

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NSF Grant SES-8906751, "Profit Regulation of Defense Contractors," August 1, 1989 - July 31, 1991.

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Named to Household International Professorship in Economics, September 1987 - August 1989

NSF Grant IRI-8705477, "Contracting Under Asymmetric Information," July 1987 - December 1989

NSF Grant SES-8504304, "Moral Hazard, Reputation, and Product Quality," April 1985 - September 1987

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Shelby Cullom Davis Fellowship, 1979

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Co-Editor, *Economic Inquiry*, October 2007- present.

Research Director of Program on Competition, Anti-Trust and Regulation, Searle Center on Law, Regulation, and Economic Growth, Northwestern University, September 2007- present.

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Chair of Northwestern's Program Review Committee, September 2002 - June 2003.

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Member of Editorial Board, *Review of Accounting Studies*, September 1993 to December 2003.

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Member of the Editorial Board, *Journal of Industrial Economics*, October 1995- Sept. 1998.

Editor, *Defense and Peace Economics*, January 1995 - December 1998.

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“On the Relationship Between Historic Cost, Forward-Looking Cost, and Long Run Marginal Cost, October 2005.

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