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

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| In the Matter of | ) | |
| | ) | |
| The Commission's Cable Horizontal and Vertical Ownership Limits | ) | MM Docket No. 92-264 |
| | ) | |
| Implementation of Section 11 of the Cable Television Consumer Protection and Competition Act of 1992 | ) | CS Docket No. 98-82 |
| | ) | |
| Review of the Commission's Regulations Governing Attribution of Broadcast and Cable/MDS Interests | ) | MM Docket No. 94-150 |
| | ) | |

**REPLY COMMENTS OF VERIZON ON FURTHER NOTICE**


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April 14, 2008

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**REPLY COMMENTS OF VERIZON[1] ON FURTHER NOTICE[2]**

**INTRODUCTION AND SUMMARY**

The Commission should not impose channel occupancy limits or other unnecessary regulation in any area where two or more wireline video providers compete to provide video service, and certainly not in the case of new entrants in the video marketplace.

As a general matter, in all segments of the communications marketplace, the Commission should continue to rely on competition, rather than regulation, whenever possible. And where competition is present, regulation generally should go away. Competitive markets consistently prove themselves superior to regulatory fiat in fostering investment and innovation and in protecting consumers' interests and serving their needs.

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1 The Verizon companies participating in this filing ("Verizon") are the regulated, wholly owned subsidiaries of Verizon Communications Inc.

2 Fourth Report & Order and Further Notice of Proposed Rulemaking, *The Commission's Cable Horizontal and Vertical Ownership Limits; et al.*, 23 FCC Rcd 2134 (2008) ("*Further Notice*")

These observations are particularly true in the video marketplace where many regulations – including those being considered in this proceeding – infringe on a provider's constitutional rights to engage in protected speech. Channel occupancy limits – which limit the number of "affiliated" channels that a provider may carry – directly infringe on a provider's First Amendment rights. Such speech regulations have traditionally been justified on the basis that the cable incumbents historically had bottleneck monopolies that gave them control over the programming the consumers could access. But where that bottleneck no longer exists, the justification for speech-infringing regulation also goes away. Indeed, for precisely this reason the D.C. Circuit rejected the Commission's earlier vertical ownership rules that failed to carve out providers in areas with effective competition because those rules burdened substantially more speech than was necessary.

To be sure, there remain situations in which the cable incumbents have used their historic monopoly to try to foreclose access by competing providers, whether by locking up access to key programming or to multiple dwelling unit properties, and where regulatory action is still warranted. But the justification for other regulations such as the ones at issue here is lacking in areas where wireline competition has actually developed, particularly with respect to the new entrants who never possessed bottleneck control in the first place.

The case for removing regulations where video competition exists, however, applies fully in the context of the rules being considered here. As the Commission has recognized, the trends in the video marketplace are towards increased video competition and decreased vertical integration. Faced with competition, all providers have a strong incentive to provide the desirable programming that consumers want, whether or not that programming is affiliated with the (or any) video provider. Otherwise, their competitors will do so, and they will lose out in the marketplace.

## ARGUMENT

### I. Competition Serves Consumers Better Than Regulation and Removes Any Need for Channel Occupancy Limits.

As a general matter throughout the communications marketplace, where competition is present, regulation is unnecessary and usually affirmatively harmful to consumers. Regulation – and especially rules such as those under consideration that restrict the way a provider offers its services – is warranted only in clear cases of demonstrated market failure, and, even then, only when the benefits of government intervention outweigh the costs. When those conditions are absent, directing markets is a job best left to competitive forces, which consistently prove themselves better than regulators at maximizing consumer welfare. In dynamic industries that are undergoing rapid technological change – like most parts of the communications marketplace today including for video services – it is particularly difficult for even the most capable regulator to keep up with the market's evolution.[3]

For the same reasons, even if regulation may at one time have been necessary to protect consumers, after competition develops such regulation generally should go away. Regulation that has outlived its usefulness distorts competition, inhibits innovation and investment, and prevents competitive providers from more efficiently serving consumers.[4]

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[3] *See* Stephen Breyer, *Regulation and Its Reform* 286-87 (1982) ("[B]ecause regulation, once in place, is hard to dismantle, one would like to know whether future technological change is likely to transform an industry that is now a natural monopoly, making it structurally suited to competition."); Alfred E. Kahn, *The Economics of Regulation* 127 (1971) ("In the presence of such rapid change, the natural monopoly of yesterday may be transformed into a natural arena of competition today; and vice versa.").

[4] *See* Howard A. Shelanski, *Adjusting Regulation to Compertition: Toward a New Model for U.S. Telecommunications Policy*, 24 Yale J. on Regulation 55, 77 (2007) ("the benefits of regulation diminish as markets become competitive, while the costs of regulation remain and even increase as that transition occurs").

In light of these fundamental principles, regulations must be tightly cabined to reach no further than is justified, and they should go away where competition makes them unnecessary. Given the trends in the video marketplace towards more competition and away from vertical integration, any new channel occupancy (or other vertical ownership) rules are unnecessary and unwarranted as a general matter, and this is all the more true in any areas where wireline competition now exists and in the case of competitive providers who have never had bottleneck control.

The video marketplace is a good example of the benefits that flow to consumers where competition exists. Where competition exists, competing providers have every incentive to carry high-quality and diverse sources of information in order to differentiate themselves from, and better compete against, their competitors. And this is particularly true of new wireline entrants who must compete against entrenched, vertically-integrated incumbents, as well as other increasingly significant sources of video programming such as the Internet. Competitive providers must assemble attractive offerings that give consumers the programming that they want, without regard to regulatory mandate or the affiliation of the programming.

This is borne out by the channel line-ups of competitive wireline providers, which reveal the clear benefits to, and opportunities for, independent programmers as a result of new entry and wireline competition in the video marketplace. From the beginning and without regulatory compulsion, Verizon has negotiated carriage deals with numerous independent programmers such as The America Channel, the NFL Network, and the Hallmark Channel, in addition to a wide range of international and other niche programmers for its FiOS TV service. Likewise, FiOS TV includes several low power television stations, more than twenty channels of Spanish language programming, several international channels like TV Japan and TVP Polonia, religious programming like The Word Network, and a broad range of niche programming that consumers desire, like Blackbelt TV for martial arts enthusiasts.[5] The advanced broadband networks being deployed by many competitive providers also allow them to continue to expand their offerings to include new and diverse channels and to carry a significant amount of high-definition programming. The Commission itself recently recognized the "pro-competitive trends" in the video marketplace including "an increase in programming networks" and "a decrease in the percentage of popular national and regional networks that are affiliated with cable operators."[6]

Providers carry this increasingly diverse array of programming not because regulations require them to, but because competition and consumer demands leave them no choice. Regulations – and particularly regulations that could restrict competitive providers' ability to provide consumers with the programming that they demand regardless of the affiliation of that programming – will inhibit this healthy dynamic and could well have precisely the opposite effect. The competitive free-for-all that is shaping up between incumbent cable operators, satellite providers, online video providers, and new wireline entrants will further these pro-competitive trends and continue to increase the availability of more diverse information sources and other consumer benefits, as long as ill-fitting regulations do not get in the way.

The pro-competitive trends in the video marketplace – including more wireline competition and less vertical integration by providers that historically have had bottleneck control over access to consumers – undermine the case for adopting *any* new rules and that is all the more true in areas with two or more wireline competitors.

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[5] *See e.g.*, Verizon FiOS TV Washington Metro Channel Lineup, http://www22.verizon.com/NROneRetail/NR/rdonlyres/6D56A468-CDA3-47A8-99DE-6F10E620D7A6/0/VA_WashingtonMetro.pdf.

[6] Report and Order and Notice of Proposed Rulemaking, *Implementation of the Cable Television Consumer Protection Act of 1991; Development of Competition and Diversity in Video Programming Distribution: Section 628(c)(5) of the Communications Act: Sunset of Exclusive Contract Prohibition; Review of the Commission's Program Access Rules and Examination of Programming Tying Arrangements*, 22 FCC Rcd 17791, ¶ 16 (2007) ("*Report and Order*").

## II. At a Minimum, the First Amendment Prohibits Application of Channel Occupancy Limits in Competitive Areas and to New Entrants.

Avoiding unnecessary regulation is all the more important in the context of rules, such as those at issue here, which directly infringe on providers' First Amendment rights. To the extent courts have sustained such regulations in the past, they have done so only because of cable incumbents' historical bottleneck monopoly over access to consumers. Where two or more wireline video providers compete in an area, however, there is no such bottleneck control and no legitimate basis for regulations such as those at issue here directly infringing on protected speech. As the D.C. Circuit has previously held, channel occupancy rules that fail to take into account the presence of competition unreasonably burden speech and fail to pass First Amendment scrutiny.

As an initial matter, it is well established that the First Amendment protects video providers' right to offer video programming services. *Turner Broad. Sys. v. FCC*, 512 U.S. 622, 636 (1994) ("*Turner I*"); *City of Los Angeles v. Preferred Commc'ns., Inc.*, 476 U.S. 488, 494 (1986). Video providers express speech not only through their original programming but also through their editorial decisions over which stations and programs to disseminate. As the Supreme Court has observed, cable providers "communicate messages on a wide variety of topics and in a wide variety of formats," and are thus "entitled to the protection of the speech and press provisions of the First Amendment." *Turner I* at 636. The D.C. Circuit has recognized that ownership limits, like the channel occupancy limits being considered by the Commission in this proceeding, directly infringe on a provider's speech and must be tested against the First Amendment. *Time Warner Entm't Co., L.P. v. FCC*, 240 F.3d 1126, 1129 (D.C. Cir. 2001) ("*Time Warner II*"); *see also Time Warner Entm't Co., L.P., v. FCC*, 211 F.3d 1313 (D.C. Cir. 2000) ("*Time Warner I*").

To the extent courts have upheld regulations that infringe on video providers' speech, they have done so because of the bottleneck monopolies historically held by the cable incumbents. For example, the Supreme Court in *Turner I* emphasized the "special characteristics of the cable medium:  the bottleneck monopoly power exercised by cable operators and the dangers this power poses to the viability of broadcast television." *Id.* at 661.  And the Court noted the "potential for abuse of this private power over a central avenue of communication" held by a cable operator with "bottleneck, or gatekeeper, control." *Id.* at 656-57.

Likewise, in the context of a facial attack on the statutory provision addressing ownership limits in *Time Warner I*, the D.C. Circuit again was heavily influenced by the existence of bottleneck monopoly control.  In that case, Time Warner argued that channel occupancy limits are akin to "a law prohibiting newspapers from devoting more than a fraction of their columns to editorial content of their own," and have the effect of "alter[ing] the mix of programming available on cable" in violation of video providers' rights under the First Amendment.  *Id.* at 1320-21 (internal quotation marks omitted).  The court found that the cable companies did differ from newspapers in one respect, namely the bottleneck monopolies historically enjoyed by the cable incumbents:

> A cable operator is unlike a newspaper publisher, however, *in the one respect crucial to the Congress's reason* for enacting the channel occupancy provision:  A newspaper publisher does not have the ability to exclude competing publications from its subscribers' homes.  The cable operator's bottleneck monopoly is a physical and economic barrier to such intra-medium competition.

*Id.* at 1321 (emphasis added); *see also id.* at 1317-18 (noting that "[i]n enacting the subscriber limits, the Congress was concerned that cable operators might use that same bottleneck power to exclude other providers of cable programming" and that "[i]n *Turner I* this bottleneck power was seen to jeopardize the viability of broadcast television; in this case, it arguably threatens diversity and competition in the provision of cable programming").

Because this "gatekeeper" or "bottleneck" premise simply is not present where two or more wireline video providers compete in an area, the type of regulations at issue here cannot be sustained in any such area and certainly cannot be sustained as to any competitive entrant.  Indeed, because the regulations being considered prohibit a willing speaker from engaging in certain types of speech (*i.e.*, programming affiliated with the cable operator) with a willing listener, they are subject to strict scrutiny and are facially invalid under that standard.

But, even under intermediate scrutiny test, applying channel occupancy limits to video providers in areas with wireline competition would run afoul of the First Amendment. Even content-neutral regulations that impose only incidental burdens on speech must "further[] an important or substantial governmental interest; . . . the governmental interest [must be] unrelated to the suppression of free expression; and . . . the incidental restriction on alleged First Amendment freedoms [must be] no greater than is essential to the furtherance of that interest." *Turner I* at 662 (quoting *United States v. O'Brien*, 391 U.S. 367, 377 (1968) (internal quotation marks omitted)). Moreover, in order to satisfy intermediate scrutiny, the Commission would need to show "substantial evidence," *Time Warner II* at 1130 (quoting *Time Warner I* at 1319-20), "demonstrating that the recited harms are real, not merely conjectural." *Time Warner II* at 1130 (quoting *Turner I* at 664). In doing so, "the FCC must show a record that validates the *regulations*, not just the abstract statutory authority." *Id.*

As *Time Warner II* shows, given the absence of bottleneck control, applying channel occupancy or other ownership caps to providers in areas with two or more wireline competitors or to new entrants cannot satisfy intermediate scrutiny because such rules burden substantially more speech than is necessary to further any important governmental interest. The D.C. Circuit noted in that case the "true relevance of competition" in assessing the First Amendment limits on the Commission's ownership rules, and noted that "[i]f an MVPD refuses to offer new programming, customers with access to an alternative MVPD may switch." *Time Warner II* at 1134. The court noted that "exposure to competition will have an impact on a cable company's *ability* to indulge in favoritism for in-house productions," and pointed out that the Commission had itself recognized that "[w]here systems face effective competition, their incentive to favor an affiliated programmer will be replaced by the incentive to provide programming that is most valued by subscribers." *Id.* at 1138.

Moreover, again alluding to the lack of bottleneck control where competitions exists, the court noted that "[e]ven if competing MSOs filled all of their channels with affiliates' products (as unlikely as that seems), the Commission nowhere explains why, in the pursuit of diversity, the independence of competing vertically integrated MVPDs is inferior to the independence of unaffiliated programmers." *Id.* at 1139. Therefore, the court concluded that the Commission had failed to "justify the use of so blunt a blade" when it "refus[ed] to exempt MVPDs that are subject to effective competition," and held that "the FCC has failed to justify its vertical limit as not burdening substantially more speech than necessary." *Id.* at 1138-39. As this shows, ownership limits burden substantially more speech than the First Amendment permits when they apply to providers in areas where competition exists and when they apply to new entrants.

Nor is there any evidence that would support imposing channel occupancy or ownership limits under these circumstances. As the Commission itself has recognized, however, video competition – including nationwide competition from two satellite providers – is growing, the level of vertical integration is declining, and the capacity available on video systems is increasing.[7] In fact, no parties in the recent round of comments provided *any* argument or evidence supporting the adoption of channel occupancy limits generally, much less the requisite "substantial evidence" to support a restriction on providers' speech, and certainly provided no evidence supporting such rules in competitive areas or for new entrants.

[7] *See, e.g., Report and Order* ¶ 16.

## III. Congress's Preference for Competition Makes Rules Inappropriate.

As the statute reflects, Congress's overriding interest in requiring "reasonable limits" on the number of affiliated channels a cable operator may carry was to "enhance effective competition." 47 U.S.C. § 533(f)(1). At the time that Congress adopted this provision, it was faced with situation of an increasingly concentrated video marketplace, predominantly made up of vertically-integrated, monopoly cable operators with bottleneck control who were generally shielded from competition by exclusive and de facto exclusive franchises.[8] These operators had exhibited a history of abuses aimed at entrenching themselves, favoring their affiliated programming, and extracting concessions from independent programmers

In response to this situation, Congress adopted a number of provisions in the 1992 Cable Act aimed at ensuring that the incumbent cable operators did not exploit their bottleneck control to foreclose video competition. For example, Congress amended Section 621(a)(1) in order to encourage the entry of new wireline video competition and adopted Section 628 to ensure that new entrants had reasonable access to cable programming.[9] In all of its efforts, however, Congress's "principal objective . . . was to foster competition in the acquisition and delivery of multi-channel video programming by encouraging the development of alternative and new technologies, including cable and non-cable systems."[10] And as the Commission has recognized, "Congress evidenced a preference for competition over regulation in order to achieve this objective, believing that the presence of alternative cable and non-cable MVPDs would constrain cable operators' market power

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8 *See Turner I* at 634 (noting Congress' concern with effects of "vertical integration" and "horizontal concentration" when it adopted the 1992 Cable Act).

9 47 U.S.C. §§ 541, 548. Later, the 1996 Act further promoted video competition by removing barriers to the provision of video service by telecommunications carriers. *See* 47 U.S.C. § 571.

10 Second Further Notice of Proposed Rulemaking, *Commission's Cable Horizontal and Vertical Ownership Limits*, 20 FCC Rcd 9374, ¶ 19 (2005).

in the acquisition and distribution of multi-channel video programming, as well as improve their service and programming quality and curb their subscription rate increases." *Id.*

Consistent with this overall theme, in the context of ownership rules Congress directly expressed that its goal was to "enhance effective competition." 47 U.S.C. § 533(f)(1). Congress also included several "public interest objectives" for the Commission to consider that further emphasized the preference for competition, the intended, limited scope of any regulations, and the requirement that Commission "make such rules and regulations reflect the dynamic nature of the communications marketplace." 47 U.S.C. § 533(f)(2). Among other things, Congress also indicated that the Commission must take "particular account of the market structure . . ., including the nature and market power of the local franchise." 47 U.S.C. § 533(f)(2)(C).

Given this statutory framework, the D.C. Circuit previously concluded that the Commission exceeded its statutory authority by failing to adequately account for Congress' pro-competitive purpose and the statutory directives to consider market dynamics and structure, even in the case of the incumbent cable operators. *Time Warner II* at 1136. In light of Congress's focus, the court rejected the Commission's earlier channel occupancy cap that imposed limits on providers even in areas with competition, stating:

> Because competition raises the stakes for a firm that sacrifices the optimal price-quality trade-off in its acquisition of programming, the issue seems to trigger the legislative directive [to take "particular account of the market structure"]. Yet the Commission seems to ignore its own conclusions about cable companies' incentives and constraints, and the dynamics of the programming industry.

*Id.* at 1139; *see also id.* at 1136 (noting that the express statutory purpose of promoting competition "sharply confines the [Commission's] authority to regulate solely in the interest of diversity"). The same statutory limitations on the Commission's authority and directives to take into account the dynamic nature of the video marketplace also preclude the Commission from imposing channel occupancy limits in areas with wireline competition. And this is all the more true in the case of new entrants who, by their very existence, promote competition and provide alternative platforms for independent and diverse programmers.

### IV. There Is No Basis to Expand the Reach of Any Channel Occupancy Cap.

Just as there is no basis to impose channel occupancy or ownership limits in competitive areas or on new entrants as a general matter, there likewise is no basis for expanding any such limits beyond those previously adopted.

First, there is no basis to limit the carriage of all channels affiliated with *any* other cable operator, rather than just channels affiliated with the particular provider to whom the cap is being applied. *Further Notice* ¶ 145. The Commission was correct when it previously concluded that "the most logical interpretation of the statutory language is to apply [any channel occupancy] limits only to video programmers that are vertically integrated with the *particular* cable operator in question," and noted that "this represents the most reasoned approach given Congress' stated objective of encouraging a diversity of voices and preventing unaffiliated programmers from being denied carriage on vertically integrated cable systems."[11]

A contrary conclusion that limits the number of channels affiliated with *any* cable operator would make no sense, and could lead to absurd results. To the extent that such a rule is premised on fears of collusion between different cable operators, the D.C. Circuit has already rejected the approach of assuming possible collusion in setting ownership limits, particularly given the substantial First Amendment stakes. *See Time Warner II* at 1130-31. And that is particularly true of competitive providers who generally own few if any channels of their own and compete head-to-head with the cable incumbents everywhere that they offer service.

[11] Second Report and Order, *Implementation of Sections 11 and 13 of the Cable Television Consumer Protection and Competition Act of 1992, Horizontal and Vertical Ownership Limits,* 8 FCC Rcd 8565, ¶ 52 (1993).

Second, there is no basis for applying a vertical ownership cap to all of a providers' capacity rather than only to the first 75 channels. *See Further Notice* ¶ 145. In light of the pro-competitive trends discussed above – and the significant First Amendment limitations that apply to the Commission's actions in this regard – any such rule could not be sustained.

Respectfully submitted,

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