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

In the Matter of	)	
	)	
Petition for Rulemaking to Amend The Commission's Rules Governing Retransmission Consent	)	MB Docket No. 10-71
	)	

COMMENTS

Matthew M. Polka
President and Chief Executive Officer
American Cable Association
One Parkway Center
Suite 212
Pittsburgh, Pennsylvania 15220
(412) 922-8300

Ross J. Lieberman
Vice President of Government Affairs
American Cable Association
2415 39th Pl, N.W.
Washington, DC 20007
(202) 494-5661

Christopher C. Cinnamon
Jeremy M. Kissel
Cinnamon Mueller
307 North Michigan Avenue
Suite 1020
Chicago, Illinois 60601
(312) 372-3930

Attorneys for the American Cable Association

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SUMMARY

Retransmission consent increasingly means spiraling prices and bitter public showdowns with threatened or actual withdrawal of local network signals. Each outcome harms consumers. For smaller operators, two additional aspects of the current retransmission consent regime are of particular concern and need to be addressed:

- Price discrimination against smaller MVPDs; and
- Joint negotiations involving multiple Big 4 affiliates in a single market.

Retransmission consent price discrimination. Smaller MVPDs pay retransmission consent fees more than twice as high as larger MVPDs for the same broadcast signals. No meaningful cost-based justification exists for this disparity; it simply reflects the vast difference in bargaining power between a smaller MVPD and a Big 4 affiliate (*i.e.*, ABC, NBC, CBS, or FOX). Pervasive price discrimination against smaller MVPDs raises costs for smaller-market consumers and impedes broadband deployment – important public interest concerns the Commission must protect.

Joint negotiating of retransmission consent. Broadcasters increasingly use sharing agreements or duopolies to jointly negotiate retransmission consent for multiple Big 4 affiliates in the same market. All available evidence suggests that joint control or ownership of multiple Big 4 affiliates in a single DMA results in significantly higher retransmission consent fees, resulting in higher costs for consumers and hindering broadband deployment.

Remedies. The rulemaking proposed in the *Petition for Rulemaking* will provide the Commission the record it needs to examine the magnitude and harms of retransmission consent price discrimination, as well as how joint negotiations, both by control and ownership, result in higher costs for consumers, providing the basis to

fashion appropriate remedies to address the harms.

Legal authority. The Commission has ample statutory authority under Section 325 of the Communications Act to address the concerns raised in the *Petition for Rulemaking*, as well as ACA's concerns about retransmission consent price discrimination and broadcasters' use of joint negotiations.

The Commission should launch the rulemaking requested in the *Petition for Rulemaking* and in these Comments.

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COMMENTS

American Cable Association

I. INTRODUCTION

ACA, a party to the *Petition*,[1] submits its strongest possible support for a rulemaking on reform of retransmission consent. As the *Petition* shows, retransmission consent increasingly means spiraling prices and bitter showdowns with threatened or actual withdrawal of network signals. Each outcome harms consumers. In smaller markets especially, the escalating cost of retransmission consent also threatens broadband deployment. Through a rulemaking, the Commission can fully and fairly explore the problems and solutions.

Beyond the issues raised in the *Petition*, the rulemaking must explore two additional aspects of the current retransmission consent regime that impact consumers:

- Price discrimination against smaller MVPDs; and
- Joint negotiations involving multiple Big 4 affiliates in a single market.

[1] *In the Matter of Petition for Rulemaking to Amend the Commission's Rules Governing Retransmission Consent*, Petition for Rulemaking, MB Docket No. 10-71 (filed Mar. 9, 2010) ("*Petition*").

Retransmission consent price discrimination and joint negotiations involving two or more Big 4 affiliates (*i.e.*, ABC, NBC, CBS or FOX) in the same market especially harm smaller market consumers and MVPDs, and any reform of retransmission consent should make addressing these problems a priority.

Raising retransmission consent costs through price discrimination. As explained by Professor William Rogerson,[2] smaller MVPDs pay retransmission consent fees more than twice as high as the average retransmission consent fee paid by large operators.[3] No meaningful cost-based justification exists for this disparity; it simply reflects the vast difference in bargaining power between a smaller MVPD and a Big 4 station. As Professor Rogerson states:

> While there may be a good public policy rationale to require MVPD subscribers to make payments that help support the programming efforts of local broadcasters, the rationale for requiring the customers of small and medium sized 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 equity and fairness 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.[4]

The rulemaking proposed in the *Petition* will provide the Commission the record it needs to examine the harms of retransmission consent price discrimination and fashion

[2] ACA commissioned Professor William P. Rogerson to draft two papers that address rising retransmission consent costs through (i) price discrimination, and (ii) sharing agreements and duopolies. Professor Rogerson is a Professor of Economics at Northwestern University, and served as the Commission's Chief Economist from 1998-99.

[3] William P. Rogerson, *The Economic Effects of Price Discrimination in Retransmission Consent Agreements* (May 18, 2010) (attached as Appendix A) ("*2010 Rogerson Price Discrimination Report*").

[4] *2010 Rogerson Price Discrimination Report* at 4.

appropriate remedies.

Raising retransmission consent costs through joint negotiating. ACA members assert that broadcasters jointly negotiate retransmission consent for multiple Big 4 affiliates in the same market through sharing agreements, or as a result of duopolies. ACA identifies at least 93 sharing agreements or duopolies involving more than one Big 4 affiliate in 78 television markets – affecting more than 37% of the 210 DMAs – with the heaviest concentration in smaller markets served by ACA members. ACA members confirm having to jointly negotiate retransmission consent in many of these instances. Professor Rogerson details how this broadcaster tactic, akin to collusion, enables broadcasters to threaten simultaneous withdrawal of two “must have” channels, resulting in higher fees for MVPDs. As Professor Rogerson states:

> While there may be a good public policy rationale to require all MVPDs to make payments in support of the programming efforts of local broadcasters, it is hard to imagine a sound rationale for allowing broadcasters in some markets to extract higher payments than in other markets, based on whether they are able to enter into agreements with one another that essentially reduce the extent to which they compete with one another.[5]

The rulemaking proposed in the *Petition* will provide the Commission the record it needs to examine the harms of joint retransmission consent negotiations, both by contract and ownership, and provide the basis to fashion appropriate remedies to address the harm.

As detailed in the *Petition* and in these Comments, the current retransmission consent regime harms competition and consumers. In particular, the higher carriage fees that result from price discrimination and joint negotiations are passed through to

[5] William P. Rogerson, *Joint Control or Ownership of Multiple Big 4 Broadcasters in the Same Market and its Effect on Retransmission Consent Fees*, at 4 (May 18, 2010) (attached as Appendix B) (“*2010 Rogerson Joint Control or Ownership Report*”).

customers in the form of higher cable rates. The Commission has ample authority to address these harms.

As a first step, the Commission should launch a rulemaking addressing the issues raised in the *Petition* and these Comments.

American Cable Association. ACA represents 900 small and medium-sized cable operators, companies providing video, high-speed broadband, and phone service in smaller markets across the U.S. ACA's membership includes a variety of businesses – family-owned companies serving small towns and villages, multiple system operators serving predominantly rural markets in several states, and hundreds of companies in between. These companies deliver affordable basic and advanced services, such as high-definition television, next-generation Internet access, and digital phone, to more than 7 million households and businesses.

The current retransmission consent regime, with spiraling costs and highly disruptive withdrawals, harms consumers and the ACA members who serve them, and ACA provides its strongest support for retransmission consent reform.

II. THE RETRANSMISSION CONSENT REFORM RULEMAKING MUST ADDRESS WIDESPREAD PRICE DISCRMINATION AGAINST SMALLER MVPDS.

The *Petition* describes the harms of the current retransmission consent regime and the need for reform to address those harms. Beyond the issues raised in the *Petition*, the rulemaking must also address a retransmission consent problem concentrated in the small cable sector – price discrimination.

In 2008, ACA provided the Commission with a detailed report on retransmission consent price discrimination against smaller MVPDs.[6] That filing explained how broadcasters were discriminating against smaller MVPDs by charging substantially higher per subscriber fees than those paid by larger operators.[7] At that time, Professor Rogerson conducted an economic evaluation of retransmission consent price discrimination, concluding the following:

> 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 that possess less bargaining power.[8]

We update our 2008 filing in these Comments, showing that retransmission consent price discrimination continues unabated. Professor Rogerson has updated his economic report, and we append his analysis to these Comments.

A. Broadcasters charge small and medium-sized cable companies retransmission consent fees more than twice as much as larger MVPDs pay for the same stations.

Publicly available information, combined with reports from ACA members, shows that retransmission consent price discrimination against smaller MVPDs has not ceased since our 2008 report to the Commission. Today, smaller cable operators are paying,

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[6] *In the Matter of Implementation of the Cable Television Consumer Protection and Competition Act of 1992, Review of the Commission's Program Access Rules and Examination of Programming Tying Arrangements*, Report and Order and Notice of Proposed Rulemaking, 22 FCC Rcd. 17791 (2007) ("*2007 Program Access NPRM*"), Reply Comments of the American Cable Association, MB Docket No. 07-198, at 6-14 (filed Feb. 12, 2008) ("*ACA 2008 Program Access Reply Comments*").

[7] *ACA 2008 Program Access Reply Comments* at 7-8.

[8] *Id.*, Appendix A, William P. Rogerson, *The Economic Effects of Price Discrimination in Retransmission Consent Agreements*, at 9 (filed Feb. 12, 2008).

on average, retransmission consent fees that are at least double the amount of larger operators.

In the attached study, Professor Rogerson evaluates recent reports of retransmission consent prices compiled by Kagan Research.[9] Kagan's most recent report contains estimates and projections of retransmission consent payments broken down by MVPD type and projections for the number of MVPD subscribers by MVPD type. From this data, Professor Rogerson has calculated 2010 average per subscriber retransmission consent fees by MVPD type, summarized in Tables 1 and 2 below.

TABLE 1
2010 PER SUBSCRIBER RETRANSMISION CONSENT PAYMENTS
TO ALL BROADCAST STATIONS
BROKEN DOWN BY TYPE OF MVPD[10]

MVPD Type	Total Retrans Payments (millions of $)	Total Subscribers (millions)	Per Subscriber Retrans Payments ($ per sub per month)
Cable	$424.0	62.1	$.57
DBS	$390.0	32.3	$1.01
Telco	$119.1	8.2	$1.21
All	$933.1	102.2	$.76

Assuming that each MVPD pays for 4 Big 4 stations per market, Professor Rogerson calculates per station fees in Table 2.

[9] *2010 Rogerson Price Discrimination Report* at 10-14 (*citing* Tables 2 and 3 of Katz, Michael L., Jonathan Orzag, and Theresa Sullivan, *An Economic Analysis of Consumer Harm From the Current Retransmission Consent Regime* at 32, 34, Nov. 12, 2009 ("*Katz Economic Paper*"), attached to the Comments of the National Cable & Telecommunications Association, MB Docket No. 07-269 (filed Dec. 16, 2009).

[10] *2010 Rogerson Price Discrimination Report* at 11 (*citing Katz Economic Paper*).

TABLE 2
2010 AVERAGE PER SUBSCRIBER RETRANSMISSION CONSENT PAYMENTS TO A SINGLE BIG 4 STATION BROKEN DOWN BY TYPE OF MVPD[11]

MVPD Type	Per Subscriber Retrans Payments ($ per sub per month)
Cable	$0.14
DBS	$0.25
Telco	$0.30
All	$0.19

From this data, Professor Rogerson evaluates the magnitude of price discrimination as follows:

> To interpret these numbers, note that although there are a large number of small and medium sized cable operators, they are completely dwarfed in size by the handful of large operators with the result that only a very small fraction of cable subscribers receive service from small or medium sized MVPDs. Therefore the average per subscriber retransmission consent payment made by cable MVPDs in Table 2 should be interpreted as being very close to the average amount paid by large cable operators. In particular, then, consistent with the description of bargaining strength in Section 2, above, large cable operators pay the lowest per subscriber retransmission consent fees; on average they pay $.14 per subscriber per month to an individual Big 4 station.
>
> * * *
>
> Therefore, based on the above data, it appears that the average retransmission consent fee paid by small and medium sized cable operators is more than twice as high as the average retransmission consent fee paid by large cable operators. Representatives of the ACA have told me that, based on anecdotal evidence from their membership, they agree that $.30 per subscriber per month is likely a conservative estimate of the retransmission consent fee that the average small or medium sized MVPD pays to a single Big 4 station. In fact they are aware of numerous instances where their members currently pay retransmission consent fees as high as $.75 per subscriber per month to individual Big 4

[11] *Id.* at 11.

stations.[12]

According to ACA members, many retransmission consent contracts specify that MVPDs bear the cost of obtaining the broadcasters' signal. In accordance with these provisions, ACA members pay the fees associated with receiving the broadcast signal, whether off-air, via fiber, or other means. Thus, the difference in prices paid by large and small operators has <u>no</u> basis in broadcasters' cost of delivering the signal.[13] The principal reason for the difference relates to the bargaining power between a "must have" Big 4 broadcast station and a small MVPD.[14] Professor Rogerson's analysis underscores the trends reported by industry analysts and participants. Sanford Bernstein cable and satellite analyst Craig Moffett has described how small operators bear the brunt of retransmission consent "pain":

> "[T]wo trends are clear from 2007: <u>retrans consent generates cash and smaller operators . . . will bear the brunt of the pain</u>."[15]

Dr. John Malone, chairman of Liberty Media and DirecTV, recently described price discrimination in even more blunt terms:

> The biggest distributors have some leverage in that negotiation because they can do damage. <u>The smaller distributors are going to be pretty powerless to protect themselves from getting creamed…</u>.[16]

Broadcasters' triple-digit price discrimination against smaller MVPDs validates Dr.

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[12] *Id.* at 12-13.

[13] *Id.* at 13-14.

[14] *Id.* at 14.

[15] Mike Farrell, *Retrans on the Rise*, MULTICHANNEL NEWS, Jan. 6, 2008, *available at* http://www.multichannel.com/article/131629-Retrans_On_the_Rise.php (last visited May 18, 2010) (emphasis added).

[16] Kelley Riddell, *Malone Sees Pay-TV Industry Consolidation as Fee Disputes Mount*, BLOOMBERG NEWS, Mar. 19, 2010, *available at* http://www.bloomberg.com/apps/news?sid=aWetzLpEbhUo&pid=20601087 (last visited May 18, 2010) (emphasis added).

Malone's observation – smaller MVPDs are "getting creamed."

But Dr. Malone gets it only half right. Retransmission consent price discrimination also "creams" consumers served by smaller MVPDs, causing significant public interest harms. The impact of increased retransmission consent costs on consumers will be discussed more fully in Section IV below.

III. THE RETRANSMISSION CONSENT REFORM RULEMAKING MUST ADDRESS BROADCASTERS' USE OF JOINT NEGOTIATING TO INCREASE RETRANSMISSION CONSENT FEES.

From the perspective of smaller MVPDs, the other significant problem with the current retransmission consent regime is broadcasters' use of sharing agreements or duopolies to jointly negotiate retransmission consent for multiple Big 4 affiliates in the same market. Available evidence strongly suggests that joint control or ownership of multiple Big 4 affiliates in a single DMA results in significantly higher retransmission consent fees. Consumers, particularly in smaller markets, ultimately foot the bill in the form of higher cable rates.

Commission rules generally prohibit common ownership of Big 4 stations in a single DMA.[17] However, broadcasters circumvent this general prohibition through the Commission's waiver process, or via contractual agreements that offer one Big 4 station control of another in the same market. These arrangements come in many varieties and have various names, such as shared services agreements (SSAs) and local marketing agreements (LMAs).

ACA has examined publicly available documents and records to put together as thorough a list as possible of all instances in which multiple Big 4 broadcast affiliates

[17] 47 C.F.R. § 73.3555(b).

from the same DMA are under joint control or ownership. ACA has identified at least 93 instances of these sharing agreements or duopolies in 78 television markets – affecting more than 37% of the 210 DMAs – with the heaviest concentration in smaller markets served by ACA members.[18] In *Table 1* of Appendix C,[19] there are 36 identified instances of two Big 4 affiliates in the same DMA operating under common ownership.[20] In *Table 2* of Appendix C,[21] ACA has identified 57 instances where multiple Big 4 affiliates in the same DMA operate under some sort of sharing agreement – which typically means the stations operate under joint control for purposes of negotiating retransmission consent agreements.[22] Based on reports from ACA members and other MVPDs, ACA can confirm that in many of the 57 instances where multiple Big 4 affiliates in the same DMA operate under some sort of sharing agreement, there was a single negotiator for both stations, and reaching carriage terms for one station was contingent upon reaching terms for the other.

There are likely additional instances of sharing arrangements and duopolies involving multiple Big 4 affiliates in the same market than is reported in *Table 1* and *Table 2*. ACA will update the record as more of these instances are discovered.

[18] *See* Appendix C, *36 Identified Instances of Common Ownership of Multiple Big 4 Affiliates in the Same Market* ("*Table 1*") and *57 Identified Instances of Common Control of Multiple Big 4 Network Stations in the Same Market* ("*Table 2*").

[19] Appendix C, *Table 1*.

[20] With respect to negotiating retransmission consent, ACA makes no distinction between a broadcaster that owns two stations – whether full or low power – in the same market that is affiliated with different Big 4 networks (*i.e.*, a duopoly), and a station owner that broadcasts one Big 4 network on its primary video stream and another Big 4 network on its multicast stream (*i.e.*, a multicast duopoly).

[21] Appendix C, *Table 2*.

[22] While broadcasters appear to generally make known when sharing agreements exist between stations, they rarely publicly disclose the terms of these arrangements. Thus, it is difficult to determine from publicly available documents whether or not a sharing agreement includes the assignment of retransmission consent negotiation rights.

Furthermore, there may be instances in which broadcasters agree to jointly negotiate retransmission consent but otherwise operate separately. If such stations do not consider themselves as operating under a sharing agreement, then they would not appear in *Table 2* even though they do in fact negotiate retransmission consent prices together.

A. Economic theory shows how broadcasters' use of joint negotiating increases retransmission consent fees.

In the attached paper, Professor Rogerson applies basic economic theory to show how broadcasters' joint negotiation of retransmission consent involving multiple Big 4 affiliates in the same market can result in higher retransmission consent fees. Professor Rogerson, applying a standard modeling approach, explains:

> When a programmer and MVPD negotiate the fee that the MVPD will pay the programmer, they are essentially deciding how to split the joint economic gains created from having the MVPD carry the programming. This sort of bilateral bargaining situation has been extensively modeled in the economics literature. Application of the standard modeling approach used in the economics literature immediately demonstrates that a programmer selling two different programs will be able to charge more by bundling the programs together so long as the programs are substitutes in the sense that the marginal value of either of the programs to the MVPD is lower conditional on already carrying the other program.[23]

As Professor Rogerson notes in his paper, the theory suggests "that there will be a significant empirical effect…," but "[w]hether or not this effect is significant is an empirical issue."[24]

B. Empirical evidence available demonstrates that joint negotiating significantly increases retransmission consent fees.

[23] *2010 Rogerson Joint Control or Ownership Report* at 7-8. (citations omitted). Professor Rogerson also provides a simple example of this theory in his report. *Id.* at 8-9.

[24] *Id.* at 11.

The evidence available suggests that when broadcasters jointly negotiate retransmission consent for multiple Big 4 affiliates in a single market, the result is significantly higher retransmission consent fees.

In a recent filing with the Commission, Suddenlink Communications ("Suddenlink") reported the results of an internal analysis it conducted showing the effect ownership status of broadcast stations has on the magnitude of retransmission consent fees. Suddenlink reported:

> Suddenlink has examined its own retransmission consent agreements and has concluded that, where a single entity controls retransmission consent negotiations for more than one "Big 4" station in a single market, the average retransmission consent fees Suddenlink pays for such entity's "Big 4" stations (in all Suddenlink markets where the entity represents one or more stations) is 21.6% higher than the average retransmission consent fees Suddenlink pays for other "Big 4" stations in those same markets. This is compelling evidence that an entity combining the retransmission consent efforts of two "Big 4" stations in the same market is able to secure a substantial premium by leveraging its ability to withhold programming from multiple stations.[25]

Professor Rogerson observes, "[the Suddenlink analysis] should raise the Commission's concern, especially in light of the fact that such an outcome is completely consistent with the predictions of standard economic theory under plausible circumstances."[26]

Moreover, a recent Congressional Research Service report on retransmission consent made the following observation while discussing programmer-distributor conflicts:

> In the earlier section presenting specific examples of programmer-

[25] *In the Matter of Mediacom Communications Corporation v. Sinclair Broadcast Group, Inc.*, Retransmission Consent Complaint, CSR-8233-C, CSR-8234-M, *Ex Parte* Comments of Suddenlink Communications at 5 (filed Dec. 14, 2009).

[26] *2010 Rogerson Joint Control or Ownership Report* at 12.

> distributor conflicts, it was striking how often the broadcaster involved in a dispute owned or controlled more than one broadcast station in a small or medium sized market. It appears that where a broadcaster owns or controls two stations that are affiliated with major networks, that potentially gives that broadcaster control over two sets of must-have programming and places a distributor, especially a relatively small cable operator, in a very weak negotiating position since it would be extremely risky to lose carriage of both signals.[27]

The evidence available suggests that sharing agreements and duopolies ***do*** increase retransmission consent fees, and the higher costs have no economic rationale or public policy basis. Professor Rogerson summarizes the problem as follows:

> While there may be a good public policy rationale to require all MVPDs to make payments in support of the programming efforts of local broadcasters, it is hard to imagine a sound rationale for allowing broadcasters in some markets to extract higher payments than broadcasters in other markets, based on whether they are able to enter into agreements with one another that essentially reduce the extent to which they compete with one another.[28]

The United States Department of Justice (DOJ) initiated at least one antitrust action against broadcasters based on the combined control of multiple broadcast stations in the same market. The DOJ alleged that three broadcast stations in the Corpus Christi DMA illegally conspired to raise retransmission consent fees by jointly negotiating retransmission consent.[29] The matter was settled when the three stations

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[27] Charles B. Goldfarb, CRS Report for Congress, *Retransmission Consent and Other Federal Rules Affecting Programmer-Distributor Negotiations: Issues for Congress*, at CRS-70 (July 9, 2007), *available at* http://www.policyarchive.org/handle/10207/bitstreams/19204.pdf (last visited May 18, 2010) (emphasis added).

[28] *2010 Rogerson Joint Control or Ownership Report* at 4.

[29] *See U.S. v. Texas Television, Inc., Gulf Coast Broadcasting Co., and K-Six Television, Inc.*, Complaint, (Feb. 2, 1996), *available at* http://www.justice.gov/atr/cases/f0700/0745.pdf (last visited May 18, 2010). *See also U.S. v. Texas Television, Inc., Gulf Coast Broadcasting Co., and K-Six Television, Inc.*, Competitive Impact Statement, *available at* http://www.justice.gov/atr/cases/f0700/0746.pdf (last visited May 18, 2010).

agreed to terminate the practice and refrain from engaging in such practices in the future.

IV. RETRANSMISSION CONSENT PRICE DISCRIMINATION AND BROADCASTERS' USE OF JOINT NEGOTIATING RESULTS IN HIGHER RETRANSMISSION CONSENT FEES THAT RAISE COSTS FOR CONSUMERS AND IMPEDES BROADBAND DEPLOYMENT.

Retransmission consent price discrimination and broadcasters' use of joint negotiating impacts consumers by increasing their subscription fees and hindering MVPDs' ability to deploy broadband. As reported by Professor Rogerson, available evidence shows smaller MVPDs pay more than twice as much as larger operators for the same Big 4 local broadcasts signals. Evidence further suggests that when broadcasters jointly negotiate retransmission consent for multiple Big 4 affiliates in a single market, the result is higher retransmission consent fees than could be obtained through separate negotiations. Increased retransmission consent fees result in higher basic cable rates for consumers and impedes broadband deployment, threatening important public interests the Commission must protect.

A. Retransmission consent price discrimination and broadcasters' use of joint negotiating raises costs for consumers.

The Commission has previously concluded what recent cable rate studies show, and ACA members report: Retransmission consent fee hikes are passed along to consumers in the form of higher cable rates.

In the Commission's evaluation of the News Corporation acquisition of DIRECTV, the Commission found that increased retransmission consent fees lead to higher costs for consumers and these higher costs can harm consumers.[30] Buttressing this

[30] *In the Matter of General Motors Corporation and Hughes Electronics Corporation, Transferors, and The*

conclusion, Professor Rogerson highlights a recent study on cable prices that found, in general, that around 50 percent of programming cost increases is passed along to customers in the form of higher subscription rates.[31] Moreover, as we reported to the Commission last year, 88% of ACA members surveyed had already or planned to raise basic cable rates because of retransmission consent fee increases that incurred between 2008 and 2009.[32]

In speaking about retransmission consent recently, Chairman Genachowski expressed concern about "the *potential* for rising cable rates" and how that could impact consumers, whom the Chairman described as "third parties who aren't at the table" in retransmission consent negotiations.[33] For consumers served by smaller MVPDs, that "potential" has already become a reality, and consumers are paying the price for rampant price discrimination against smaller cable operators and joint negotiating.

With particular regard to retransmission consent price discrimination, it means 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 unreasonable cost disparity between viewers of the same programming:

News Corporation Limited, Transferee, For Authority to Transfer Control, Memorandum Opinion and Order, 19 FCC Rcd. 473, 568, ¶ 209 (2004) ("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.") ("News Corp.'s use of market power to extract artificially high levels of compensation from MVPD rivals…could make rival MVPDs less viable options for consumers, thus limiting consumer choice.").

[31] *2010 Rogerson Price Discrimination Report* at 15.

[32] *In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, Supplemental Notice of Inquiry, 24 FCC Rcd. 4401 (2009), Comments of the American Cable Association, MB Docket No. 07-269, Appendix 1, Clarus Research Group, *Impact of Retransmission Consent Costs on Members of the American Cable Association*, at 2, 7 (filed July 29, 2009).

[33] Remarks of Chairman Julius Genachowski, National Association of Broadcasters Show at 8 (Apr. 13, 2010), *available at* http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-297469A1.pdf (last visited May 18, 2010).

> Since MVPDs pass higher programming costs back to their subscribers in the form of higher subscription fees, the main ultimate 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.[34]

Beyond increasing the cost of cable, retransmission consent price discrimination and broadcasters' use of sharing agreements and duopolies also threaten broadband deployment in rural markets. As discussed, while about 50 percent of retransmission consent cost increases are passed along to consumers, the remainder depletes capital that could be used to deploy other advanced services, including broadband.

B. Increased retransmission consent fees hurt broadband deployment in smaller markets.

In markets served by smaller MVPDs, the current retransmission consent regime also threatens the Commission's top policy priority – broadband. The calculus is straightforward – for businesses with limited resources, broadcasters' escalating demands require diverting funds from network expansion and upgrades. Because of triple-digit percentage price discrimination, smaller MVPDs and rural markets are most vulnerable.

ACA began reporting this dynamic to the Commission in 2008.[35] Other smaller MVPDs and their representatives have corroborated this problem.

From NTCA:

> 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.[36]

[34] *2010 Rogerson Price Discrimination Report* at 15.

[35] *2007 Program Access NPRM*, Comments of the American Cable Association, MB Docket No. 07-198, at 20 (filed Jan. 3, 2008) ("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.).

[36] *2007 Program Access NPRM*, Comments of the National Telecommunications Cooperative

From CA2C:

> 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.[37]

From OPASTCO, et al.:

> 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.[38]

As described above, retransmission consent price discrimination and broadcasters' use of sharing agreements and duopolies results in substantial public interest harms. The Commission should make addressing these problems a top priority in the retransmission consent reform rulemaking.

V. REMEDIES.

The Commission must address the consumer harms identified in the *Petition* and these Comments, although specific remedies can be developed through a retransmission consent rulemaking. Any remedies <u>must address</u> the significant retransmission consent price discrimination faced by smaller MVPDs, as well as broadcasters' use of joint negotiating to obtain higher fees than that which can be achieved through separate negotiations. ACA looks forward to working with the Commission to identify specific remedies to address these consumer harms in a rulemaking proceeding.

Association, MB Docket No. 07-198, at 2 (filed Jan. 4, 2008).

[37] *2007 Program Access NPRM*, Comments of the Coalition for Competitive Access to Content, MB Docket No. 07-198, at 20 (filed Jan. 4, 2008).

[38] *2007 Program Access NPRM*, Comments of the Organization for the Promotion and Advancement of Small Telecommunications Companies, *et al.*, MB Docket No. 07-198, at 19 (filed Jan. 4, 2008).

VI. THE COMMISSION HAS AMPLE AUTHORITY TO ADDRESS RETRANSMISSION CONSENT PRICE DISCRIMINATION AND BROADCASTERS' USE OF JOINT NEGOTIATING TO INCREASE RETRANSMISSION CONSENT FEES.

The Commission has ample statutory authority to address the concerns raised in the *Petition* and these Comments in a retransmission consent reform rulemaking.

A. The Commission has broad authority under Section 325 to adopt rules governing retransmission consent agreements.

Section 325(b)(3)(A) tells the Commission "to govern the exercise by television broadcast stations of the right to grant retransmission consent…."[39] With this language, Congress expressly gives the Commission broad authority to adopt rules that protect the public interest as it relates to broadcasters' grant of retransmission consent rights to MVPDs. This clause provides the Commission with the authority to promulgate regulations that address the harms that result from retransmission consent price discrimination against small and medium-sized operators, as well as joint negotiations involving multiple Big 4 network affiliates in the same market. It was Congress's intent that the Commission be empowered to address these concerns.

B. Congress expressly granted the Commission authority to craft rules that considers the impact of the retransmission consent granting process on cable rates.

Section 325(b)(3)(A) also instructs the Commission to consider "the impact that the grant of retransmission consent by television stations may have on the rates for the basic service tier…," and to make sure its rules are not inconsistent with its obligation "to ensure that the rates for the basic service tier are reasonable."[40] Congress has

[39] 47 U.S.C. § 325(b)(3)(A).

[40] *Id.*

provided the Commission with the express authority to formulate retransmission consent rules that would, in instances where broadcaster actions impact the rates paid by consumers, minimize the effect of price discrimination and joint negotiations involving multiple Big 4 affiliates in the same market.

As detailed in Sections II and III above, economic theory and available evidence shows that consumers of small and medium-sized operators pay higher cable rates as a result of retransmission consent price discrimination and joint negotiating of multiple Big 4 affiliates in the same market. With respect to price discrimination, smaller operators pay more than twice as much as the average retransmission consent fees paid by larger operators. In retransmission consent negotiations involving multiple Big 4 stations in the same market, it has been reported that carriage fees are 20% more than deals negotiated individually. The higher retransmission consent fees that result from price discrimination and joint negotiations are passed on to subscribers through higher subscription fees – particularly for the basic service tier, which must include all broadcast stations carried by an MVPD. In instances where the process for granting retransmission consent impacts cable rates – for example, price discrimination and joint negotiations – Congress expressly granted the Commission authority to address these concerns and expected it to do so.

The rulemaking proposed in the *Petition* and these Comments will provide the Commission the record it needs to examine how price discrimination and duopolies – both by contract and ownership – result in higher cable rates for consumers, and provide the basis to fashion appropriate remedies to address the harm.

C. The Commission has authority to adopt rules restricting broadcasters from engaging in price discrimination that results in

different retransmission consent prices and terms that are not based on competitive marketplace considerations.

Section 325(b)(3)(C)(ii) states that it is not a failure to negotiate retransmission consent in good faith if television broadcast stations propose or enter into retransmission consent agreements with different MVPDs containing different terms and conditions, including price terms, if based on "competitive marketplace considerations."[41] This express statutory provision makes clear that the converse – negotiations not based on competitive marketplace considerations – violates the duty to negotiate in good faith.

As shown above, smaller MVPDs face significant retransmission consent price discrimination. Professor Rogerson notes that these operators, on average, pay more than twice the retransmission consent fees paid by larger operators. In some instances, the price disparity is much greater. Price discrimination is a common feature in monopolistic markets, whereas in perfectly competitive markets price discrimination does not exist. Somewhere between these boundaries lies the "competitive marketplace considerations" Congress imagined. It is within the Commission's authority to conclude that the price discrimination faced by smaller operators today is not based on "competitive marketplace considerations," and to impose regulations to address the resulting harm.[42]

[41] 47 U.S.C. § 325(b)(3)(C)(ii) (emphasis added).

[42] Similarly, nothing here would prevent the Commission from adopting rules that would limit price discrimination against small and medium-sized cable operators pursuant to authority derived from other provisions in this section.

VII. CONCLUSION.

The rulemaking proposed in the *Petition* will provide the Commission the record it needs to examine the current retransmission consent marketplace and provide the basis to fashion appropriate remedies to address the harm. The Commission should launch the rulemaking requested in the *Petition*.

Respectfully submitted,

AMERICAN CABLE ASSOCIATION

By: ______________________________

Matthew M. Polka
President and Chief Executive Officer
American Cable Association
One Parkway Center
Suite 212
Pittsburgh, Pennsylvania 15220
(412) 922-8300

Ross J. Lieberman
Vice President of Government Affairs
American Cable Association
2415 39th Pl, N.W.
Washington, DC 20007
(202) 494-5661

Christopher C. Cinnamon
Jeremy M. Kissel
Cinnamon Mueller
307 North Michigan Avenue
Suite 1020
Chicago, Illinois 60601
(312) 372-3930

Attorneys for the American Cable Association

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Appendix A

The Economic Effects of Price Discrimination in Retransmission Consent Agreements

THE ECONOMIC EFFECTS OF PRICE DISCRIMINATION IN RETRANSMISSION CONSENT AGREEMENTS*

by

William P. Rogerson**

May 18, 2010

***	Prepared for the American Cable Association**

****	Professor of Economics, Northwestern University. FCC Chief Economist, 1998-99.**

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I. 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 carry their signals. In response to a petition for rulemaking,[2] the Commission has asked for comments evaluating the performance of the current retransmission consent regime. The central argument in the petition for rulemaking is that changes in market structure that have occurred since the introduction of the current framework have fundamentally altered the balance of bargaining power in this industry in favor of broadcasters. As a result, the fees that broadcasters are able to charge for retransmission consent are rising to much higher levels than were ever originally contemplated when the rules were first introduced. These fee increases are of course passed through to subscribers in the form of higher subscription prices. A related problem is the increasing occurrence of temporary withdrawals of broadcast signals during negotiations in which broadcasters attempt to exercise their increased bargaining power. The petition for rulemaking suggests that the Commission consider allowing parties to request binding arbitration with mandatory interim carriage of signals to address these problems.

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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).

[2] Public Knowledge, DirecTV, Inc., DISH Network LLC, Charter Communications, Inc., American Cable Association, New America Foundation, OPASTCO, Time Warner Cable, Inc., Verizon, Cablevision Systems Corp., Mediacom Communications Corp., Bright House Networks, LLC, Insight Communications Company, Inc., and Suddenlink Communications ("Petitioners"), "Petition for Rulemaking," *Petition for Rulemaking to Amend the Commission's Rules Governing Retransmission Consent*, MB Docket No. 10-71, March 9, 2010.

I agree with the basic economic conclusions of the petitioners as I have described them above, and also agree that the direction of reform suggested by the petitioners is a sensible course of action for the Commission to consider.

The purpose of this paper is to describe a related but additional problem with the retransmission consent process and possible approaches to solving it, that I believe the Commission should also seriously consider as part of its over-all evaluation of whether and how the regulatory framework governing the retransmission consent process could be improved.[3] The problem is that significant levels of price discrimination occur in agreements for retransmission consent. In particular, small and medium sized MVPDs are generally charged significantly higher retransmission consent fees than their larger competitors. Since increases in retransmission consent fees are passed through to consumers in the form of higher MVPD subscription prices, the result of this is essentially that subscribers to small and medium sized MVPDs are paying higher prices than subscribers to large MVPDs to be provided with the signals of broadcast networks.

In the remainder of this section I will briefly summarize the main points that I make about this problem and how retransmission consent rules could be reformed to deal with it.

1. Small and medium sized MVPDs generally have significantly less bargaining power than their larger competitors, 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. The result of this is that small and medium sized MVPDs are often required to pay

[3] I discuss an additional problem with the retransmission consent process in a companion paper also being submitted by the ACA in this proceeding entitled "Joint Control or Ownership of Multiple Big 4 Broadcasters in the Same Market and its Effect on Retransmission Consent Prices."

retransmission consent fees that are significantly higher than the fees that large MVPDs are required to pay for permission to retransmit exactly the same broadcast signal.

3. 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 even if they were not allowed to charge even higher prices to small and medium sized MVPDs. Therefore the main effect of price discrimination in this case, is simply to allow broadcasters to charge higher prices to MVPDs that possess less bargaining power.

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

5. While there may be a good public policy rationale to require MVPD subscribers to make payments that help support the programming efforts of local broadcasters, the rationale for requiring the customers of small and medium sized 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 equity and fairness 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.

6. The problem of price discrimination could be addressed by requiring broadcasters negotiating retransmission consent agreements to make the same terms and conditions available to all MVPDs, regardless of their size.

The remainder of the paper is organized as follows. Section 2 explains that small and medium sized MVPDs are charged higher retransmission consent fees because they have less bargaining power. Section 3 argues that the available evidence suggests that these differences in retransmission consent fees are significant. Section 4 describes the main potential efficiency benefit of price discrimination - that it may result in expansion of output - and shows that it does NOT apply to the case of price discrimination in retransmission consent agreements. Section 5 therefore draws the conclusion that the main economic effect of price discrimination in retransmission consent agreements is simply that different viewers are required to pay different fees for viewing exactly the same programming. Section 6 considers possible solutions and section 7 draws a brief conclusion.

2. SMALL AND MEDIUM SIZED MVPDS ARE CHARGED HIGHER FEES FOR RETRANSMISSION CONSENT BECAUSE THEY HAVE LESS BARGAINING POWER

A local broadcaster typically faces 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 in less developed areas typically served by a much larger number of very small cable systems. Of course, the two DBS providers, DirecTV and DISH, also generally make their services available throughout the viewing area. Finally, although local telephone companies ("telcos") are beginning to provide MPVD service in some areas, their presence at the moment is still quite limited. 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 customers served by any other MVPD (i.e., the telcos and small and medium sized MPVDs) is relatively insignificant.

There is widespread agreement among industry participants, policy makers, and economists and financial analysts that study this industry that, holding all other factors equal, the per subscriber retransmission consent fee that an MVPD is able to negotiate with a local broadcaster generally depends on the share of the local broadcaster's viewers served by the

MVPD. In particular, there is widespread consensus that an MPVD that serves a larger share of a local broadcaster's viewers is generally able to negotiate lower per subscriber retransmission consent fees than an MVPD that serves a smaller share of the broadcaster's viewers. Given the typical viewer shares described above, the result of this phenomenon is that large cable companies typically pay the smallest retransmission fees, with DBS providers paying somewhat larger fees, and telcos and small and medium sized cable companies paying the largest fees. I will provide some data to describe the level of these fee differences in the next section. However, before doing so, I will briefly describe the economic factors that cause this pricing pattern.

The rationale given for this phenomenon by industry participants and observers usually revolves around observations to the effect that MVPDs that serve a lower share of a broadcaster's viewers have less "bargaining power" or "leverage" to demand higher prices than do MVPDs that serve a higher share of a broadcaster's viewers. For example the New York Times quotes Bernstein Research analyst Craig Moffett 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."[4]

The industry publication MultiChannel News quotes this 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." [5]

Dr. John Malone, chairmen of Liberty Media and DirecTV has recently stated

"The biggest distributors have some leverage in that negotiations because they can do

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

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

> damage [but] the smaller distributors are going to be pretty powerless to protect themselves from getting creamed."[6]

Bernstein Research has recently released a comprehensive new report on retransmission consent[7] which describes in great detail its conclusion that an MVPD's bargaining strength with respect to a broadcaster depends critically on the share of the broadcaster's audience that the MVPD serves.

A recent report by the Congressional Research Service[8] reaches many of the same conclusions. For example, it 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."

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

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[6]Riddel, Kelley, "Bloomberg Sees Pay-TV Industry Consolidation as Fee Disputes Mount," Bloomberg News, March 19, 2010.

[7]Bernstein Research, *U.S. Cable & Satellite Broadcasting & U.S. Media: Sizing the "Retrans" Battle Royal*, April 14, 2010.

[8]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*").

penetration in those markets, which helps in negotiations with local broadcast stations." [9]

From an economic perspective, a local broadcaster can be viewed as an "upstream firm" that sells the input of retransmission consent to MPVDs which are "downstream firms" that combine this input with other inputs to produce the final product of MVPD service that is sold to consumers. Thus, from an economic perspective, the case of retransmission consent appears to be a situation where larger buyers are able to extract lower input prices from a supplier than are smaller buyers. There are a number of papers in the economics literature that investigate the general issue of whether and why we might expect large buyers to be able to negotiate lower input prices than smaller buyers.[10] John Kenneth Galbraith coined the term "countervailing power" to describe this phenomenon and this is often the term used to describe it in the economics literature.[11] Both the theoretical and empirical literature suggest that the exercise of counterveiling power may occur in some input markets but may not occur in others depending upon the particular combination of economic factors present in any given market.

One factor identified by the literature that will tend to generate discounts for large buyers is risk aversion on the part of the seller.[12] If the seller is risk averse, he will view the threat of a

[9]CRS Report at 13

[10]For an extensive discussion of both the theoretical and empirical literature see Snyder, Christopher, "Countervailing Power," *The New Palgrave Dictionary of Economics,* second edition, Steven N. Durlauf and Lawrence E. Blume, eds., Palgrave Macmillian, 2008. Also, see Normann, Hans-Theo, Bradley J. Ruffle, and Christopher M. Snyder, "Do Buyer Size Discounts Depend on the Curvature of the Surplus Function," *Rand Journal of Economics, 38, 2007, 747-767* for a demonstration that such effects can occur in a laboratory situation.

[11] Galbraith, J. K., *American Capitalism: The Concept of Countervailing Power,*" Boston: Houghton Mifflin, 1982.

[12] For example, see Snyder (2008) which explains this theory and attributes it to DeGraba,

large loss of business as much more serious than the threat of a small loss of business. Since larger buyers can threaten a large loss of business, this gives them more bargaining power. I believe that the explanations of industry observers that I have quoted above can be interpreted as identifying precisely this factor.

In the particular case of retransmission consent, I believe that there is another closely related issue that may also partially explain why smaller MVPDs have less bargaining power than larger MVPDs, which I will refer to as a "threshold effect." When a local broadcaster and MVPD are unable to come to an agreement, the threat of the MVPD is to temporarily withdraw carriage until an agreement is reached. In the short run the broadcaster will generally have already sold all of its advertising time and the short run threat to the broadcaster's profit is that advertisers may notice the temporary withdrawal of carriage and go to the trouble of attempting to negotiate some sort of adjustment with the local broadcaster to reflect the reduced viewership. While such negotiations are almost certain to happen when the broadcaster loses carriage on an MVPD serving a significant share of its market, they are much less likely to happen when the broadcaster loses carriage on an MVPD serving an insignificant share of its market. To the extent that advertisers do not demand adjustments for short-term withdrawals of carriage on MVPDs below some threshold size, the cost to the broadcaster of a short term withdrawal of carriage by such MVPDs is zero. Any standard model of bargaining would predict that this would result in higher retransmission consent fees for the affected MVPDs.

Patrick, "Quantity Discounts from Risk Averse Sellers," U. S. Federal Trade Commission, mimeo, 2003 and Chae, S. and P. Heidhues, "Buyers' Alliances for Bargaining Power," *Journal of Economics and Management Strategy*, 13, 2004, 731-754.

3. AVAILABLE EVIDENCE SUGGESTS THAT SIGNIFICANT LEVELS OF PRICE DISCRIMINATION OCCUR IN RETRANSMISSION CONSENT AGREEMENTS

The universal use of non-disclosure clauses in retransmission consent agreements severely limits the amount of publicly available evidence on the magnitude of retransmission consent fees and how they vary between MVPDs of different sizes. Furthermore, the fact that retransmission fees paid by all MVPDs are still escalating rapidly over time makes it even more difficult to draw conclusions from the occasional reports of fee levels in the media or analysts' reports.

The only publicly available source of data that I am aware of on industry-wide levels of retransmission consent fees is from Kagan Research.[13] In particular, Kagan has very recently published 2010 projections for retransmission consent payments broken down by MVPD type (cable, DBS, and telco) and 2010 projections for the number of MVPD subscribers by MVPD type. This data can therefore be used to calculate 2010 projected average per subscriber retransmission consent fees by MVPD type. Table 1 presents this data and the calculation of average per subscriber retransmission consent fees.

[13]Kagan Research, "Broadcast Retrans Fees on Track to Break $1 Billion by 2011," *Broadcast Investor: Deals & Finance,* June 30, 2009 reported in Tables 2 and 3 of Katz, Michael L., Jonathan Orzag, and Theresa Sullivan, "An Economic Analysis of Consumer Harm From the Current Retransmission Consent Regime," November 12, 2009, provided to the Commission as an attachment to the Comments of the National Cable & Telecommunications Association, MB Docket No. 07-269 (filed Dec. 16, 2009).

TABLE 1
2010 PER SUBSCRIBER RETRANSMISION CONSENT PAYMENTS
TO ALL BROADCAST STATIONS
BROKEN DOWN BY TYPE OF MVPD

MVPD Type	Total Retrans Payments (millions of $)	Total Subscribers (millions)	Per Subscriber Retrans Payments ($ per sub per month)
Cable	$424.0	62.1	$.57
DBS	$390.0	32.3	$1.01
Telco	$119.1	8.2	$1.21
All	$933.1	102.2	$.76

Source: Kagan Research (June 30, 2009) as reported in Tables 2 and 3 of Katz, Orzag, and Sullivan (November 12, 2009).

The last column in Table 1 gives total retransmission consent fees per subscriber per month paid to all broadcast stations by MVPD type. Since significant retransmission consent fees are typically only charged by affiliates of the Big 4 networks (i.e., ABC, NBC, CBS, and FOX), we can calculate the average per subscriber per month retransmission consent fee charged by an individual Big 4 station by dividing the numbers in the last column of Table 1 by 4. This yields the numbers reported in Table 2.

TABLE 2
2010 AVERAGE PER SUBSCRIBER RETRANSMISSION CONSENT PAYMENTS
TO A SINGLE BIG 4 STATION
BROKEN DOWN BY TYPE OF MVPD

MVPD Type	Per Subscriber Retrans Payments ($ per sub per month)
Cable	$0.14
DBS	$0.25
Telco	$0.30
All	$0.19

To interpret these numbers, note that although there are a large number of small and medium sized cable operators, they are completely dwarfed in size by the handful of large operators with the result that only a very small fraction of cable subscribers receive service from small or medium sized MVPDs. Therefore the average per subscriber retransmission consent payment made by cable MVPDs in Table 2 should be interpreted as being very close to the average amount paid by large cable operators.[14] In particular, then, consistent with the description of bargaining strength in Section 2, above, large cable operators pay the lowest per subscriber retransmission consent fees; on average they pay $.14 per subscriber per month to an individual Big 4 station. DBS providers pay the considerably higher amount of $.25 per subscriber per month and telcos pay the even higher amount of $.30 per subscriber per month. Thus, DBS providers pay retransmission consent fees that on average are 79% higher than those paid by large cable operators and telcos pay fees that are 114% higher than those paid by large cable operators.

The Kagan data does not directly provide any information about the fees paid by small and medium sized cable companies. However, given the general consensus that small and medium size cable companies pay retransmission fees that are at least as high as any other operators in the market, I believe that the average retransmission consent fee paid by telcos - i.e., $.30 per subscriber per month to an average Big 4 station - provides a reasonably conservative estimate of the average per subscriber retransmission consent fee paid by small and medium sized cable operators. Therefore, based on the above data, it appears that the average

[14]The best estimate of the amount paid by large cable operators would actually be somewhat smaller than the figure of $.14. Therefore the estimates of price differences provided below, which use the figure of $.14 as the amount paid by large cable operators, are actually somewhat conservative.

retransmission consent fee paid by small and medium sized cable operators is more than twice as high as the average retransmission consent fee paid by large cable operators. Representatives of the ACA have told me that, based on anecdotal evidence from their membership, they agree that $.30 per subscriber per month is likely a conservative estimate of the retransmission consent fee that the average small or medium sized MVPD pays to a single Big 4 station. In fact they are aware of numerous instances where their members currently pay retransmission consent fees as high as $.75 per subscriber per month to individual Big 4 stations.

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 continue to rise rapidly over the next few years. For example, Kagan Research reports that total retransmission consent fees rose from $214.6 million to $738.7 million between 2006 and 2009 and projects that they will climb to $1,283.5 million in 2012 and $1,630.0 million in 2015.[15] 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.

Finally it is also important to note that these price differences can NOT be justified by differences in costs of providing retransmission consent to different sized MVPDs. My understanding based on my conversations with ACA members, is that individual MVPDs generally make their own arrangements at their own cost to download the signals of broadcast networks to their headends. Thus retransmission consent fees are simply the fees that MVPDs pay for permission to carry the signals of broadcasters and broadcasters essentially incur no marginal costs of providing this permission to any MVPD. In particular, then, there is no cost

[15]Kagan Research (June 30, 2009) as reported in Katz, Orzag, and Sullivan (November 12, 2009).

difference to provide retransmission consent to different sized MVPDs.

4. 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 direct effect of price discrimination in this case, is simply to allow broadcasters to charge higher prices to MVPDs with less bargaining power.

5. 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

Standard economic principles suggest that a significant share of any increase in retransmission consent fees will be passed through to subscribers in the form of higher subscription prices. In particular, since retransmission consent fees are levied on a per subscriber basis, they represent a marginal cost of providing service to the MVPD, and we would normally expect a substantial share any increase in marginal costs to be passed on to consumers in the form of higher prices. For example, one recent study of cable prices found that, in general, about 50 percent of increases in programming costs were passed though to subscribers in the form of higher subscription fees.[16] In its evaluation of the News Corp./ DirecTV merger, the Commission itself concluded that higher programming fees are "passed on to consumers in the form of higher rates."[17] The FTC reached a similar conclusion in its evaluation of the Time Warner/Turner Merger.[18]

Since MVPDs pass higher programming costs back to their subscribers in the form of higher subscription fees, the main ultimate 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 broadcasters' 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 payments that help support the programming efforts of local

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[16]Ford, George S. And John D. Jackson, "Horizontal Concentration and Vertical Integration in the Cable Television Industry," *Review of Industrial Organization*, 12, 1997, 513-14.

[17]FCC, "Memorandum Opinion and Oder," *In the Matter of General Motors Corporation and Hughes Electronics Corporation, Transferors, and The News Corporation, Transferee, For Authority to Transfer Control*, MB Docket No. 03-124, December 19, 2003 at para. 208.

[18]See *Time Warner, Inc. et. al., Proposed Consent Agreement with Analysis to Aid Public Comment,* 61 Fed. Reg. 50301, 50309 (rel. Sept.25, 1999). "The complaint alleges . . . that substantial increases in wholesale programming costs for both cable systems and alternative providers - including direct broadcast satellite service and other forms of non-cable distribution - would lead to higher service prices."

broadcasters, the rationale for requiring the customers of small and medium sized 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.

6. POSSIBLE SOLUTIONS

The Commission could solve this problem by requiring broadcasters to make the same terms and conditions available to all MVPDs regardless of their size. Such requirements are typically referred to as most favored nation (MFN) requirements and, in fact, MFN clauses are a relatively standard type of clause and are already included in some existing programming contracts. MPVDs generally view an MFN clause as extremely desirable, and it is often the case that only MVPDs in the most powerful bargaining position are able to extract such clauses. Furthermore, as the clauses are currently used, they typically specify the number of subscribers the MVPD is paying for as one of the terms of the contract that must be matched in order to invoke the MFN clause. (That is, an MVPD with an MFN clause would only be able to opt into a lower rate offered another MVPD if it had at least as many subscribers as the MVPD receiving the lower rate.) However, the fact that firms in the industry already find inclusion of MFN clauses to be commercially practical in some cases, suggests that requiring the general use of such clauses is a feasible regulatory alternative for the Commission to consider.

The main potential difficulty in implementing this approach will be dealing with complex retransmission consent agreements that sometimes bundle numerous contractual obligations together in a single deal. For example, when a large MVPD with multiple systems located all across the country negotiates a retransmission consent deal with a network on behalf of its owned and operated (O&O) stations or with a large station group on behalf of the all the stations in its group, a single contract often specifies retransmission consent fees for all of the parties' broadcast stations and cable systems. Furthermore, especially with the case of O&O groups, the contracts also sometimes include carriage of additional national cable networks and/or RSNs under common ownership with the group of broadcast stations. Finally, the contracts sometimes specify other obligations of the MVPD, such as purchasing specified amounts of advertising from specified local broadcasters at specified prices.

The simplest and cleanest solution would be to require that retransmission consent for each local broadcaster be contracted for in a separate stand alone contract that other MVPDs could opt into. Note that this would not preclude large MVPDs and large station groups from conducting single master-negotiations in which they simultaneously established terms for all of the local broadcast stations owned by the group that operate in areas where the large MVPD is present. Rather, it would simply require that the terms for each local broadcaster be separately specified and that any other MVPD be able to opt into the terms for any individual local broadcaster. Note also, that some type of "stand alone" contracting will likely be required in any event if the Commission decides to adopt some version of the mandatory arbitration proposal suggested by the petitioners. This is because the mandatory arbitration clause will likely need to allow for arbitration on a station-by-station basis. Finally, it might well be possible to allow some sorts of bundling within a DMA such as allowing two jointly owned local broadcasters to be bundled together[19] or allowing other programming or advertising purchases to be bundled together with retransmission consent. An MFN clause would simply require the entire bundle to be made available at the same terms to other MVPDs operating in the area. Thus, although there will undoubtedly be some difficult details to work through, I expect that it would be both feasible and practical for the Commission to adopt a regulatory framework that required local broadcasters to make their signals available to all MVPDs on the same terms.

7. CONCLUSION

Significant levels of price discrimination occur in markets for retransmission consent. In particular, smaller operators with less bargaining power are charged higher retransmission consent fees than their larger competitors. This essentially means that customers of small and medium sized MVPDs are paying higher fees to support local broadcasters than are customers of larger MVPDs, which seems difficult to justify from a policy perspective. This problem could be addressed by requiring broadcasters negotiating retransmission consent agreements to make the same terms available to all MVPDs, regardless of their size.

[19]Note, however, that, as I discuss in my companion paper to this paper, “Joint Control or Ownership of Multiple Big 4 Broadcasters in the Same Market and its Effect on Retransmission Consent Prices,” being submitted by the ACA in this same proceeding, there are additional problems created by joint ownership or control of multiple Big 4 stations in the same DMA. In light of these problems, I would recommend that bundling of jointly owned local stations be limited to cases where at most one of the stations is a Big 4 affiliate.

Appendix B

Joint Control or Ownership of Multiple Big 4 Broadcasters in the Same Market and Its Effect on Retransmission Consent Fees

JOINT CONTROL OR OWNERSHIP OF
MULTIPLE BIG 4 BROADCASTERS IN THE SAME MARKET
AND ITS EFFECT ON
RETRANSMISSION CONSENT FEES*

by

William P. Rogerson**

May 18, 2010

***	Prepared for the American Cable Association**

****	Professor of Economics, Northwestern University. FCC Chief Economist, 1998-99.**

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1. 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 carry their signals. In response to a petition for rulemaking,[2] the Commission has asked for comments evaluating the performance of the current retransmission consent regime. The central argument in the petition for rulemaking is that changes in market structure that have occurred since the introduction of the current framework have fundamentally altered the balance of bargaining power in this industry in favor of broadcasters. As a result, the fees that broadcasters are able to charge for retransmission consent are rising to much higher levels than were ever originally contemplated when the rules were first introduced. These fee increases are of course passed through to subscribers in the form of higher subscription prices. A related problem is the increasing occurrence of temporary withdrawals of broadcast signals during negotiations in which broadcasters attempt to exercise their increased bargaining power. The petition for rulemaking suggests that the Commission consider allowing parties to request binding arbitration with mandatory interim carriage of signals to address these problems.

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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).

[2] Public Knowledge, DirecTV, Inc., DISH Network LLC, Charter Communications, Inc., American Cable Association, New America Foundation, OPASTCO, Time Warner Cable, Inc., Verizon, Cablevision Systems Corp., Mediacom Communications Corp., Bright House Networks, LLC, Insight Communications Company, Inc., and Suddenlink Communications ("Petitioners"), "Petition for Rulemaking," *Petition for Rulemaking to Amend the Commission's Rules Governing Retransmission Consent*, MB Docket No. 10-71, March 9, 2010.

I agree with the basic economic conclusions of the petitioners as I have described them above, and also agree that the direction of reform suggested by the petitioners is a sensible course of action for the Commission to consider.

The purpose of this paper is to describe a related but additional problem with the retransmission consent process and possible approaches to solving it, that I believe the Commission should also seriously consider as part of its over-all evaluation of whether and how the regulatory framework governing the retransmission consent process could be improved.[3] The problem arises because, in many local television markets, multiple Big 4 stations (i.e., affiliates of NBC, ABC, FOX, and CBS) are able to act as a single entity for purposes of negotiating retransmission consent prices. In some cases, this occurs because the stations are under common ownership. However, in other cases, this occurs because the stations enter into agreements to jointly negotiate retransmission consent prices, even though they are separately owned. This coordinated activity allows broadcast stations to negotiate higher retransmission consent fees than they would otherwise be able to, which are, in turn, passed on to consumers in the form of higher MPVD subscription prices.

In point form, the main arguments I make about this problem and possible approaches to solving it are as follows.

1. Although Commission rules generally prohibit common ownership of multiple Big 4 broadcasters in the same DMA, there are a number of instances where common ownership has been permitted through waivers or exceptions.

2. Separately owned Big 4 stations in the same DMA sometimes agree to jointly negotiate retransmission consent agreements. Such arrangements are often negotiated as part of

[3] I discuss an additional problem with the retransmission consent process in a companion paper also being submitted by the ACA in this proceeding entitled "The Economic Effects of Price Discrimination in Retransmission Consent Agreements."

more comprehensive sharing agreements, that transfer control of all or part of the operations of one station to the management of another station in the same DMA.

3. Standard economic theory suggests that, under plausible assumptions, when an entity jointly negotiates retransmission consent fees for multiple Big 4 stations in the same DMA, the entity will be able to charge higher prices than if the negotiations for each signal were conducted separately.

4. The evidence that is available suggests that joint ownership or control of multiple Big 4 stations in the same DMA does result in significantly higher retransmission consent fees.

5. Increased retransmission consent fees are passed through to MVPD subscribers in the form of higher subscription prices.

6. While there may be a good public policy rationale to require all MVPDs to make payments in support of the programming efforts of local broadcasters, it is hard to imagine a sound rationale for allowing broadcasters in some markets to extract higher payments than in other markets, based on whether they are able to enter into agreements with one another that essentially reduce the extent to which they compete with one another.

7. For separately owned broadcasters, this problem could be addressed by prohibiting them from jointly negotiating retransmission consent agreements, even if some of their operations are jointly controlled through sharing agreements.

8. Allowing parties to retransmission consent negotiations to request binding arbitration with mandatory interim carriage, as suggested by the petitioners in this proceeding, would limit the exercise of monopoly power due to joint ownership or joint control of multiple Big 4 stations in the same market.

9. On a going-forward basis, the Commission should take the harm of higher retransmission consent prices into account when it determines whether to permit exceptions or grant waivers that allow joint ownership of multiple Big 4 stations in the same market.

The remainder of the paper is organized as follows. Section 2 provides some background information on joint control and ownership of multiple Big 4 broadcasters in the same market. Section 3 shows that, under plausible assumptions, standard economic theory suggests that these types of arrangements will lead to higher retransmission consent fees. Section 4 argues that the evidence that is available suggests that these fees increases may be significant. Section 5 discusses possible approaches to solving the problem and section 6 draws a brief conclusion.

2. IN SOME LOCAL MARKETS MULTIPLE BIG 4 STATIONS ARE UNDER COMMON OWNERSHIP OR OPERATE UNDER JOINT CONTROL FOR PURPOSES OF NEGOTIATING RETRANSMISSION CONSENT AGREEMENTS

A single entity will negotiate retransmission consent agreements for multiple Big 4 stations in the same DMA if the stations are under common ownership or if the stations are separately owned but agree to operate under joint control for purposes of negotiating retransmission consent agreements.[4] Although Commission rules[5] generally prohibit common ownership of multiple Big 4 broadcasters in the same local market or DMA, there are a number of instances where common ownership has been permitted through waivers or exceptions. Separately owned Big 4 stations in the same DMA sometimes agree to jointly negotiate retransmission consent agreements. Such arrangements are often negotiated as part of more comprehensive sharing agreements that transfer control of all or part of the operations of one station to the management of another station in the same DMA.[6]

The ACA has combed through publicly available documents and records to compile as

[4]In this paper I will always use the term "joint control" to refer the situation where stations are separately owned but agree to operate under joint control for purposes of negotiating retransmission consent agreements. That is, "jointly controlled" should always be interpreted as meaning "separately owned but jointly controlled."

[5] See 47 C.F.R. 73.3555 which prohibits ownership of more than one of the four highest ranked stations in any DMA.

[6]These types of agreements are referred to using a number of different terms besides sharing agreements, including shared services agreements (SSAs), shared management agreements (SMAs) and local marketing agreements (LMAs). In this paper I will use the term sharing agreements as a generic term to refer to any arrangement where one station transfers control of all or part of its operations to the management of another station in the same DMA.

complete a listing as possible of all instances where pairs of Big 4 broadcast stations in the same DMA are under joint ownership or joint control.[7] To the best of my knowledge, this is the first time that such a list has ever been compiled and made publicly available. The data shows that these arrangements are very common. Table 1 in the ACA comments provides a listing of all instances where two Big 4 stations in the same DMA are under common ownership. There are 36 such instances. Table 2 provides a listing of all instances where two Big 4 stations in the same DMA operate under some sort of sharing agreement and thus are very likely to operate under joint control for purposes of negotiating retransmission consent agreements.[8] There are 57 such instances.

Thus, there are a total of 93 instances where multiple Big 4 stations in the same DMA are jointly owned or controlled. The total number of DMAs is equal to 210. Tables 1 and 2 can be used to track how the 93 instances of joint control or ownership are spread across these 210

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[7]Ownership or control of more than two Big 4 stations in the same DMA is quite rare. As can be seen from inspecting Tables 1 and 2, the ACA was able to identify 5 instances where three stations in the same DMA were under joint control or ownership. These markets are Youngstown, OH, Wheeling, WV-Steubenville,OH, Charlottesville, VA, Meridian, MS and Victoria, TX. All of the remaining instances of joint control or ownership of multiple stations in the same DMA involve only two stations.

[8]Although stations generally provide publicly available information regarding whether they operate under some sort of sharing agreement, they generally do not describe details of the arrangement in publicly available documents. Thus, it is generally not possible to specifically determine from publicly available documents whether or not the sharing agreement includes joint negotiation of retransmission consent agreements. Based on conversations with ACA members, I believe that in many cases sharing agreements provide for joint negotiation of retransmission consent prices. Furthermore, there may cases where stations agree to negotiate retransmission consent prices jointly but operate separately in all other respects. If such stations do not describe themselves as operating under a sharing agreement, they would not be included in Table 2 even though they do in fact jointly negotiate retransmission consent prices. Thus I believe that the number of stations publicly reporting sharing agreements provides a reasonably good and possibly even conservative estimate of the number of cases where retransmission consent prices are jointly negotiated.

DMAs. In particular, there are 16 DMAs with two instances of joint control or ownership[9] and 62 DMAs with one instance of joint control or ownership. Therefore, of the 210 DMAs, fully 78, or more than one third of them have one or two pairs of jointly owned or controlled Big 4 stations. The fact that these arrangements are so pervasive suggests that it is important that the Commission carefully evaluate their economic effects.

3. STANDARD ECONOMIC THEORY SUGGESTS THAT THESE ARRANGEMENTS RESULT IN HIGHER RETRANSMISSION CONSENT FEES WHICH ARE PASSED THROUGH TO CONSUMERS IN THE FORM OF HIGHER SUBSCRIPTION PRICES

When a programmer and MVPD negotiate the fee that the MVPD will pay the programmer, they are essentially deciding how to split the joint economic gains created from having the MVPD carry the programming. This sort of bilateral bargaining situation has been extensively modeled in the economics literature.[10] Application of the standard modeling approach used in the economics literature immediately demonstrates that a programmer selling two different programs will be able to charge more by bundling the programs together so long as

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[9]i.e., four instances of joint control or ownership occur in the same DMA when there are two pairs of Big 4 stations, with each pair being jointly owned or controlled by a different entity. The other 11 markets are Jacksonville, FL, Springfield, MO, Peoria-Bloomington, IL, Monroe, LA-El Dorado, AR, Erie, PA, Joplin, MO-Pittsburg, KS, Wichita Falls, TX-Lawton, OK, Sherman, TX-Ada, OK, Clarksburg-Weston, WV, Quincy, IL-Hannibal MO-Keokuk, IA, Bowling Green, KY.

[10]For general treatments of the bargaining problem see, for example, Harsanyi, John C., "Bargaining," *The New Palgrave Game Theory*, W.W. Norton, 1989; Alvin Roth *Axiomatic Models of Bargaining*, Springer-Verlag, 1979; and Ariel Rubinstein, "Perfect Equilibrium in a Bargaining Model," *Econometrica*, 50, 1982, 97-109. For an extended discussion of how this modeling approach can be interpreted to apply to the case of retransmission consent negotiations, see Katz, Michael L, Jonathan Orszag, and Theresa Sullivan, *An Economic Analysis of Consumer Harm from the Current Retransmission Consent Regime*, Nov. 12, 2009, provided to the Commission as an attachment to the Comments of the National Cable & Telecommunications Association, MB Docket No. 07-269 (filed Dec. 16, 2009).

the programs are substitutes in the sense that the marginal value of either of the programs to the MVPD is lower conditional on already carrying the other program.

A simple example will make this point clear. Suppose that an MVPD can carry two programs. Suppose that it would earn a profit of $1.00 per subscriber if it carried just one of the two programs and that is would earn a profit of $1.50 per subscriber if it carried both of the programs. Note that the marginal value of adding a program is $1.00 if the other program is not being carried, but is only equal to $.50 if the other program is already being carried. The programs are thus substitutes in the sense that the marginal value to the MVPD of either program is lower conditional on already carrying the other program. Note, in particular, that the fact that programs are substitutes does NOT mean that the MVPD only wishes to purchase one of the two programs. The MVPD will clearly make more profit if it carries BOTH programs. Nonetheless, the two programs are substitutes in the sense that the marginal value of carrying one of the programs is smaller conditional on the other program already being carried. To the extent that customers appreciate and are willing to pay for increases in variety at a diminishing rate as variety increases, we would expect this condition to hold.

To keep the example as simple as possible, assume that the programmer's cost of providing the program to the MVPD is zero so the joint gain if the MVPD carries the programming is simply equal to the MVPD's profit.[11] Also, assume that the MVPD and programmer have equal bargaining strength in the sense that they choose a price to evenly split

[11]It is easy to see that the example described below continues to yield the same conclusion if we assume that there is a cost of delivering the programming or if the programmer earns additional advertising revenue when the MVPD shows the programming.

the joint profit. [12]

First suppose two different programmers each own one of the two programs. Then, so long as the MVPD carries both networks in equilibrium, when the MVPD negotiates with either of the two programmers, the marginal profit of adding a program will be equal to $.50 per subscriber and the negotiated fee will therefore be equal to half this amount or $.25. Therefore the total fees paid for both programs will be $.50. Now suppose that the same programmer owns both programs. In this case the joint profit of adding both networks is equal to $1.50. Therefore, so long as the programmer sells both networks bundled together as a single item, the negotiated fee for the bundle will be half this amount or $.75.

Thus a single owner will be able to negotiate higher total fees than will two separate owners. The basic economic reason is simply that, when negotiations for each program occur separately, each programmer is only able to extract some share of the joint profit from adding the *last* program. However, when negotiations occur for a bundle of programs, the programmer is able to extract a share of the joint surplus from adding the *entire bundle*. So long as programs within the bundle are substitutes, the joint surplus from adding a bundle of both programs will be greater than twice the surplus from adding the last program.

Standard economic principles suggest that a significant share of any increase in retransmission consent fees will be passed through to subscribers in the form of higher subscription prices. In particular, since retransmission consent fees are levied on a per subscriber basis, they represent a marginal cost of providing service to the MVPD, and we would normally expect a substantial share any increase in marginal costs to be passed on to consumers

[12]It is easy to see that the example described below continues to yield the same conclusion if we assume that the programmer receives a share α of the total surplus where α is between 0 and 1.

in the form of higher prices. For example, one recent study of cable prices found that, in general, about 50 percent of increases in programming costs were passed though to subscribers in the form of higher subscription fees.[13] In its evaluation of the News Corp./ DirecTV merger, the Commission itself concluded that higher programming fees are "passed on to consumers in the form of higher rates."[14] The FTC reached a similar conclusion in its evaluation of the Time Warner/Turner Merger.[15]

4. THE AVAILABLE EVIDENCE SUGGESTS THAT THESE FEE INCREASES MAY BE SIGNIFICANT

Note that the effect on retransmission consent fees described above in Section 3 depends upon the property that the programs are substitutes for one another. To elaborate on this, two programs can be defined to be independent of one another if the value of adding one of the programs does not depend on whether or not the other program is being carried. Similarly, two programs can be defined to be complements for one another if the value of adding one of the programs is greater when the other program is being carried. For example, if the MVPD could earn a profit of $.75 per subscriber by carrying one program and $1.50 per subscriber by carrying

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[13]Ford, George S. And John D. Jackson, "Horizontal Concentration and Vertical Integration in the Cable Television Industry," *Review of Industrial Organization*, 12, 1997, 513-14.

[14]FCC, "Memorandum Opinion and Oder," *In the Matter of General Motors Corporation and Hughes Electronics Corporation, Transferors, and The News Corporation, Transferee, For Authority to Transfer Control,* MB Docket No. 03-124, December 19, 2003 at para. 208.

[15]See *Time Warner, Inc. et. al., Proposed Consent Agreement with Analysis to Aid Public Comment,* 61 Fed. Reg. 50301, 50309 (rel. Sept.25, 1999). "The complaint alleges . . . that substantial increases in wholesale programming costs for both cable systems and alternative providers - including direct broadcast satellite service and other forms of non-cable distribution - would lead to higher service prices."

both programs, the programs would be independent. Similarly, if the MPVD could earn a profit of $.50 per subscriber by carrying one program and $1.50 per subscriber by carrying both programs, the programs would be complements. While the general principle that consumers value variety at a diminishing rate suggests that it may generally be the case that programs are substitutes for one another to some extent, this general principle obviously does not necessarily suggest that this effect will be significant. Furthermore, it is obviously possible to also imagine circumstances in which programs might be complements.[16]

Therefore, while the argument in Section 3 certainly explains why it would not be surprising if we found that joint ownership or control of multiple Big 4 stations in the same DMA caused retransmission consent prices to be significantly higher, it does not prove that we would necessarily expect to find such a result. The theory simply tells us that there will be a significant empirical effect to the extent that the signals of the Big 4 networks are significantly substitutable for one another in the sense that the marginal cost to an MVPD of losing carriage of a Big 4 network would be higher if it had already lost carriage of another Big 4 network. Whether or not this effect is significant is an empirical issue.

The universal use of non-disclosure clauses in retransmission consent agreements severely limits the amount of publicly available evidence on the magnitude of retransmission consent fees and how they vary with market structure. The only publicly available evidence on this question that I am aware of is from a recent filing of the MVPD Suddenlink with the Commission that reports the results of a study that it did on how the magnitude of retransmission

[16]For example, if subscribers were never willing to subscribe to an MVPD unless it carried both programs, then the programs would be complements.

consent fees that it pays for Big 4 stations is affected by the ownership/control status of the stations. It reports finding the following results.

> "Suddenlink has examined its own retransmission consent agreements and has concluded that, where a single entity controls retransmission consent negotiations for more than one 'Big 4' station in a single market, the average retransmission consent fees Suddenlink pays for such entity's "Big 4' stations (in all Suddenlink markets where the entity represents one or more stations) is 21.6% higher than the average retransmission consent fees Suddenlink pays for other 'Big 4' stations in those same markets. This is compelling evidence that an entity combining the retransmission consent efforts of two 'Big 4' stations in the same market is able to secure a substantial premium by leveraging its ability to withhold programming from multiple stations."[17]

While this is only one data point, I think that, at a minimum, it should raise the Commission's concern**,** especially in light of the fact that such an outcome is completely consistent with the predictions of standard economic theory under plausible circumstances. If the Commission decides to further investigate the issue of retransmission consent as part of a rulemaking proceeding, I think that it would very useful to encourage other parties to report the results of conducting their own Suddenlink-like analysis of their fee data.

It is also worth noting that the Department of Justice (DOJ) has brought at least one anti-trust action based on the theory that combined control of multiple Big-4 stations in the same market will result in anti-competitive increases in retransmission consent fees. In particular, on February 6, 1996 the DOJ filed a complaint alleging that three of the Big 4 stations in the Corpus Christi DMA had illegally colluded to raise retransmission consent fees by entering into an agreement to jointly negotiate these fees. In response the three firms entered into a settlement

[17] Suddenlink Communications, "Ex Parte Comments of Suddenlink Communications in Support of Mediacom Communications Corporation's Retransmission Consent Complaint," *Mediacom Communications Corp., Complainant, v. Sinclair Broadcast Group, inc. Defendant,* CSR No 8233-C, 8234-M at 5.

agreement to halt this practice and refrain from such practices in the future.[18]

Finally, in its recent comprehensive report on retransmission consent, the Congressional Research Service describes a large number of retransmission consent disputes if detail and offers the following qualitative observation.

> "In the earlier section presenting specific examples of programmer-distributor conflicts, it was striking how often the broadcaster involved in a dispute owned or controlled more than one broadcast station in a small or medium sized market. It appears that where a broadcaster owns or controls two stations that are affiliated with major networks, that potentially gives that broadcaster control over two sets of must-have programming and places a distributor, especially a relatively small cable operator, in a very weak negotiating position since it would be extremely risky to lose carriage of both signals."[19]

5. POSSIBLE SOLUTIONS

While there may be a good public policy rationale to require all MVPDs to make payments in support of the programming efforts of local broadcasters, it is hard to imagine a sound rationale for allowing broadcasters in some markets to extract higher payments than broadcasters in other markets, based on whether they are able to enter into agreements with one another that essentially reduce the extent to which they compete with one another.

The problem of separately owned broadcasters that jointly negotiate retransmission consent agreements could be addressed simply by prohibiting them from jointly negotiating retransmission consent agreements, even if some aspects of their operations were jointly controlled through sharing agreements. It would be important that the regulation prohibit both formal and informal agreements to jointly negotiate. In order to make informal agreements less

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[18]*United States of America v. Texas Television, Inc., Gulf Coast Broadcasting Company, and K-Six Television, Inc.,*

[19]*CRS Report, id*, page 70.

likely, the Commission could consider prohibiting broadcasters participating in any sharing agreement from discussing or exchanging information of any sort about retransmission consent agreements.

A somewhat analogous approach for the case of commonly owned Big 4 stations in the same DMA would be to require the common owner to separately negotiate separate stand-alone retransmission consent agreements for each station. However, to the extent that a single owner was still negotiating both agreements and was, by virtue of this, always aware of the status of both sets of negotiations, it is not clear that simply requiring the single owner to ultimately sign two separate agreements and to avoid explicitly linking the results of the two negotiations would necessarily have much effect on negotiations. One way to insure that the negotiations would be more separate would be to require the owner to assign different teams that were not allowed to communicate with one another to each negotiation. If the Commission determined that such an approach would be workable and that it could limit bargaining power arising from common ownership of multiple Big 4 stations in the same market, this would also be worth consideration.

Note also that the recommendation of the petitioners in this proceeding to allow parties the right to request binding arbitration would also likely limit the exercise of monopoly power due to joint ownership or joint control of multiple Big 4 stations. This is because the arbitrator could use prices determined in markets with no joint ownership or control to determine a benchmark price.

Finally, on a going-forward basis, the Commission should consider taking the harm of higher retransmission consent prices into account when it determines whether to permit exceptions or grant waivers that allow joint ownership of multiple Big 4 stations in the same market.

6. CONCLUSION

In some local television markets multiple Big 4 stations are under joint ownership or operate under joint control for purposes of negotiating retransmission consent agreements. These arrangements increase retransmission consent fees which are passed through to consumers in the form of higher MVPD subscription prices. In markets where all of the Big 4 stations are separately owned, this problem could be prevented simply by requiring separately owned stations to separately negotiate retransmission consent agreements, even if some aspects of their operations are jointly controlled through sharing agreements. Also, the policy approach suggested by petitioners in this rulemaking, to allow parties negotiating retransmission consent agreements to request binding arbitration, would likely limit the exercise of market power due to joint ownership or joint control, since fees in markets without joint ownership or control could be used as benchmarks.

Appendix C

36 Identified Instances of Common Ownership of Multiple Big 4 Affiliates in the Same Market

57 Identified Instances of Common Control of Multiple Big 4 Network Stations in the Same Market

36 Identified Instances of Common Ownership of Multiple Big 4 Affiliates in the Same Market

			Station or Signal #1		Station or Signal #2	
DMA	DMA Rank	Station(s) Owner	Call Letters	Affil.	Call Letters	Affil.
Raleigh-Durham (Fayetteville), NC#	26	Capital Broadcasting	WRAL	CBS	WRAZ	FOX
Grand Rapids-Kalamazoo-Battle Creek, MI#	41	LIN Media	WOOD	NBC	WOTV	ABC
Norfolk-Portsmouth-Newport News, VA#	43	LIN Media	WAVY	NBC	WVBT	FOX
Albuquerque-Santa Fe, NM#	44	LIN Media	KASA	FOX	KRQE	CBS
Jacksonville, FL#	47	Gannett Co.	WJXX	ABC	WTLV	NBC
Santa Barbara-Santa Maria-San Luis Obispo, CA#	120	Cowles Media	KKFX	Fox	KCOY	CBS
Binghamton, NY#	157	Newport Television LLC	WIVT	ABC	WBGH-CA	NBC
Clarksburg-Weston, WV#	168	Withers Broadcasting Co.	WDTV	CBS	WVFX	FOX
Meridian, MS#	185	Michael Reed (WGBC-TV)	WGBC 30.1	FOX	WMDN	CBS
North Platte, NE+	209	Hoak Media Corp.	KNOP	NBC	K11TW	FOX
Beaumont-Port Arthur, TX*	141	London Broadcasting Co.	KBMT 12.1	ABC	KBMT 12.2	NBC
Salisbury, MD*	144	Draper Holdings Business Trust	WBOC 16.1	CBS	WBOC 21.2	FOX
Bluefield-Beckley-Oak Hill, WV*	156	West Virginia Media Holdings	WVNS 59.1	CBS	WVNS 59.2	FOX
Wheeling, WV-Steubenville, OH*	159	West Virginia Media Holdings	WTRF 7.1	CBS	WTRF 7.2 & 7.3	FOX & ABC
Sherman, TX-Ada, OK*	161	Gray Television	KXII 12.1	CBS	KXII 12.3	FOX
Sherman, TX-Ada, OK*	161	Lockwood Broadcasting Group	KTEN 10.1	NBC	KETN 10.3	ABC
Yuma, AZ-El Centro, CA*	164	News-Press & Gazette Co.	KECY 9.1	FOX	KECY 9.2	ABC
Clarksburg-Weston, WV*	168	West Virginia Media Holdings	WBOY 12.1	NBC	WBOY 12.2	ABC
Quincy, IL-Hannibal, MO-Keokuk, IA*	171	Barrington Broadcasting Group	KHQA 7.1	CBS	KHQA 7.2	ABC
Quincy, IL-Hannibal, MO-Keokuk, IA*	171	Quincy Newspapers	WGEM 10.1	NBC	WGEM 10.3	FOX
Harrisonburg, VA*	178	Gray Television	WHSV 3.1	ABC	WHSV 3.2	FOX
Alexandria, LA*	179	Hoak Media Corp.	KALB 5.1	NBC	KALB 5.2	CBS
Marquette, MI*	180	Barrington Broadcasting	KLUC 6.1	NBC	KLUC 6.2	FOX
Bowling Green, KY*	182	Gray Television	WBKO 13.1	ABC	WBKO 13.2	FOX
Bowling Green, KY*	182	Max Media	WNKY-DT 40.1	NBC	WNKY-DT 40.2	CBS
Meridian, MS*	185	Michael Reed (WGBC-TV)	WGBC 30.1	FOX	WGBC 30.2	NBC
Greenwood-Greenville, MS*	187	Commonwealth Communications	WAGB 6.1	ABC	WAGB 6.2	FOX

#Common Ownership Thru Duopoly w/ Full Power Station

@Common Ownership Thru Duopoly w/ Low Power Station

+Common Ownership Thru Duopoly w/ Class A Station

*Common Ownership Achieved Thru a Primary Video and Multicast Stream

36 Identified Instances of Common Ownership of Multiple Big 4 Affiliates in the Same Market

			Station or Signal #1		Station or Signal #2	
DMA	DMA Rank	Station(s) Owner	Call Letters	Affil.	Call Letters	Affil.
Parkersburg, WV[*]	194	Gray Television	WTAP 15.1	NBC	WTAP 15.2	FOX
Mankato, MN[*]	199	United Communications Corp.	KEYC 12.1	CBS	KEYC 12.2	FOX
Bend, OR[*@]	189	News-Press & Gazette Co.	KTVZ 21.1	NBC	WTVZ 21.3 (KFXO-LP)	FOX
Victoria, TX[*@]	204	Saga Communications	KAVU 25.1	ABC	KAVU 25.2 (KMOL-LP)	FOX
Charlottesville, VA[*@]	183	Gray Television	WCAV 19.1	CBS	WCAV 19.3 (WAHU-LP)	FOX
Topeka, KS[*+]	136	New Vision Television	KSNT 27.1	NBC	KSNT 27.2 (KTMJ-CA)	FOX
Palm Springs, CA[*+]	142	News-Press & Gazette Co.	KESQ 42.1	ABC	KESQ 33.2 (KDFX-CA)	FOX
Charlottesville, VA[*@]	183	Gray Television	WVAW-LD 16.1	ABC	WVAW-LD 16.2 (WCAV 19.1)	CBS
Youngstown, OH[*@]	110	New Vision Television	WKBN 27.1	CBS	WKBN 27.2 (WYFX-LP)	FOX

[#]Common Ownership Thru Duopoly w/ Full Power Station

[@]Common Ownership Thru Duopoly w/ Low Power Station

[+]Common Ownership Thru Duopoly w/ Class A Station

*Common Ownership Achieved Thru a Primary Video and Multicast Stream

57 Identified Instances of Common Control of Multiple Big 4 Network Stations in the Same Market

		Station #1			Station #2		
DMA	DMA Rank	Owner (**also Controlling Entity**)	Call Letters	Affil.	Owner	Call Letters	Affil.
Columbus, OH	34	Sinclair Broadcast Group	WSYX	ABC	Cunningham Broadacsting Corp.	WTTE	FOX
Jacksonville, FL	47	Newport Television	WAWS	FOX	High Plains Broadcasting	WTEV	CBS
Providence, RI-New Bedford, MA	53	LIN TV Corp	WPRI	CBS	WNAC	WNAC	FOX
Wilkes Barre-Scranton, PA	54	NexStar Broadcasting Group	WBRE	NBC	Mission Broadcasting	WYOU	CBS
Charleston-Huntington, WV	63	Sinclair Broadcast Group	WCHS	ABC	Cunningham Broadacsting Corp.	WVAH	FOX
Ft. Myers-Naples, Fl	64	Waterman Broadcasting Co.	WBBH	NBC	Montclair Communications, Inc.	WZVN	ABC
Dayton, OH	65	Sinclair Broadcast Group	WKEF	ABC	Cunningham Broadacsting Corp.	WRGT	FOX
Honolulu, HI	71	Raycom Media	KHNL	NBC	MCG Capital	KGMB	CBS
Springfield, MO	74	Schurz Communications	KYTV	NBC	Perkin Media	KSPR	ABC
Springfield, MO	74	NexStar Broadcasting Group	KSFX	FOX	Mission Broadcasting	KOLR	CBS
Rochester, NY	80	NexStar Broadcasting Group	WROC	CBS	Sinclair Broadcast Group	WUHF	FOX
Syracuse, NY	83	Barrington Broadcasting	WSTM	NBC	Granite Broadcasting Crop.	WTVH	CBS
Cedar Rapids-Waterloo-Iowa City and Dubuque, IA	88	Sinclair Broadcast Group	KGAN	CBS	Second Generation Iowa	KFXA	FOX
Tri-Cities, TN-VA	93	Bonten Media Group	WCYB	NBC	Esteem Broadcasting of North Carolina	WEMT	FOX
Burlington, VT-Plattsburgh, NY	94	Smith Media	WFFF	FOX	Lambert Broadcasting of Burlington	WVNY	ABC
Baton Rouge, LA	95	Communication Corp of America	WGMB	FOX	White Knight Broadcasting	WVLA	NBC
Savannah, GA	96	New Vision Television	WJCL	ABC	Parkin Broadcasting	WTGS	FOX
El Paso, TX	98	Communication Corp of America	KTSM	NBC	Titan TV	KDBC	CBS
Ft. Smith-Fayetteville-Springdale-Rogers, AR	100	NexStar Broadcasting Group	KNWA	NBC	NexStar Broadcasting Group	KFTA	FOX
Johnstown-Altoona, PA	101	Peak Media	WWCP	FOX	Palm Television	WATM	ABC
Greenville-New Bern-Washington, NC	103	Bonten Media Group	WCTI	ABC	Esteem Broadcasting of North Carolina	WFXI	FOX
Lincoln and Hastings-Kearney, NE	105	Pappas Telecasting	KWNB	ABC	Omaha World-Herald	KFXL	Fox
Fort Wayne, IN	107	Granite Broadcasting Corp.	WISE	NBC	Malara Broadcasting Group	WPTA	ABC
Tyler-Longview(Lufkin and Nacogdoches), TX	109	Communication Corp of America	KETK	NBC	White Knight Broadcasting	KFXK	Fox
Youngstown, OH	110	New Vision Television	WKBN 27.1	CBS	Parkin Broadcasting	WYTV	ABC
Augusta, GA	114	Media General	WJBF	ABC	Schurz Communications	WAGT	NBC
Peoria-Bloomington, IL	116	Granite Broadcasting Crop.	WEEK	NBC	Barrington Broadcasting	WHOI	ABC
Peoria-Bloomington, IL	116	NexStar Broadcasting Group	WMBD	CBS	Sinclair Broadcast Group	WYZZ	FOX

57 Identified Instances of Common Control of Multiple Big 4 Network Stations in the Same Market

		Station #1			Station #2		
DMA	DMA Rank	Owner (**also Controlling Entity**)	Call Letters	Affil.	Owner	Call Letters	Affil.
Traverse City-Cadillac, MI	117	Barrington Broadcasting	WPBN	NBC	Tucker Broadcasting of Traverse City	WGTU	ABC
Fargo-Valley City, ND	121	Hoak Media Corp.	KVLY	NBC	Parker Broadcasting	KXJB	CBS
Monterey-Salinas, CA	124	Cowles Publishing	KION	CBS	Seal Rock Broadcasters	KCBA	Fox
Columbus, GA	128	Raycom Media	WTVM	ABC	Southeastern Media Holdings	WXTX	FOX
Corpus Christi, TX	129	Cordillera Communications	KRIS	NBC	Eagle Creek Broadcasting	KZTV	CBS
Amarillo, TX	131	NexStar Broadcasting Group	KAMR	NBC	Mission Broadcasting	KCIT	FOX
Wilmington, NC	132	Raycom Media	WECT	NBC	Southeastern Media Holdings	WSFX	FOX
Rockford, IL	134	NexStar Broadcasting Group	KQRF	FOX	Mission Broadcasting	WTVO	ABC
Monroe, LA-El Dorado, AR	138	Hoak Media Corp.	KNOE	CBS	Parker Broadcasting	KAQY	ABC
Monroe, LA-El Dorado, AR	138	NexStar Broadcasting Group	KARD	FOX	Mission Broadcasting	KTVE	NBC
Duluth, MN-Superior, WI	139	Granite Broadcasting Crop.	KBJR & KRII	NBC	Malara Broadcast Group	KDLH	CBS
Lubbock, TX	143	NexStar Broadcasting Group	KLBK	CBS	Mission Broadcasting	KAMC	ABC
Erie, PA	146	NexStar Broadcasting Group	WJET	ABC	Mission Broadcasting	WFXP	FOX
Erie, PA	146	SJL of Pennyslvania	WICU	NBC	Lilly Broadcasting	WSEE	CBS
Joplin, MO-Pittsburg, KS	147	NexStar Broadcasting Group	KSNF	NBC	Mission Broadcasting	KODE	ABC
Joplin, MO-Pittsburg, KS	147	Saga Communications	KOAM	CBS	Surtsey Media	KFJX	FOX
Sioux City, IA	148	Titan Broadcast Group (TTBG)	KPTH	FOX	Waitt Broadcasting	KMEG	CBS
Wichita Falls, TX-Lawton, OK	149	NexStar Broadcasting Group	KFDX	NBC	Mission Broadcasting	KJTL	FOX
Wichita Falls, TX-Lawton, OK	149	Drewry Broadcast Group	KSWO	ABC	Hoak Media Corp.	KAUZ	CBS
Terre Haute, IN	152	NexStar Broadcasting Group	WTWO	NBC	Mission Broadcasting	WFXW	FOX
Rochester, MN-Mason City, IA-Austin, MN	153	Quincy Newspapers	NBC	KTTC	SagamorHill Broadcasting	KXLT	FOX
Idaho Falls-Pocatello, ID	162	Sunbelt Communications Co.	KPVI-DT	NBC	Compass Communications	KFXP	FOX
Abilene-Sweetwater, TX	165	NexStar Broadcasting Group	KTAB	CBS	Mission Broadcasting	KRBC	NBC
Billings, MT	169	NexStar Broadcasting Group	KSVI	ABC	Mission Broadcasting	KHMT	FOX
Utica, NY	170	NexStar Broadcasting Group	WFXV	FOX	Mission Broadcasting	WUTR	ABC
Grand Junction-Montrose, CO	184	Hoak Media Corp.	KREX	CBS	Parker Broadcasting	KFQX	CBS
San Angelo, TX	198	NexStar Broadcasting Group	KLST	CBS	Mission Broadcasting	KSAN	NBC
Ottumwa, IA-Kirksville, MO	200	Barrington Broadcasting	KTVO	ABC	Ottumwa Media Holdings	KYOU	FOX
Victoria, TX	204	Saga Communications	KAVU	ABC	Surtsey Media	KVCT	FOX