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August 20, 2010

Via USPS

Marlene Dortch
Secretary
Federal Communications Commission
9300 East Hampton Drive
Capitol Heights, MD 20743

Received & Inspected
AUG 26 2010
FCC Mail Room

Re: American Cable Association ("ACA") Reply to responses on the applications by Comcast Corporation, General Electric, and NBC Universal; MB Docket No. 10-56

Dear Ms. Dortch:

On behalf of ACA and in reference to above mentioned proceeding, we enclose a copy of ACA's Reply as filed electronically on August 19, 2010.

Please contact the undersigned with any questions.

Sincerely,

Alma Hoxha
Paralegal

Enclosures

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List A B C D E

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

Received & Inspected
AUG 2 8 2010
FCC Mail Room

In the Matter of	)	
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Applications of Comcast Corporation, General Electric Company, and NBC Universal, Inc., to Assign and Transfer Control of FCC Licenses	)	MB Docket No. 10-56
	)	

American Cable Association

REPLY

Pursuant to the Public Notice issued by the Federal Communications Commission ("FCC" or "Commission") in the above-captioned proceeding on March 16, 2010,[1] the American Cable Association ("ACA"),[2] by its attorneys, hereby files its Reply to responses on the applications by Comcast Corporation ("Comcast"), General Electric Company ("GE") and NBC Universal ("NBCU") (hereinafter referred to jointly as the "Applicants") for consent to assign and transfer control of certain

[1] *Commission Seeks Comment on Applications Filed by Comcast Corporation, General Electric Company and NBC Universal, Inc. to Assign and Transfer Control of FCC Licenses*, Public Notice, DA 10-457, MB Docket No. 10-56 (rel. Mar. 18, 2010) ("Public Notice").

[2] The ACA represents approximately 900 small and medium-sized cable companies serving mostly smaller markets and rural areas throughout the United States. ACA's membership encompasses a wide 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. Together, these companies serve more than 7.6 million households and businesses. All ACA members transact with Comcast, NBCU and their affiliates for "must have" cable and broadcast programming, and other popular and important video offerings.

local broadcast stations end RSNs, and commercial arbitration for all programming. The ACA then proposes three critical measures to ensure that smaller MVPDs can effectively employ these remedies. The following summarizes the key features of these two integrated proposals:

1. General Remedies to Address Increases in Programming Prices

- The program access rules shall be applied to Comcast-NBCU's sale of its broadcast stations and its other programming regardless of the means by which any of the programming is delivered to subscribers (e.g. online and mobile).

- Comcast-NBCU must sell each NBC O&O and each Comcast RSN on a stand-alone basis to all MVPDs. This remedy will significantly decrease the complexity and cost of commercial arbitration, including the proposed special commercial arbitration process for smaller operators.

- Comcast-NBCU is subject to a commercial arbitration process to ensure that it does not sell programming – broadcast stations, RSNs, and national cable networks – at a price that exceeds fair market value.

2. Special Provisions to Ensure Remedies are Useful for Smaller MVPDs

- MVPDs with fewer than 125,000 MVPD subscribers in the relevant market cannot be charged more than 5% higher than the lowest Net Effective Rate charged to other MVPDs for NBC O&Os and Comcast RSNs. To ensure transparency and assist in enforcing this right, Comcast-NBCU and Comcast must file annual certifications.

- To enable smaller MVPDs to enforce their ability to access NBC O&Os and Comcast RSNs at competitive rates, a new, lower-cost arbitration process with an automatic right of continued carriage is established.

- Comcast-NBCU must negotiate in good faith with Bargaining Agents, and these agents shall have comparable rights to MVPDs to obtain programming from Comcast-NBCU.

Finally, to ensure the remedies adequately address the harms and reflect the dynamic of the programming market and other carriage agreements entered into by the Applicants with other parties to the FCC's proceeding, they should remain in effect for 9 years.

SUMMARY

From the time the proposed combination of Comcast and NBCU was announced some eight months ago, the ACA has sought to precisely assess the competitive harms and provide empirical evidence as to their nature and magnitude. The ACA appreciates that the Commission too is conducting a very serious, fact-driven review. After all, the proposed combination is a "big deal," whose harmful effects will be widespread and extensive.

This Reply filing represents the final part of the ACA's case that without sufficient relief, the Commission cannot find the proposed combination is in the public interest. In its initial comments, the ACA demonstrated that the proposed transaction, if consummated, would have significant deleterious horizontal and vertical competitive effects. In its July 21, 2010 filing responding to the initial comments, the ACA, using documents submitted by the Applicants pursuant to the Commission's directive buttressed its arguments and the conclusion that, if the proposed combination were permitted, significant competitive harms would result and therefore the transaction should not be approved absent enforceable conditions sufficient to protect competition and consumer welfare. In this Reply, the ACA, relying on a new report from its economic expert, Professor William Rogerson, first addresses and rebuts arguments raised by the Applicants and their economists in their response to comments. Second, the ACA, again using the Rogerson Report, sets forth proposed conditions that the Applicants would need to adopt to ameliorate the harms caused by the proposed transaction, including by enabling smaller MVPDs to enforce any rights provided in the remedies either directly or through a bargaining agent.

At its core, the ACA's remedies ensure that MVPDs – especially smaller MVPDs – can carry NBCU's broadcast stations, its cable networks and Comcast's RSNs at rates, terms, and conditions reflecting pre-combination conditions. To achieve this aim, the ACA first proposes general measures most of which were either used in or based upon previous Commission decisions. These measures, which apply generally to all MVPDs, include expanding the reach of the program access rules to cover all programming sold by Comcast-NBCU and all platforms by which MVPDs may distribute that programming, the stand-alone sale by Comcast-NBCU of

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REPLY

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August 19, 2010

spectrum licenses to a new limited liability company that would constitute a joint venture of GE and Comcast ("Joint Venture").[3] The ACA explained in its initial comments that the proposed transaction, if consummated, would have significant deleterious horizontal and vertical competitive effects.[4] In its July 21, 2010 filing responding to the initial comments,[5] the ACA demonstrated that documents submitted by the Applicants pursuant to the Commission's directive[6] buttressed its arguments and the conclusion that, if the proposed combination were permitted, significant competitive harms would result and therefore the transaction should not be approved absent enforceable conditions sufficient to protect competition and consumer welfare. In this Reply, the ACA, relying on a new report from its economic expert, Professor William Rogerson,[7] first addresses and rebuts arguments raised by

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[3] *In the Matter of Applications of Comcast Corporation, General Electric Company and NBC Universal, Inc. For Consent to Assign Licenses or Transfer Control of Licensees*, Applications and Public Interest Statement (filed Jan. 28, 2010) ("Application").

[4] *In the Matter of Applications of Comcast Corporation, General Electric Company, and NBC Universal, Inc., to Assign and Transfer Control of FCC Licenses*, MB Docket No. 10-56, Comments of the American Cable Association (filed June 21, 2010) ("ACA Initial Comments"). ACA's initial comments included a report from its economist, Professor William Rogerson, analyzing the nature and extent of horizontal and vertical harm that would result from the proposed combination. William P. Rogerson, "Economic Analysis of the Competitive Harms of the Proposed Comcast-NBCU Transaction," June 21, 2010 ("Rogerson I").

[5] *In the Matter of Applications of Comcast Corporation, General Electric Company, and NBC Universal, Inc., to Assign and Transfer Control of FCC Licenses*, MB Docket No. 10-56, Response to Comments of the American Cable Association (filed July 21, 2010) ("ACA Response Comments").

[6] Letter from William T. Lake, Chief, Media Bureau, to Michael H. Hammer, Esquire, James H. Casserly, Esquire, Michael D. Hurwitz, Esquire, Brien C. Bell, Esquire, Willkie Farr & Gallagher LLP, Counsel for Comcast Corporation, MB Docket 10-56, May 21, 2010; Letter from William T. Lake, Media Bureau, to Bryan N. Tramont, Esquire, Kenneth E. Satten, Esquire, David H. Solomon, Esquire, Natalie G. Roisman, Esquire, Wilkinson Barker Knauer, LLP, Counsel for NBC Universal, Inc., MB Docket No. 10-56, May 21, 2010.

[7] William P. Rogerson, "A Further Economic Analysis of the Proposed Comcast-NBCU Transaction," Aug. 19, 2010, attached hereto as Attachment A ("Rogerson II").

the Applicants and their economists in their response to comments.[8] Second, the ACA, again using Rogerson II, sets forth proposed conditions that the Applicants would need to adopt to ameliorate the harms caused by the proposed transaction. These conditions, which operate as an integrated package, will protect consumers from higher prices and the loss of programming that otherwise would result from the transaction.

I. A BRIEF REVIEW OF THE COMPETITIVE HARMS CAUSED BY THE PROPOSED COMBINATION.

Horizontal Harm:[9] The proposed combination creates horizontal competitive concerns because key programming assets now separately owned by NBCU and Comcast – NBCU's 10 Owned & Operated ("O&O") and affiliated broadcast television stations, its block of national cable programming and Comcast's 9 Regional Sports Networks ("RSNs") -- will be joined post-transaction. Moreover, these assets, which are "must have" programming, are substitutes in the sense that the value of one network to a multichannel video programming distributor ("MVPD") is lower conditional on already carrying the other network. Under standard economic theory, if two different programmers own two different networks (or blocks of networks) that each create market power, combined ownership of both will generally create

[8] *In the Matter of Applications of Comcast Corporation, General Electric Company, and NBC Universal, Inc., to Assign and Transfer Control of FCC Licenses*, MB Docket No. 10-56, Opposition to Petitions to Deny and Response to Comments, Comcast Corporation, General Electric Company, NBC Universal, Inc. (filed July 21, 2010) ("Applicants' Opposition"). The Applicants' Opposition includes two exhibits: Exhibit 1, Gregory L. Rosston, Ph.D. and Michael D. Topper, Ph.D, "The Proposed Comcast-NBCU Transaction: Response to Comments and Petitions Regarding Competitive Benefits and Advertising Competition" (July 21, 2010); and, Exhibit 2, Mark Israel and Michael L. Katz, "Economic Analysis of the Proposed Comcast-NBCU-GE Transaction" (July 20, 2010) ("Israel/Katz Report").

[9] *See* ACA Initial Comments at 18-25.

significant additional market power. That is what would occur from the proposed combination of NBCU's and Comcast's programming assets, which would allow the new Joint Venture to charge much higher programming fees. These fee increases will be substantially passed through to subscribers in the form of higher subscription prices. In its prior comments, the ACA offered evidence in support of this claim and the magnitude of the harm.[10]

The greatest threat of horizontal harm from this proposed combination occurs in regions of the country served by an NBC O&O[11] and a Comcast RSN. In such regions, NBCU's control over retransmission consent for the NBC broadcast signal and control over its popular national cable networks will be combined with Comcast's control over its RSN. Approximately 12.1% of all TV households in the United States,

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[10] The retransmission consent market supplies the best available evidence on the effect of combined ownership or control on programming fees. This is because retransmission consent markets are local and the extent to which multiple Big 4 stations in the same market are jointly owned or controlled varies from market to market. The available evidence suggests that joint control or ownership of multiple Big 4 stations in the same DMA can increase retransmission consent fees by 20% and possibly much more. This level exceeds the threshold for harm in the *Horizontal Merger Guidelines* used by the Department of Justice and the Federal Trade Commission.

The ACA's concern about the effects of Big 4 collusion leading to increased retransmission fees was recently echoed by the National Cable Telecommunications Association: "Permitting a broadcaster to negotiate retransmission consent on behalf of two stations in a market ...is likely to result in consumer harm rather than the pro-competitive efficiencies envisioned when LMAs were created. As Time Warner Cable explains, "[b]y aggregating their market power and negotiating in tandem instead of in competition with one another, broadcasters can more easily raise the price of retransmission consent and more effectively threaten to withhold their signals during negotiations." (Comments of the National Cable Telecommunications Association, MB Docket No. 09-182, July 26, 2010, at 4.)

[11] For purposes of assessing the extent of harm and discussing remedies in these comments, the term "NBC O&O" shall include NBC Owned and Operated broadcast television stations currently or in the future owned or controlled by Comcast-NBCU and any other NBC local television affiliate on whose behalf Comcast-NBCU negotiates retransmission consent agreements.

spread over six different metropolitan areas, are located in DMAs with these characteristics.[12]

The transaction also threatens horizontal harm in regions served by a Comcast RSN but not served by an NBC O&O. In such regions, NBCU's control over its popular national cable networks will be combined with Comcast's control over its RSN. Approximately 28% of TV households are located in designated market areas ("DMAs") with these characteristics. Therefore, regions containing at least 40% of all TV households are threatened with the horizontal harm from this transaction. The harm in fact may be even more widespread if the Applicants swap assets to aggregate programming in markets or if the Applicants are able to negotiate on behalf of NBCU affiliates for retransmission fees.[13]

Vertical Harm:[14] Vertical harm will arise from the proposed combination when the programming assets of NBCU are combined with Comcast's ownership of the country's largest MVPD. This union will increase Comcast-NBCU's ability to command higher programming fees from MVPDs that compete with Comcast. These fee increases will be substantially passed through to subscribers in the form of higher subscription fees.

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[12] These are Chicago, IL, Philadelphia, PA, San Francisco-Oakland-San Jose, CA, Washington, DC, Miami-Fort Lauderdale, FL, and Hartford and New Haven, CT.

[13] *See* ACA Response to Comments at 13-18 (a "review of the documents produced by Applicants demonstrates that in fact they recognize there is substantial overlap in the programming assets of Comcast and NBCU, that they intend to sell these assets in combination to MVPDs and that they are likely to add to them to increase the number of programming overlaps. In other words, Professor Rogerson's analysis *should be viewed as a conservative assessment of the post-transaction behavior in which the Applicants plan to engage and the impact such behavior is likely to have on MVPDs and subscribers.*") (emphasis added).

[14] *See* ACA Initial Comments at 25-37.

The economic theory underlying the ACA's analysis is as follows: So long as the Joint Venture and Comcast are able to coordinate their actions to take advantage of opportunities to maximize their combined profits, the Joint Venture and Comcast will collectively make decisions to maximize their combined profits. The reason that programming fees will rise is because the Joint Venture will seek to recoup through its negotiations for programming the opportunity cost of not acquiring new customers from rival MVPDs through the permanent withholding of programming. Increases in opportunity cost have the same impact on programming fees as increases in direct cost. In the absence of other information, a standard and well-accepted practice in economic theory is to predict that the negotiated price between a buyer and seller will rise by half the amount of any cost increase.

The impact of the transaction will be most significant in DMAs served by an NBC O&O where Comcast has a significant presence as the incumbent multichannel video programming distributor ("MVPD"). Approximately 12% of all TV households in the United States, spread over six metropolitan areas, are located in such DMAs, which happen to be the same markets that will also suffer the most significant horizontal harm from the transaction. Under plausible parameter values, the retransmission consent fees charged by NBC O&Os will increase by approximately 100% in these DMAs.

The transaction also would have a significant impact on the fees that the joint venture charges for NBCU's national cable networks. Under plausible parameter values, the fees for this programming will increase by approximately 18-20% for large

MVPDs who compete against Comcast, such as DirecTV, DISH Network, Verizon's FiOS service and AT&T's U-verse offering.

Cable overbuilders will experience higher programming fee increases to the extent that Comcast passes a high percentage of their subscribers. Under plausible parameter values, if Comcast passes almost all of an overbuilder's customers, its retransmission consent fees will increase by 100% and its fees for NBCU's national cable networks will increase by 44%. However, cable overbuilders will still experience significant price increases even if the share of their customers passed by Comcast drops to much more modest levels. ACA has identified 40 members who are Comcast rivals in all or some of their service areas.

II. THE APPLICANTS' AND THEIR ECONOMISTS DO NOT PROVIDE COGENT ARGUMENTS TO COUNTER THE CONCLUSION THAT THE PROPOSED COMBINATION WILL CAUSE SIGNIFICANT HORIZONTAL AND VERTICAL HARMS.

A. Horizontal Harm.

1. Introduction.

In Rogerson I, Professor Rogerson described how the horizontal combination of NBCU and Comcast programming networks would result in MVPDs paying higher prices "so long as the networks are substitutes for one another in the weak sense that the value of one network to an MVPD is lower conditional on already carrying the other network."[15] The economic rationale for this conclusion is that when negotiations for NBCU and Comcast networks occur separately, each can only

[15] *See* Rogerson I at 4-5 for a summary of the horizontal harms. The NBCU and Comcast programming networks can be substitutes even if subscribers have a strong preference to subscribe to a MVPD that carries both networks.

extract a limited share of the joint profit from adding the last network. However, when NBCU and Comcast combine networks, they will be able to extract the full share of the profit from adding the entire bundle, which will be greater then twice the surplus from adding just the last network. This result holds even if the NBCU and Comcast programming networks are not perfect or even relatively close to perfect substitutes and are merely partial substitutes.

Applicants' economists, Drs. Israel and Katz, attempt to rebut Professor Rogerson's analysis by making a series of claims that the NBCU and Comcast programming are not close substitutes and that empirical evidence shows that combining such networks does not raise prices. In the next section, the ACA, using the attached report by Professor Rogerson, responds to each of these arguments.

2. The arguments of the Applicants do not undermine the conclusion demonstrated by the ACA in its initial comments that horizontal harms will result from the proposed combination.

The Applicants' make five different arguments in attempting to counter the ACA's conclusion that the combination of NBCU and Comcast programming networks will lead to significently increased prices for consumers. In each instance, these shots fired by the Applicants either fall wide or short of their mark. Below the ACA, relying on Rogerson II, discusses each of the Applicants' arguments and shows that they do not undermine the conclusion that the proposed combination will result in substantial horizontal harms to MVPDs and their subscribers.

1. **Applicants' Contention:** "A basic review of the content carried suggests that Comcast's RSN's and NBC broadcast stations are not likely to be close substitutes."[16]

ACA Response: Drs. Israel and Katz present a much too narrow view of what constitutes substitutability. As Professor Rogerson states, "To the extent that substitutability between networks is caused simply by the fact that subscribers value increases in variety at a decreasing rate, it is perfectly possible and reasonable that two very different types of networks could be partial substitutes for one another in the sense that the value of adding one of the two networks decreases conditional on the other network already being carried." [17] In other words, subscribers may pay $1 extra to add either a sports or general entertainment network but, once one of those were added – and overall variety increased – subscribers would only be willing to pay a significant amount less than $1 to add the other network. Thus, contrary to the Applicants' claim, content alone is not sufficient to determine substitutability.

2. **Applicants' Contention**: "The Commission has previously found that RSNs, broadcast networks, and national cable networks 'differ significantly in their characteristics, focus, and subject matter,' and are imperfect substitutes that should be analyzed in separate 'categories.'"[18]

ACA Response: Drs. Israel and Katz seem to be asking the Commission to conclude that because it has stated that RSN programming differs significantly from programming on other networks, these other networks and the RSNs cannot be close substitutes. If that is the case, the ACA believes they are overstating the effect of the

[16] Israel/Katz Report, ¶ 111.

[17] Rogerson II at 27-28.

[18] Israel/Katz Report, ¶ 104.

Commission's finding as it applies to Professor Rogerson's analysis. As stated above, for Professor Rogerson's results to hold, the networks do not have to be perfect or near-perfect substitutes. Rather, it is sufficient that the networks be partial substitutes, and the Commission's previous statements do not foreclose such a finding.

> **3. Applicants' Contention:** "The demographic profiles of the NBC broadcast network and the Comcast RSNs look nothing like each other."[19]

ACA Response: Just because demographic profiles of viewers on different types of networks may differ does not necessarily mean that the networks are not substitutes. First, even assuming the demographic profiles of two types of networks differ, a substantial number of viewers may still watch both networks – and thus view the networks as partial substitutes. Second, most households (the decision making entity for procuring programming from a MVPD) have multiple viewers with different demographic profiles – and thus even if individual viewers may only watch one type of network, the overall household watches both types of networks, viewing them as substitutes.

> **4. Applicants' Contention:** "The transaction involves a relatively small share of television viewing and will not substantially increase the concentration of broadcast and cable networks combined, or cable networks on their own."[20]

ACA Response: Drs. Israel and Katz base their examination of concentration in the programming market on the share of total viewing hours that households devote –

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[19] Israel/Katz Report, ¶ 113.

[20] Israel/Katz Report, ¶ 109.

before and after the proposed combination -- to watching all the networks produced by a programmer. Using their approach, the shares are relatively low pre-combination and do not rise substantially post-combination, especially to the levels that normally concern antitrust authorities. While superficially plausible, this approach, as Professor Rogerson states, "completely ignores the Commission's own determination that calculating concentration ratios in this manner is not the correct way to assess the extent of market power in programming markets."[21] For example, their approach runs counter to the Commission's conclusion that programmers with RSNs or local broadcast networks have significant market power.

> **5. Applicants' Contention**: An empirical analysis of the combination of Fox's O&Os and its RSNs indicates that "on average, joint ownership by New Corporation had no significant effect on the level of RSN affiliate fees."[22]

ACA Response: The ACA does not disagree that the effects of the combination of Fox's O&Os and RSNs would provide a good indication of the potential harms that would result from the combination proposed by the Applicants. However, because no such evidence was available, the ACA presented the next best evidence – the effects of combining multiple Big 4 local broadcast stations – to make the general point that combined control of multiple networks (especially "must have" networks) can lead to higher programming fees. Using this evidance, the ACA showed that prices from the proposed combination would increase by 20% if not more.

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[21] Rogerson II at 30.

[22] Israel/Katz Report, ¶ 124.

To date, no one has attempted to analyze the pricing effects of combining Fox O&Os and RSNs. Professor Rogerson notes this is because there are "limitations in the amount and type of data available and the inherent impossibility of controlling for other factors that might affect RSN fees."[23] For example, it is well-known that the attractiveness of a RSN can change dramatically if a sports team enters into or walks away from a carriage agreement with the network. In addition, the ownership of a RSN may play a large role in determining prices, terms, and conditions and the type of programming carried. These and other variables may be viewed as not that significant -- that is, important to control -- if there are a very large number of events. However, if the data set is limited, controlling for these unusual events so that the results are credible becomes essential.

In their filing, Drs. Israel and Katz take on this daunting challenge. They gathered data and then analyzed the pricing effects of the Fox's O&O and RSN combinations. From this work, they concluded there is no substantial effect, that is, where combinations existed, prices did not rise significantly.

The flaws in the empirical analysis conducted by Drs. Israel and Katz are numerous and serious, and the Commission should not rely on its conclusion. To begin with, Drs. Israel and Katz have a limited data set -- "eleven transactions" that occurred between 2000 and 2009. Professor Rogerson, in the attached report, reviews each of these transactions.[24] First he finds that six of these transactions are

[23] Rogerson II at 32.

[24] Rogerson II at 33-37.

not suitable for analysis because they are based on a single post-transaction year of data, an especially troubling problem where most agreements between programmers and MVPDs are multi-year deals:

> The first thing to notice about this list of transactions is that six of the listed eleven transactions all occurred in 2008 when News Corp. sold a number of Fox O&Os. Since Drs. Israel and Katz have annual fee data from 1999-2009, this means that they only have one post-transaction year of data for RSN fees for these six transactions. Furthermore, it is typically the case that programmers and MVPDs sign multi-year agreements. Therefore it may well be the case that many of the RSN fees paid in 2009 were determined by contracts signed prior to News Corp.'s sale of the Fox affiliates. Therefore, in my judgment, these six transactions should not be included in the study.[25]

The remaining five transactions involve Fox purchasing a RSN. As discussed above, a change in ownership by itself can have dramatic effects on the objectives, operations, and content of – and, of course, carriage fees charged by – a RSN. One of these five transactions involved the purchase of Turner South, which aired both regional sports and non-sports programming. After Fox's purchase, the RSN changed programming line-ups and carried only regional sports programming. Another transaction involved Fox Sports Ohio, which just after its purchase by Fox in 2005 lost the rights to carry its anchor-tenant, the Cleveland Indians baseball games. It is likely that this occurrence led Fox to drop its prices, or, at the very least, refrain from any increases. This in turn would greatly affect the overall results of the analysis by Drs. Israel and Katz; yet, they did not control for it. As for the other three events, there may well have been uncontrolled-for events as well. In sum, their empirical study has far too many problems for it to be considered reliable by the Commission,

[25] Rogerson II at 35.

and the best available evidence continues to be the ACA's submission of price increases resulting from the combination of Big 4 local television stations.

B. Vertical Harm.

1. Introduction.

Professor Rogerson's first report set forth the theory of vertical harm that arises from the proposed combination of Comcast and NBCU and then calculated the extent of this harm. In essence, because the Joint Venture will take account of the fact that selling programming to MVPDs that compete with Comcast will reduce Comcast's profits, the combination of Comcast's ownership share of the Joint Venture and its ownership of its MVPDs assets would cause the Joint Venture to bargain for higher programming fees from MVPDs that compete with Comcast and these higher fees would be substantially passed through to subscribers, increasing their fees (The "Raising Rival's Costs" effect). Professor Rogerson then calculated that in regions with an NBCO O&O, the expected increase in fees charged to competing MVPDs (DBS and telephone providers) for both retransmission and for carriage of cable networks would be approximately $.95 per subscriber per month.[26]

The Applicants' Opposition, relying on the Israel/Katz Report, seeks to refute Professor Rogerson's analysis by contending:

1. "[I]t would be inappropriate to consider the potential programming-cost increases that may arise because NBCU may internalize Comcast's profits…without also accounting for programming cost decreases flowing from

[26] For a cable overbuilder where Comcast passed 80% of the same homes, the price increase would be larger, $1.06 per subscriber per month.

efficiencies – notably the reduction in double marginalization – that will arise because Comcast, while paying the same price to NBCU for programming as determined in arm's-length negotiations, will internalize NBC profits…Once these efficiencies are incorporated, the net effect of the transaction on average MVPD programming costs is negative."[27]

2. The "Raising Rival's Costs" approach used by Professor Rogerson "does not predict how players will allocate the surplus generated by their agreement" and, in any event, his calculation overstates the likely effect.[28]

3. The Commission should not be concerned if post-combination the Joint Venture raises programming fees for cable overbuilders since these providers have an insignificant number of subscribers.[29]

In the following sections, the ACA uses Rogerson II to demonstrate the fundamental flaws in the arguments propounded in the Applicants' Opposition and the Israel/Katz Report.

2. Contrary to the Applicants' claim, the reduction in Comcast's costs post-combination because of double marginalization is relatively insignificant.

The Applicants contend that double marginalization exists pre-combination because "although the marginal cost of NBCU when MVPDs distribute programming to an additional subscriber is typically near zero, NBCU charges Comcast (and other

[27] Applicants' Opposition at 149-150.

[28] Applicants' Opposition at 143-144.

[29] Israel/Katz Report, n.100.

MVPDs) a pre-subscriber price that is above zero for most of its content."[30] They then argue that double marginalization will be reduced post-combination because "for every dollar that Comcast pays to NBCU, it will retain ownership of 51 cents through its interest in NBCU" and that "these double marginalization savings represent a true reduction in the average cost (across MVPDs) for NBCU programming."[31] Finally, they maintain that the reduction in costs as the result of double merginalization is so great that the price increases calculated by Professor Rogerson are "swamped by the price effects of transaction-related efficiencies."[32]

While the Applicants' double marginalization analysis may at first seem appealing, Professor Rogerson demonstrates in Rogerson II that Drs. Israel and Katz "make a grave error in economic reasoning that results in a completely false conclusion."[33] Professor Rogerson does not disagree that post-combination Comcast will operate as if its marginal cost of providing NBCU programming to its cable subscribers is zero. He, however, finds that Drs. Israel and Katz ignore in their analysis the new opportunity cost that arises because the Joint Venture charges a programming fee not only to Comcast but to all competing MVPDs and that this entire programming fee charged to competing MVPDs represents profit to the Joint Venture. As a result, should Comcast lower its subscription price slightly to attract more customers, the Joint Ventura will lose these fees paid by other MVPDs and the

[30] Israel/Katz Report at 150.

[31] Israel/Katz Report at 151.

[32] Israel/Katz Report at 152.

[33] Rogerson II at 8.

attending profit.[34] Professor Rogerson shows (using $1.56 as a reasonably plausible value for the cost of NBCU programming) that when the new opportunity cost is taken into account the effect of reduced double marginalization is minimal:[35]

> [I]f θ is the switcher share for Comcast, then this means that θ of the customers that it would attract by lowering its price slightly would be customers that switch from some other MVPD. This means that the opportunity cost of attracting a new customer is θ x $1.56, because this is the amount of profit that the vertically integrated firm will lose when it attracts new customers. Therefore a complete accounting of the effects of vertical integration on the marginal cost to the combined entity of serving new MVPD customers is as follows. First, because the payment of Comcast to the joint venture of $1.56 is now simply a transfer payment, the marginal cost goes down by $1.56. However, second, because θ of the customers that Comcast attracts will be from other MVPDs, there is a new opportunity cost of θ x $1.56 per subscriber per month. A decrease in cost of $1.56 combined with an increase in cost of θ x $1.56 yields a net decrease in cost of (1-θ) x $1.56. In particular, if θ is close to 1 [which should be expected since most new customers will be existing MVPD customers], then the net decrease in cost due to the double marginalization effect will be close to 0.[36]

Even if the share of new customers that are "switchers" from competing MVPDs is somewhat lower – that is, the value of θ is not 1 but .9 – the cost reduction from double marginalization would only be $.16 per subscriber per month. To provide context for this reduction, Rogerson I found that post-combination, competing MVPDs would see an increase of $.95 in their cost to carry NBCU programming. Thus,

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[34] This is based on the perfectly reasonable assumption that, given the large percentage of MVPD subscribers, almost all of the new customers switch from other MVPDs.

[35] For purposes of reading the following passage, Professor Rogerson defines the "switcher share," denoted by the parameter θ, as follows. Suppose that an MPVD lowers its price slightly in an attempt to attract new customers. Some of the new customers will be people who switch from some other MVPD (the "switchers") and some will be people who previously subscribed to no MVPD. The switcher share, θ, is defined to be the share of new customers that are "switchers." Professor Rogerson argues that the switcher share is likely very close to 1.

[36] Rogerson II at 10.

contrary to the claim of the Applicants, the harm from the proposed combination dwarfs the putative benefits.[37]

3. Applicants' arguments do not lessen concerns that Comcast-NBCU will raise programming prices to rival MVPDs post-combination.

The Applicants present a series of arguments in their attempt to undermine the validity of the Raising Rivals' Costs approach used by Professor Rogerson to demonstrate that post-combination Comcast would raise the prices competing MVPDs would pay for NBCU programming. The ACA responds to each:

> **1. Applicants' Contention**: The benefits of double marginalization can be achieved without close coordination and redistribution of profits and thus could occur with Comcast only holding 51% of the Joint Venture. In contrast, the Raising Rivals' Costs approach requires close coordination and redistribution of profits which will not occur because of General Electric's interest in the Joint Venture.[38]

ACA Response: First, as discussed above, the efficiencies gained by double marginalization are minimal. Thus, even if Comcast fully internalized all of the upstream profits, the effects of double marginalization would not give it sufficient incentive to make significantly different pricing decisions at the downstream level.

[37] The ACA also notes that Professor Rogerson highlights another concern the Commission should consider in addressing the issue of double marginalization. In n.17 in Rogerson II, he states: "I would also like to raise the more minor point that even if the reduced double marginalization effect was of the same order of magnitude as raising rivals' costs effect, this would still potentially create an issue of concern for the Commission. In the markets that Comcast serves, it is generally the dominant provider. Any transaction that had the effect of giving Comcast a significant cost advantage over its competitors might threaten to drive Comcast's competitors out of the market entirely or at least weaken them considerably, and thus damage competition. Thus, even if the effect of the transaction was to lower Comcast's own costs and raise its rivals' costs by approximately the same amount, it is not at all clear that the net effect on subscribers would be minor. If the result of this was to drive Comcast's competitors from the market or at least considerably weaken them, the reduction in competition might ultimately make it profitable for Comcast to raise its own subscription prices."

[38] Israel/Katz Report, ¶26.

Second, there are important classes of efficiencies that can only be achieved by close coordination and profit redistribution. Thus, the Applicants' cannot contend the proposed combination will produce meaningful efficiencies if they do not also believe they can and will act in concert.

> **2. Applicants' Contention**: The bargaining model used by Professor Rogerson is too stylized and "cannot generate reliable predictions about the pricing effects of the proposed transaction."[39]

ACA Response: While Drs. Israel and Katz criticize the bargaining model, they also admit that it "commonly is used in academic settings to derive basic insights about various types of negotiations." Moreover, Dr. Katz found the bargaining model sufficiently valuable to use as the basis of a paper he submitted to the Commission late last year to justify a client's policy position.[40] As Professor Rogerson notes, "Almost all economic models are highly stylized, including most of the game theoretic models that provide the foundation for modern industrial organization theory and that play a key role in providing guidance for antitrust policy...[and in deriving] basic insights useful for policy analysis."[41] Finally, in its most recent review of a significant vertical integration, the Adelphia-Time Warner-Comcast transaction, the Commission relied on a type of bargaining model to analyze the vertical effects.[42]

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[39] Israel/Katz Report, ¶ 35. *See also* Israel/Katz Report, ¶¶ 43-48.

[40] See *In the Matter of Mediacom Communications Corporation v. Sinclair Broadcast Group, Inc.*, Retransmission Consent Complaint, CSR-8233-C, CSR-8234-M, Comments of Comcast, Submission of Michael Katz, Jonathan Orszag, and Theresa Sullivan, "An Economic Analysis of Consumer Harm From the Current Retransmission Consent Regime," Nov. 12, 2009 (filed Nov. 25, 2009).

[41] Rogerson II at 14.

[42] *In the Matter of Applications for Consent to the Assignment and/or Transfer of Control of Licenses Adelphia Communications Corporation, (and subsidiaries, debtors-in-possession), Assignors, to Time Warner Cable Inc. (subsidiaries), Assignees; Adelphia Communications Corporation, (and subsidiaries,*