Before the
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554

In the Matter of	)	
	)	
Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming	)	MB Docket No. 07-269
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COMMENTS OF NETFLIX, INC.

Netflix, Inc. ("Netflix") hereby submits these comments in response to the Commission's Further Notice of Inquiry ("NOI")[1] in the above-captioned proceeding. Netflix commends the Commission's focus on the issues raised in the NOI, including a focus on the increased availability of video programming made available over the Internet by online video distributors ("OVDs") and the resulting expansion of consumer choice.[2]

Though the OVD market today offers consumers numerous choices, Netflix urges the Commission to continue vigilant oversight of the market for the delivery of video programming. The fact that broadband network operators, who are also MVPDs, control the delivery pipes and generate significant revenue from content that travels over those pipes provides such network operators with

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[1] *Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, Further Notice of Inquiry, MB Docket No. 07-269, FCC 11-65 (rel. Apr. 21, 2011) ("NOI").
[2] NOI at 3, ¶ 2.

both the means and motive for discriminating against OVDs that might threaten that revenue. As discussed below, the Commission must continue to monitor network operators to ensure that they do not discriminate against OVDs by leveraging their dominant position in the broadband market, denying access to programming, imposing discriminatory charges on terminating traffic, or adopting pricing plans that have the effect of discriminating against OVDs.

I. INTRODUCTION

A. Netflix

With more than 23 million subscribers, Netflix is the largest online video subscription service in the United States.[3] Having built a successful DVD-by-mail rental subscription business, Netflix has become a leader in online video, offering its subscribers a large and growing library of movies and TV shows streamed to their computers and TVs, and is today primarily an online video streaming provider. Netflix has seen rapid growth in recent years, more than doubling its number of subscribers in the last 18 months and adding almost 9 million subscribers in the last year. Today, Netflix offers its subscribers unlimited online streaming video programming content for $7.99 per month, with additional charges for those subscribers who receive DVDs via mail.

In keeping with the open nature of most broadband networks, Netflix has partnered with a broad array of consumer electronics providers to bring to

[3] Netflix, founded in 1997, is headquartered in Los Gatos, California and is publicly traded on the NASDAQ under the symbol, NFLX.

market a range of devices that permit Netflix subscribers to stream movies and TV shows instantly and directly to their viewing screens. These devices include Blu-ray disc players, Internet-enabled TVs, leading game consoles like Microsoft's Xbox 360, Nintendo Wii, and Sony's PlayStation 3, the Roku digital video player, TiVo digital video recorders, and tablet computers. Netflix's service is available through over one hundred different consumer devices.

Netflix has built its OVD business around the legal distribution of video programming over the Internet by licensing the content from various producers and distributors. As Netflix's subscriber base has grown, it has continued to license more content for streaming, thereby providing an increasingly valuable revenue stream to the producers and distributors of that content. Today, Netflix's subscribers can instantly enjoy a wider and better selection of TV shows and movies than ever before, including programming from all four broadcast networks and many of the largest cable TV networks. For example, pursuant to recent deals with Fox and Lionsgate, Netflix subscribers can instantly watch previous seasons' episodes of popular TV series such as *Glee*, *Mad Men*, and *Sons of Anarchy*. The growth and popularity of Netflix's service demonstrates that consumers want legally delivered content and that content owners and distributors can make money from such online distribution of video programming content.

B. The Online Video Distributor Market

The OVD market is intensely competitive and subject to rapid change. Netflix faces competition from a number of sources, ranging from other OVDs that focus on streaming content such as Hulu Plus, Amazon Prime, and YouTube, to Internet-based content outlets like Apple's iTunes. Perhaps most significant is the competition from online video offerings of multichannel video programming distributors ("MVPDs"), such as "TV Everywhere" services, as well as from video on demand (VOD) offerings from MVPDs. The variety of OVD service offerings, as well as the range of consumer electronics devices on which such programming can be accessed, gives U.S. consumers more choices than ever before to consume video programming and has helped the content industry keep pace with changing consumer demand and consumption habits.

The Commission is right to consider OVDs as a complement rather than a substitute for MVPD service.[4] While Netflix has an ever-growing catalog of content, the overwhelming majority of its subscribers continue to rely on their MVPD subscriptions for sports, current season TV shows, news and other entertainment. With respect to TV shows, Netflix's focus is on prior season shows and completeness of series. Moreover, Netflix believes that its offerings of

[4] *See* NOI at 5 n.16; *see also Application of Comcast Corporation, General Electric Company and NBC Universal, Inc. for Consent to Assign Licenses and Transfer Control of Licenses*, Memorandum Opinion and Order, MB Docket No. 10-56, FCC 11-4, at ¶¶79-85 (rel. Jan. 20, 2011) ("*Comcast-NBCU Order*").

prior seasons of hit shows like *Glee* and *Mad Men* help to grow the audience for the current season of these shows on MVPDs.

The proposition that OVDs are a complement to and not a substitute for MVPD service is supported by the fact that the total number of U.S. MVPD subscriptions has been growing recently, even as OVD use has been growing at an extremely rapid pace.

II. BECAUSE MVPDs ARE TYPICALLY THE SAME ENTITITES THAT OFFER CONSUMERS THE BROADBAND SERVICES NEEDED TO ACCESS OVD PROGRAMMING, THE COMMISSION MUST CONTINUE TO BE VIGILANT IN ITS OVERSIGHT OF THE MARKET FOR THE DELIVERY OF VIDEO PROGRAMMING

As discussed above, the growth of OVDs like Netflix has given consumers greater choices for accessing video programming and has given content creators additional outlets — and revenue streams — for delivering legal content. However, given that OVDs are reliant on broadband providers to deliver their services and that broadband providers and MVPDs are typically the same entities, the Commission must remain vigilant in its oversight of the video distribution marketplace. Specifically, the Commission should be aware that structural factors such as vertical integration of broadband network operators and MVPDs limit the competitive constraints on MVPDs.

The fact that broadband network operators, who are also MVPDs, control the delivery pipes and generate significant revenue from content that travels over those pipes provides both the means and motive for discriminating against

OVDs that might threaten that revenue.[5] In its NOI, the Commission requests information regarding the challenges faced by OVDs.[6] Simply stated, the incentive and ability of network operators who are also MVPDs to discriminate against unaffiliated OVDs defines those challenges.

The following discussion of the challenges faced by OVDs like Netflix is not intended to be an exhaustive discussion of the issues identified, but is instead intended to raise issues that could shield MVPDs from competition from new entrant OVDs and caution against lessening the Commission's oversight of market for the delivery of video programming in the face of entry by OVDs.

TV Everywhere: Under such services, MVPDs provide free on-demand Internet video as part of a consumer's MVPD package. By bundling traditional MVPD services with Internet delivery of content, vertically integrated MVPDs leverage their dominant market position at the expense of competitive online offerings.

Access to programming: As established entities in the market with revenues that dwarf those of OVDs, MVPDs exercise significant content purchasing power which they can use — and have been using — to extract discriminatory concessions from unaffiliated video content providers.[7] Of course, in the case of vertically integrated MVPDs that also

[5] *See Comcast/NBCU Order* at 26, ¶ 61.
[6] NOI at 23, ¶ 54.
[7] *See, e.g.*, Andrew Wallenstein, *Turner Chief Explains How TV Industry Will Neutralize Netflix*, paidContent.org, Jan. 5, 2011, *available at* http://paidcontent.org/article/419-turner-chief-explains-how-tv-industry-will-neutralize-netflix/ (quoting Turner

control video content, MVPDs may simply deny OVDs access to their content.[8]

Charges for Delivering Internet Traffic: Today, some MVPD/broadband network operators charge to terminate traffic on their networks, despite the traffic having been requested by their own subscribers.[9] Because network operators control access to the last mile facilities of their subscribers, they are in a position to charge for termination of traffic to those subscribers even when OVDs such as Netflix have brought the requested data to regional interchanges of the network operators' choosing. Thus, broadband network operators can use their terminating access monopolies to raise the cost of terminating unaffiliated traffic, distorting the operation of the Internet and raising the costs of OVDs and to consumers.

Broadcasting Chairman and CEO Phil Kent: "We tell our suppliers, the studios we buy from: [Having programming available on Netflix] is going to have a significant impact on what we'll be willing to pay for programming or even bid at all."); *Comcast/NBCU Order* at 30, ¶ 73 (concluding that Comcast/NBCU will have increased leverage to negotiate restrictive online rights from third parties to the detriment of competition, that such restrictive agreements may harm consumer choice, diversity, and broadband investment, and adopting a condition restricting Comcast/NBCU from entering into restrictive agreements with third-party content providers regarding online rights).

[8] *See Comcast/NBCU Order* at 31-37, ¶¶ 78-90.

[9] This issue was central to a recent dispute between Comcast and Level 3. *See, e.g.*, *Ex Parte* Letter from John M. Ryan, Assistant Chief Legal Officer, Level 3 Communications, Inc. to Marlene H. Dortch, Secretary, FCC, GN Docket No. 09-191, WC Docket Nos. 07-52 & 10-127 (Dec. 10, 2010); *Ex Parte* Letter from John M. Ryan, Chief Legal Officer, Level 3 Communications, Inc. to Marlene H. Dortch, Secretary, FCC, GN Docket No. 09-191 (Jan. 14, 2011).

Usage-based Billing: Moves by network operators toward pay-per-gigabyte pricing plans could adversely impact and discriminate against OVDs. Such pricing schemes are particularly worrisome as they do not meaningfully address traffic management, but instead seem to be a profit maximizing ploy in a non-competitive marketplace.[10] If such plans are implemented by means of a large cap that affects only the heaviest of users, we believe they would have little adverse impact on Netflix subscribers. However, lower data caps could have a chilling effect on usage of OVD services and/or could cause OVDs to provide lower quality video to its users.

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Netflix thanks the Commission for its focus on the increased availability of video programming made available by OVDs and the resulting benefits from the expansion of consumer choice. For the reasons discussed above, Netflix urges the Commission to continue vigilant oversight of the market for the delivery of video programming.

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[10] Data caps are in fact a very poor way to manage demand and limit network congestion. The costs of supplying residential broadband are associated with supporting the peak loads; bandwidth consumed during off-peak hours is essentially free from the standpoint of the cost to the network. However, data caps make no distinction between bandwidth consumed during peak and off-peak hours and simply charge consumers for bandwidth overages.

Respectfully submitted,

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