September 13, 2012

BY ELECTRONIC FILING

Marlene H. Dortch, Secretary
Federal Communications Commission
445 Twelfth Street, S.W.
Washington, DC 20554

Re: *Revision of the Commission's Program Access Rules*, MB Docket No. 12-68; *News Corporation, The DIRECTV Group, Inc., and Liberty Media Corporation,* MB Docket No. 07-18; *Adelphia Communications Corporation, Time Warner Cable Inc., and Comcast Corporation*, MB Docket No. 05-192

Dear Ms. Dortch:

Throughout this proceeding, competitive multichannel video programming distributors ("MVPDs") have presented empirical evidence and expert economic analysis[1] to demonstrate that the cable exclusivity prohibition remains "necessary to *preserve and protect* competition and diversity in the distribution of video programming"—the standard for renewing the prohibition.[2] Now, less than one month before the Commission must act in this proceeding,[3] the National Cable & Telecommunications Association ("NCTA") has filed the first economic report submitted on behalf of those who favor allowing the prohibition to sunset.[4]

As discussed below, this belated effort provides no basis for abandoning the regime currently in place. The report does little more than repackage assertions that the cable industry has made for years now in prior proceedings, where they have been rejected by the Commission and the courts. Indeed, some of those assertions are inconsistent with economic arguments made to the Commission by cable operators in

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1 *See, e.g.,* Report of Professor Kevin M. Murphy (June 22, 2012) ("Murphy Report") (attached to Comments of DIRECTV, LLC, MB Docket Nos. 12-68, 07-18, and 05-192 (June 22, 2012)).

2 47 U.S.C. § 548(c)(5) (emphasis added).

3 *See Revision of the Commission's Program Access Rules*, 27 FCC Rcd. 3413, ¶ 3 (2012) ("*Notice*") (noting that exclusivity prohibition expires on October 5, 2012).

4 *See* Declaration of Dr. Mark Israel, "An Economic Assessment of the Prohibition on Exclusive Contracts for Satellite-Delivered, Cable-Affiliated Networks" (Sep. 6, 2012) ("Israel Report") (attached to Letter from Rick Chessen to Marlene H. Dortch, MB Docket Nos. 12-68, 07-18, and 05-192 (Sep. 7, 2012)).

other recent proceedings. Moreover, the report also fails to meaningfully address the new economic analysis and empirical evidence in the record of this proceeding that directly contradict its theoretical assertions.

We address each of the principal economic arguments in the Israel Report below.

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Assertion 1: A vertically integrated MVPD that can distribute its programming exclusively has greater incentives to invest in high-quality content than it would have under a requirement that the content be shared with its rivals in the MVPD marketplace.[5]

This is perhaps the most often recycled of NCTA's arguments—one that cable operators make at every opportunity, and one that the Commission has rejected every time it has been made. For example, the cable industry raised this argument in the two prior sunset proceedings, and the Commission rejected it both times:

- In 2002, in response to arguments that exclusivity would lead to additional investment, the Commission noted that the number of national programming networks (including cable-affiliated networks) had increased substantially *with* an exclusivity ban, and thus concluded that "the retention of the exclusivity prohibition will not reduce the incentives to create new or diverse programming."[6] (The explosive growth in national networks has continued, with today's approximately 800 networks more than doubling the 294 that existed in 2002.[7])

- In 2007, in response to the same argument, the Commission noted that cable-affiliated programmers had only rarely exercised their option to seek approval of exclusive arrangements; moreover, all three networks (CourtTV, Speed, and SyFy) that were the subjects of exclusivity petitions that were denied had flourished despite the lack of exclusivity.[8]

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5 *See, e.g.*, Israel Report, ¶ 21.

6 *See Implementation of the Cable Television Consumer Protection and Competition Act of 1992 – Development of Competition and Diversity in Video Programming Distribution*, 17 FCC Rcd. 12124, ¶ 64 (2002) ("*2002 Extension Order*").

7 *See Notice*, Appendix B, Table 1.

8 *Implementation of the Cable Television Consumer Protection and Competition Act of 1992 – Development of Competition and Diversity in Video Programming Distribution: Sunset of Exclusive Contract Prohibition*, 22 FCC Rcd. 17791, ¶ 63 (2007) ("*2007 Extension Order*), *aff'd sub nom. Cablevision Sys. Corp. v. FCC*, 597 F.3d 1306 (D.C. Cir. 2010) ("*Cablevision I*").

Likewise, although Cablevision and MSG recently claimed that withholding the HD feed of two RSNs would lead to more investment and innovation, the Commission found that they were able to "put forth no evidence demonstrating that this theory motivated their withholding strategy" and that they "put forth no evidence demonstrating that this withholding strategy has resulted in increased investment in the networks or that it has improved the quantity and quality of programming on the networks."[9]

It is also worth noting that some of the more recent cable submissions not only present "no evidence" that exclusivity is necessary for investment, but essentially concede that the opposite is true. Specifically, in the *Comcast/NBCU* proceeding, Comcast submitted an expert report that discussed at length the synergies and incentives for investment that would arise from the proposed transaction,[10] concluding that "[t]he major benefits to consumers and the companies come from vertical efficiencies that lead to increased investment in distribution and programming and the expansion of output."[11] Noticeably absent is any mention of the possibility that the exclusivity prohibition might lead Comcast to underfund its new acquisitions, or that the cited benefits depended on repeal of the exclusivity prohibition. Comcast's CEO has consistently touted investments in NBCU programming ever since the transaction closed.[12] If Dr. Israel has any evidence to the contrary, it would be of great interest to MVPDs that face demands for ever-increasing fees for Comcast/NBCU programming.

Although there are several instances of cable exclusivity from which to draw (*e.g.*, years of RSN exclusivity in Philadelphia or San Diego), Dr. Israel fails to offer any empirical evidence of increased investment or innovation arising from exclusivity. Nor

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9 *Verizon Tel. Cos. and Verizon Svcs. Corp. v. Madison Square Garden, L.P. and Cablevision Sys. Corp.*, 26 FCC Rcd. 13145, ¶ 33 (MB 2011); *AT&T Svcs. Inc. and S. New England Tel. Co. d/b/a AT&T Connecticut v. Madison Square Garden, L.P. and Cablevision Sys. Corp.*, 26 FCC Rcd. 13206, ¶ 34 (MB 2011).

10 *See* Gregory L. Rosston, "An Economic Analysis of Competitive Benefits from the Comcast-NBCU Transaction," ¶¶ 64-92 (May 4, 2010) (attached to Letter from Michael H. Hammer to Marlene H. Dortch, MB Docket No. 10-56 (May 4, 2010)).

11 *Id.*, ¶ 91.

12 *See, e.g.,* Comcast Corp., Q4 2011 Earnings Call Transcript at pp. 2-3 (Feb. 15, 2012) ("We invested in new shows in both Cable Networks and on our Broadcast Networks. We invested in our own stations. We extended the NHL and PGA rights, purchased 100% of the Orlando theme parks, have some exciting film franchises launching in 2012. We invested to extend the Harry Potter franchise in several of our theme parks. We also brought together all of our company's capabilities in successful bids for the Olympics. For the Spanish language rights for FIFA World Cup soccer. And we extended the all-important Sunday Night Football franchise with the NFL. In each case, we secured important rights for many years, and we got more content to be used over many new platforms, putting us on a path to make these investments profitable over time and to significantly strengthen the business."), *available at* http://files.shareholder.com/downloads/CMCSA/1922203650x0x542776/5719e32e-a4f8-47af-9b8a-7f79e3df784f/COMCAST%20Q411%20transcript.pdf.

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does his theory explain why non-cable MVPDs such as Verizon, AT&T, and DISH Network that are free to vertically integrate and thereafter enter into exclusive agreements with their affiliated programmers have not done so. If competitive conditions and efficiencies available to be captured were as he posits, one would expect to see at least some instances of such integration/exclusivity.[13] Yet ironically, the only competitive MVPD with interests in national and regional programming is DIRECTV, which (like cable) cannot enter into exclusive arrangements with affiliated programmers. Indeed, the primary example of investment in programming innovation cited by Dr. Israel is DIRECTV's NFL Sunday Ticket[14]—exactly the type of an arrangement with a non-affiliated programmer that the existing rules *do not* prohibit for cable.

Given all this, the contention that exclusivity is a necessary or important incentive for investment in programming cannot be taken seriously.

Assertion 2: An exclusivity prohibition would be good economic policy only if refusals to deal by vertically integrated cable networks were anti-competitive under nearly all circumstances, without offsetting pro-competitive benefits.[15]

Dr. Israel argues that an exclusivity prohibition is only appropriate if exclusivity is *always* harmful, and that otherwise, a case-by-case formulation is required.[16] This, however, is not the standard the Commission has applied (and the court has approved) in prior extension proceedings.

Rather, in both 2002 and 2007, the Commission sought to determine "if, in the absence of the prohibition, competition and diversity [in the distribution of video programming] would be preserved and protected."[17] Based on its analysis of the available empirical evidence and the application of its own predictive judgment, the Commission concluded on both occasions that vertically integrated cable operators had the incentive and ability to withhold at least some programming, and that such practices

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13 Recent assertions by cable operators themselves suggest that vertical integration is not necessary to the development of innovative and high-value programming in the first place. In the proceeding on the spin-off of Time Warner Cable from its programming affiliate, the applicants asserted that disaggregation "will place both companies in a better position to improve the number and quality of products and services they provide," Time Warner Cable, Inc., Application for Consent to Assignment and/or Transfer of Control of Licenses, MB Docket No. 08-120, Exhibit B-2 at 3 (filed June 13, 2008), and that "such focus and flexibility can be vital" under current market conditions, Reply, MB Docket No. 08-120, at 6 (filed Aug. 15, 2008).

14 Israel Report, ¶ 21.

15 *See, e.g., id.*, ¶ 20.

16 *See, e.g., id.*, ¶¶ 18, 31.

17 *See 2002 Extension Order*, ¶ 14; *2007 Extension Order*, ¶ 13. This standard was approved by the D.C. Circuit. *See Cablevision I*, 597 F.3d at 1313.

predictably harm competition and diversity in the distribution of video programming, to the detriment of consumers.[18] Since that time, the Commission has consistently found that vertically integrated cable operators continue to have the incentive and ability to withhold programming, and that such withholding has anticompetitive consequences.[19] Given this precedent, a straightforward application of the Commission's predictive judgment would justify an extension of the exclusivity prohibition.

Dr. Israel's formulation also fails to recognize two important considerations. First, he does not account for the substantial costs (both monetary and operational) in pursuing a case-by-case remedy for withholding. Such costs can make bright-line rules more preferable than individualized determinations. Second, to the extent cable operators and their affiliated programmers feel otherwise, Congress *already* empowered them to seek a case-by-case determination by petitioning the Commission for authority to engage in exclusive arrangements that would serve the public interest.[20] Under Congress's formulation, however, it is cable programmers rather than cable's rivals that must seek such relief from the Commission.

The question before the Commission, then, is not whether it should prohibit all exclusive arrangements everywhere or examine each arrangement individually. It is what the default rules should be. On this question, Dr. Israel does not discuss, much less attempt to refute, the analysis presented by Professor Kevin Murphy demonstrating that cable-affiliated programmers are most likely to withhold programming in precisely those cases where doing so would have the most harmful effects. As Professor Murphy concludes:

> Vertically integrated programmers find it in their interest to withhold precisely when withholding has the worst price impacts for consumers, i.e., in those cases where the prices of the vertically integrated MVPD would fall the most and its competitor's prices would increase the least if the rival MVPD had access to the programming. The competitive conditions where extending the cable exclusivity prohibition likely will benefit consumers the most through price competition are those where the vertically integrated firm has the greatest incentive to refuse to license.[21]

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[18] *See, e.g., 2002 Extension Order*, ¶ 4; *2007 Extension Order*, ¶ 29 and Appendix C, ¶ 20.

[19] *See Comcast Corp., General Electric Co. and NBC Universal, Inc.*, 26 FCC Rcd. 4238, ¶¶ 29, 39 (2011) ("*Comcast/NBCU Order*"); *Verizon Tel. Cos. and Verizon Svcs. Corp. v. Madison Square Garden, L.P. and Cablevision Sys. Corp.*, 26 FCC Rcd. 15849 (2011); *AT&T Svcs. Inc. and Southern New England Tel. Co. d/b/a AT&T Connecticut v. Madison Square Garden, L.P. and Cablevision Sys. Corp.*, 26 FCC Rcd. 15871 (2011); *Review of the Commission's Program Access Rules and Examination of Program Tying Arrangements*, 25 FCC Rcd. 746, ¶ 25 (2010).

[20] *See* 47 U.S.C. § 548(c)(2)(D).

[21] Murphy Report at 28.

Dr. Israel's report makes no attempt to rebut Professor Murphy's conclusion that cable exclusivity would have the worst effects on consumers and competition in nearly all circumstances it is likely to occur. Given the way Dr. Israel framed the issue, this failure is especially telling.

Assertion 3: A prohibition on exclusivity can only be justified if the cable-affiliated network is an essential facility without which other MVPDs cannot compete effectively for new subscribers.[22]

Here again, Dr. Israel attempts to frame an issue in a manner previously rejected by the Commission. He suggests that exclusivity should be allowed unless it would threaten the competitive viability of rival MVPDs. In two recent program access cases, Cablevision and its Madison Square Garden Company affiliate made this same argument. The Commission squarely rejected it, and noted that the D.C. Circuit had specifically rejected the claim that an MVPD must show complete foreclosure to prevail in a program access complaint.[23] It should similarly reject Dr. Israel's formulation as well.

As the Commission found in 2007, "the more salient point for our analysis is not whether individual competitors will remain in the market if the exclusive contract prohibition were to sunset, but how competition in the video distribution market will be impacted if the exclusive contract prohibition were to sunset."[24] Although Dr. Israel essentially ignores this salient question, the Commission has on many occasions found that competition would be negatively affected by cable exclusivity.[25] Most recently, it found that "successful exclusion (whether involving complete foreclosure or cost-raising strategies) of video distribution rivals would likely harm competition by allowing Comcast to obtain or (to the extent it may already possess it) maintain market power."[26] By focusing on the wrong question (competitive viability), Dr. Israel sidesteps the Commission's prior findings entirely.

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22 Israel Report, ¶ 16.

23 *Verizon Tel. Cos. and Verizon Svcs. Corp. v. Madison Square Garden, L.P. and Cablevision Sys. Corp.*, 26 FCC Rcd. 15849, ¶ 11 (2011); *AT&T Svcs. Inc. and S. New England Tel. Co. d/b/a AT&T Connecticut v. Madison Square Garden, L.P. and Cablevision Sys. Corp.*, 26 FCC Rcd. 15871, ¶ 11 (2011) (same).

24 *See 2007 Extension Order*, ¶ 61.

25 *See*, *e.g.*, n.*19*, *supra*.

26 *Comcast/NBCU Order*, ¶ 39.

Assertion 4: The Commission's analysis is flawed because it fails to consider market responses to withholding and other factors.[27]

Dr. Israel finds fault in several aspects of the analysis upon which the Commission has based its conclusion that cable operators continue to have the incentive and ability to withhold programming to the detriment of competition. He raised a number of these criticisms in the *Comcast/NBCU* proceeding, where the Commission considered and rejected them.[28] His primary new criticism in this proceeding is that the Commission fails to take into account the potential competitive response of foreclosed rivals once they lose access to programming. For example, Dr. Israel asserts that such a rival can simply develop or improve its own alternative programming.[29] Yet the Commission has previously found that "cable programming is highly differentiated, so the foreclosed rivals cannot practically or inexpensively avoid the harm by substituting other programming."[30] Dr. Israel lists other potential responses, but provides no evidence that MVPDs are not already employing those strategies to compete under current market conditions.

Here again, moreover, Dr. Israel ignores the analysis submitted by Professor Murphy, which presents a bargaining model that includes likely responses by competitors. Indeed, it is the evidence that a competitor who gains access to programming will likely take its gains from trade in the form of additional subscribers rather than higher prices that leads to his conclusion about the effects of withholding.[31] Given his failure to grapple with the analysis of likely competitive response in Professor Murphy's model, Dr. Israel's criticism of the Commission for failing to fully account for this consideration rings hollow.

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NCTA's expert report mostly recycles arguments that the Commission and courts have already rejected. While the filing makes a handful of new arguments, those arguments ignore the evidence already in the record undercutting them. In the end, NCTA's last-minute effort has little to offer the Commission.

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[27] *See, e.g.*, Israel Report, ¶ 9.

[28] *See Comcast/NBCU Order*, Appendix B, ¶¶ 17-18, 20.

[29] Israel Report, ¶ 22 and n.25.

[30] *Comcast/NBCU Order*, ¶ 37 n.90. Dr. Israel's attempt to analogize cable exclusivity with exclusive arrangements between programmers and their content suppliers is inapt. *See* Israel Report at ¶ 23. When a producer licenses a show exclusively to HBO, it knows that HBO is widely available to subscribers over a wide variety of platforms. By contrast, when a programming network grants a cable operator an exclusive license, it limits its potential distribution to that cable operator's subscribers alone.

[31] Murphy Report at 26-28, 30-32.

Respectfully submitted,

/s/

William M. Wiltshire
Michael Nilsson

Counsel for DIRECTV, LLC

cc: Lyle Elder
David Grimaldi
Alexander Hoehn-Saric
Holly Saurer
Matthew Berry
Erin McGrath
Elizabeth Andrion
William Lake
Michelle Carey
Mary Beth Murphy
David Konczal
Steven Broeckaert
Jonathan Levy
Kathy Berthot