Senator METZENBAUM Let me ask you, Mr Hostetter—your entire statement will be included in the record as will the entire statement of each of the witnesses today

How important is the availability of HBO to the success of a cable system, or Showtime?

Mr HOSTETTER The availability of unique product is what has built the cable industry The product we are selling is a smorgasbord of channels And the fact that we have things from Black Entertainment Television to first run motion pictures, whether it be by HBO or by Showtime, it is the mix that we market and it is the uniqueness of that mix

Senator METZENBAUM You stated recently that following the acquisition of American Cablesystems, that it is inevitable that the cable TV industry will become more concentrated What is the reasoning behind that prediction?

Mr HOSTETTER Because as yet, even the largest of these companies are not large by American industrial standards And the trend towards concentration as a result of efficiency of operation, regional clustering of systems, additional revenue sources are going to come from more concentrated blocks of systems The fact that Bascomb would have a different CATV company from Fostoria or from Tiffin or from Finley is just illogical, and eventually those clusters are going to pull together for the efficiency of marketing the service

Senator METZENBAUM Am I correct that just as in TV stations, cable systems have a one-time major capital investment? I know that there are supplementals But in the main, you lay down the wire and that is the major capital investment, and from that point on that there is not substantial additional capital investment required unless you are expanding or unless you are buying up another system Is that true or false?

Mr HOSTETTER That is false The revenue-to-investment relationship in broadcasting, revenues will run five or six times the invested capital In cable almost the reverse is true Our invested capital will be five or six times our gross revenue And the pattern is that every new customer who is hooked up requires an installation from the house, some internal wiring in the house, a converter box We have $150 to $200 just per pop with each new installation

We then have rolling stock to replace We have to maintain and update the plant The plant we built in Tiffin and Fostoria, OH, 25 years ago has been totally rebuilt twice since that day

Senator METZENBAUM Why is that needed?

Mr HOSTETTER Because the capacity of the plant becomes obsolete

Senator METZENBAUM That is because you are expanding

Mr HOSTETTER We are adding to the number of services that we are offering

Senator METZENBAUM Number of services offered or number of persons served?

Mr HOSTETTER Well, as the town grows, we will grow with it But that original system was a 12-channel system We now have either a 36- or a 40-channel system in both Tiffin and Fostoria We had an intervening step where we had a 25-channel system

Senator METZENBAUM What is the normal number of outlets? In other words, 30, 25, 40?

Mr HOSTETTER Channels on a system?

Senator METZENBAUM Yes, channels

Mr HOSTETTER Thirty-six is probably the standard today There are some, I mean, we have systems with over 80-channel capacity But 36—I think throughout our systems in Ohio we have a 36- to 40-channel standard

Senator METZENBAUM Explain this to me because I am not too hep as to what happens with these VCR's, et cetera My recollection is that the VCR that we have does not have 36 different buttons on it It has maybe 18 or so How is that handled?

Mr HOSTETTER If you have a VCR, in addition to giving you a converter to operate your set, we will probably have to give you a converter to operate your VCR So that you will not use the tuner on the VCR, you will use it on our converter

And by way of remaking a point, instead of you being a household that would cost $150 to $200 to install, we have got to double that because you want to also serve your VCR

If I may, Senator, picking up on a question to Mr Mooney about rates I would just like to make one point on that Any year-to-year comparison is really tough You do not know what the date of the last rate increase is

I sat here and did a back of the envelope calculation In 1965, when we started in Tiffin and Fostoria, our rates were $5 95 a month and we offered a 12-channel service Today our rates there are approximately $14 and we offer a 36-channel service CPI, which is a series that started in 1967, so it was a couple of years after we started, basis 1967 of 100 is currently 340 So if we had simply kept our rates up with the CPI, our $5 95 rate would now be $20 23 It is not It is $14 and we have tripled the number of channels we are offering

So I think there is an element of demagoguery in—not, please be sure, not suggesting by the chair or the committee, but by those who criticize cable's rate pattern We have been incredibly restrained And I would point out for Mr Finneran's benefit, the record of State rate regulation was that in those States that regulated rates, rates were higher than in those States that did not regulate rates

Senator METZENBAUM Could you describe for us the trend of Continental's prices since cable was deregulated on January 1, 1987? In other words, what has been the percentage increase in your company's prices since that time?

Mr HOSTETTER I would be happy to Our average basic rate in the State of Ohio on the last day of 1986 was $13 51 Our average rate on the last day of 1987 was $14 90, a 10 3-percent increase Now our typical subscriber also buys a pay unit so that his bill was the $13 plus $9 for pay, approximately $22 We slightly lowered our pay rates from $9 72 to $9 70

So the average Ohio customer's bill increased almost exactly 5 percent in the year 1987, in the year from the date of deregulation to a year later That is only slightly above the CPI change for that year, and I think is a much more typical pattern both of us nationally and of the cable industry nationally than some of the specific examples that have been cited

Senator METZENBAUM I have some additional questions We may submit them to you in writing, Mr Hostetter We are very happy to have you with us today

Mr HOSTETTER I would be happy to respond, and I thank you for the opportunity

Senator METZENBAUM Our next witness is Mr Robert Thomson, vice president of government affairs, TCI, Denver, CO

STATEMENT OF ROBERT N THOMSON

Mr THOMSON Good to see you again, Mr Chairman

Senator METZENBAUM Good to see you, sir

Mr THOMSON Since I am batting cleanup, I am not going to summarize my statement in any detail But I would like to focus on one or two of the issues that the other panelists have yet to touch on

I would like to commend its reading, particular with respect to its description of the competitive environment which we think we operate in In that competitive environment, broadcasting stations are clearly the dominant competitors

With respect to our pay services—and I am sure Mr Collins would agree with this—the VCR industry is a substantial competitor As you may know, there are more television households that have VCR's now than those that have cable In addition, in the VCR industry they have an earlier exhibition window than do our pay services, 3 to 6 months after a theatrical appearance a title will appear in a VCR store, as opposed to an average of 12 months for our premium services

I would like to spend a little bit of time on the competitive impact of the home satellite dish industry There are essentially four issues, Mr Chairman, that have been discussed, the growth of the industry, access to programming, the prices that are available to customers in the home satellite dish industry, and the distributors that are allowed to distribute the product

You have already received information on growth The growth in the industry, as a matter of fact, has been quite phenomenal There are a lot of dish owners out there

As far as access to programming, they get all cable programming and more It is true that some of the services are scrambled But now that the scrambling technology is widely available, and there has been a settlement on a standard, access we do not think is going to be a long term problem unless the security of the encryption system is breached If that happens, then access will once again be a problem

As far as the prices, as you noted, my statement does say and our price list for TCI programming does indicate that home satellite dish owners can receive a basic package of programming which is very, very similar to that which our cable subscribers receive, for much less money, approximately two-thirds the cost

TCI is not unique in that pricing practice That is common to other cable companies and other distributors It is the retail prices here that are important It is the consumer, we would suggest, that we should be concerned about And the retail prices to consumers are less

In addition to that, when we talk about distributors, there are at least—I would suggest that there are now 20 distributors available that are active now in the home satellite dish marketplace Only a very few of those are connected with cable

As a matter of fact, cable is getting its lunch eaten in this particular marketplace Only 5 percent of home satellite dish programming is sold by cable operators, 50 percent is sold by equipment—that is satellite equipment—wholesalers and distributors The dish dealers themselves sell 20 percent or 25 percent And Mr Collins and Showtime and the others sell the rest directly We do not monopolize this home satellite dish industry programming business by any stretch of the imagination

As far as our business practices and policies and how we have responded to what we consider to be a very, very competitive market, I suggest to you that one of the first weapons we have used to compete is our pricing policy We think we have low prices, some of the lowest in our industry Last year we increased prices 6 percent after deregulation kicked in This year we increased 5 percent, approximately at the rate of inflation

I am going to stop now You may have other questions for me, and I will let you set the agenda from here on

[The prepared statement of Mr Thomson follows]

Statement of Robert Thomson

Vice President

Tele-Communications, Inc

Mr Chairman and Members of the Subcommittee, my name is Robert Thomson, Vice President of Tele-Communications, Inc ("TCI") in Denver, Colorado TCI is an operator of cable systems throughout the United States

Thank you for the opportunity to testify this morning and to give our views on a number of issues that now affect our industry When an industry grows as rapidly as the cable industry has in the past few years and is so highly visible, we can understand why you, Mr. Chairman, and other Members of your Subcommittee would want to keep yourselves current on developments Consequently, TCI is pleased to participate in this process

We believe your study will reveal an industry that is entrepreneurial and competitive in the extreme and whose investments and creative efforts have yielded substantial benefits for the television viewing public

In my statement today, I first would like to focus on the competitive environment in which the cable industry operates Since this environment shapes the business decisions of cable operators and programmers, it is key to understanding how and why the industry works Against that backdrop, I will discuss some of the business practices and policies of TCI, which represent our attempt to succeed in this competitive environment Finally, I will briefly discuss some of the specific issues that are likely to be raised in your hearing today

A COMPETITIVE OVERVIEW

The cable industry is in the business of providing televised entertainment, news, sports, and information programming to homes and commercial establishments In so doing, it competes with numerous other alternatives for consumers' leisure time and dollars

Cable obviously faces the most direct competition from other video programming alternatives First and foremost among these video alternatives are over-the-air television stations -- both local network affiliates and independent broadcast stations In virtually all of our franchise areas, potential cable viewers can receive three or more broadcast stations Although cable programming over the years has made dramatic inroads in increasing the number of cable subscribers, broadcast stations continue to account for the overwhelming share of viewing audiences In spite of our offering of 30 or more channels of cable service, our subscribers spend 53 percent of their viewing hours watching the three broadcast networks and 16 percent watching local independent or public broadcasting stations

The cable industry has grown in recent years, but the broadcast industry remains strong and healthy, judging from market activity Notwithstanding changes in the tax laws and the stock market correction, 1987 was a record $7 5 billion year in station sales Television sales in 1987 on a per station basis averaged approximately $28 million, an increase from $21 million in 1986 and very close to the 1985 zenith of $33 million There is every indication that station values will continue to appreciate

Ironically, some measure of this current health must be attributed to the cable industry, which under regulatory requirements, such as the "must-carry" rule, had to provide certain local over-the-air broadcast signals to cable viewers Under the current "must-carry" rule, cable systems are required to facilitate over-the-air television viewing Cable systems must install A-B switches for new subscribers which enable them to switch off cable and to receive broadcast signals directly We are also required to educate our subscribers in the use of the switch and to inform them of over-the-air television alternatives to cable services

In the process, TCI and other cable companies have made UHF independent stations much more powerful competitors than they otherwise might have been by extending their reach far beyond the geographic area in which the broadcast signals could be received by antenna As a result of expanded viewership, these stations also benefit from increased advertising revenues, which enable them to be significantly stronger competitors to cable within their off-air service areas

Cable's premium or "pay" movie services (only a decade ago the unique feature that propelled cable growth) are particularly affected by competition from the video cassette industry Today, more American homes have VCR's than have cable Prerecorded videocasette movies are widely available for rental prices as low as $ 99, even for movies not available on cable

The VCR industry has a number of other competitive advantages over cable In competing for viewing audiences, the VCR industry usually has an earlier distribution window for recent Hollywood movies For example, the window for VCR rentals is as early as 3-6 months after theatrical release, but cable programming services must wait up to 12 months to exhibit the same product Modern video superstores carry at least 7500 titles This compares to a movie channel on cable which generally shows between 50 and 100 movies a month Video tapes can be watched at the viewers' leisure, but cable movies are only available when scheduled Finally, the VCR industry has the option to capitalize on whatever marketplace there is for movies unsuitable for over-the-air or cable transmission

Another rapidly growing alternative to cable is the home satellite dish ("HSD") industry The HSD industry is today competing with cable by distributing the very same programming that cable itself has developed over the years with investments of hundreds of millions of dollars

Since HBO became the first programmer to scramble its signal in January, 1986 -- in a very real sense creating today's industry -- a standard scrambling technology has emerged, and despite early shortages, descrambling equipment is today widely available at prices that continue to decrease over time The HSD industry has grown dramatically since this time, today, there are almost 2 million home satellite dish owners in the United States

Recognizing the growing importance of the HSD industry, TCI has been a leader in efforts to market satellite programming to these viewers Although TCI and other cable companies have the rights to sell cable programming to HSD owners in their franchise areas and adjacent counties, only a small percentage of dish owners actually buy their programming from cable operators Recent market research we have done indicates that at least 20 companies are marketing cable programming to HSD owners nationwide, with 50 percent of the programming sold by HSD equipment wholesalers and manufacturers, 25 percent sold by equipment retailers, 20 percent sold directly by the programmers themselves and only 5 percent of HSD programming sold by cable operators

Not surprisingly, given this range of purchasing options, HSD owners currently receive cable programming at retail prices far below that which cable subscribers pay For example, HSD owners who purchase programming from TCI pay $10 50 a month to receive virtually every basic service TCI's cable subscribers pay around $15 00 a month on the average for similar programming An HSD owner can buy basic programming services plus HBO or Cinemax from TCI for $16 00 A comparable package costs cable subscribers around $23 00

Another growing source of competition for cable operators is from multi-point, multi-channel, distribution systems ("MMDS") and satellite master antenna television ("SMATV") services, which offer additional distribution methods for satellite programming Other distribution technologies, such as direct broadcast satellites, are likely to be available in the near future

Telephone companies also compete with cable Notwithstanding public perceptions, current law allows all telephone companies except for AT&T or the Bell operating companies to provide cable service anywhere outside their telephone service areas or, with an FCC exemption, even inside their service areas In fact, there is a built-in exemption for phone companies to serve any uncabled rural areas within their service areas Electric utilities are becoming increasingly interested in cable, for example, Florida Power and Light is actively overbuilding existing cable companies

This brings us to another source of competition for cable operators -- other cable operators Cable television franchises are typically non-exclusive Overbuilding, where two cable systems compete head-to-head to attract viewers, has become a fact of life in our industry

B TCI'S RESPONSE TO COMPETITIVE REALITIES

TCI's business policies and practices are based on our realistic view of this competitive environment and of the cable product we sell Cable programming is important to many consumers, but not at any cost In economic terms, the demand curve for our product is highly elastic, since at certain price levels many viewers will turn instead to the range of alternatives described above

Cable operators are not utilities with guaranteed rates of return on investment for providing, on an exclusive basis, an essential lifeline service No cable company is guaranteed any return on its investment Moreover, cable service is not an absolute necessity to anyone Even in those areas where cable services are available, half of all households choose not to subscribe Obviously, to sell our service we must convince people that we offer value equal to the the cost of our service

TCI's financial performance depends on convincing the potential viewers who live in our franchise areas to exercise the option that each has to subscribe to cable In recent years, TCI has taken a variety of steps to achieve this goal and has seen some measure of success in the rising level of cable penetration

As a first step, TCI tries to keep its prices as low as possible, both in absolute terms and also in relation to our competitors Currently our systemwide average rate for basic service is less than $15 00 a month Almost all TCI systems that increased prices at the beginning of this year did so only at the rate of inflation TCI would obviously like to be able to recover increased costs through price increases whenever possible But the reality is that competition and local economic factors, not TCI's corporate policies, will have the determinative influence on future pricing decisions

It is relevant to note that TCI's revenues per subscriber are lower than most other cable companies In a study released late last year, our company ranked 19th out of the top 20 multiple systems operators ("MSO's") on a revenue per subscriber basis and 36th out of 53 cable companies measured Whatever economies of size we enjoy, we pass on the savings to our subscribers This is good business and good for consumers

Of course, the cost of cable services to subscribers includes more than just the basic rate, and TCI also seeks to control these other components as well For example, it is one of the few companies that does not collect a monthly fee for extra cable hook-ups Cable companies that do levy such charges normally collect $3 00 to $6 00 a month from a subscriber for each additional television set hooked up in a residence, in addition to their regular charges In addition, every TCI cable subscriber receives a monthly cable magazine (Cablevision) without any additional charge

Like other cable companies, TCI has as one of its top corporate objectives improvements in the service and the programming we offer our subscribers We believe that our business will be more competitive -- and more successful -- if we continue to improve the quality of the product we sell With respect to service improvements, TCI generally uses internally generated cash flow These funds are used primarily for increasing the channels and picture quality on our systems, extending cable to underserved areas, improving telephone and other administrative systems, investing in technological research and development, and training of customer service representatives and other system personnel

Implementing this program involves significant financial costs It is important to recognize in this context that the cable industry is still making capital investments to extend our cable to those who want it Although it is possible now to foresee a day when all subscribers who can economically be served by cable are served, TCI and other cable companies are still spending enormous amounts of money on new-builds, line extensions, upgrades and rebuilds For example, TCI will spend $240 million in 1988 alone for those purposes, including cost-intensive inner-city construction in major metropolitan areas like Chicago and Washington, D C TCI will build and improve enough miles of cable this year to stretch halfway around the world

As we complete our program of system builds, more and more resources will become available to improve other aspects of our operations, such as telephone service and training of customer service representatives and installers Since we have no guaranteed rates of return like a utility offering telephone or electric service, all these investments come at the expense of bottom-line, near-term profits None of our cash flow goes to shareholders, TCI has never declared a dividend

An equally important part of TCI's competitive strategy is to expand the range and quality of programming available to cable subscribers and to do so in way that creates an attractive body of "cable-unique" programming that will draw viewers to cable systems as opposed to other available alternatives TCI has no controlling interest in any programmer Our company does not manage any programming entity, nor does TCI, as a corporate objective, seek to become a programmer However, we are committed to the concept that, given the number of video distribution technologies described above, the best way for cable to distinguish itself in the mind of the viewing public is to develop new and attractive programming options

TCI has "put its money where its mouth is" by making several types of programming investments in recent years One of the earliest examples of innovative programming pioneered by cable is C-SPAN I and C-SPAN II, which is funded primarily by cable companies TCI is proud to have been one of C-SPAN's founders As you know, these services televise proceedings of the House of Representatives and this body and other governmental and public interest proceedings in a level of depth never contemplated by the commercial television networks

A more recent example of cable industry involvement to create new programming services is the bridge financing we and other companies are providing to the Vision Interfaith Satellite Network (the VISN Channel), which will launch this summer VISN has been organized by mainline Protestant, Roman Catholic, Orthodox and Jewish groups to allow each group to reach cable subscribers with religious and values-based programming more efficiently, without on-air solicitations or criticisms of other religious views

Second, TCI has made certain minority investments in a number of programming services which reach certain categories of subscribers who have been generally underserved by broadcast television in the past These include our non-controlling investments in the Black Entertainment Television Channel, The Discovery Channel, which features quality nature, scientific and technology programming, and American Movie Classics, which features movies with substantial artistic merit

Third, TCI and other cable companies have made timely minority investments in high quality programmers that are exceptionally popular among cable subscribers, but are threatened by adverse business circumstances Last year, a consortium of cable companies made a substantial investment in the Turner Broadcasting Company ("TBS") to help that company survive Ted Turner and TBS have made substantial contributions to the cable industry through programming services such as CNN and CNN-Headline News Thanks to the cable operators' investment, TBS will continue to offer new services such as TNT -- Turner Network Television -- which will make its debut this fall

In making this investment, all of us were concerned that the programming brilliance of Ted Turner and his associates might disappear from cable Fortunately, it now appears this will not happen

Fourth, cable companies have begun to explore investments in which particularly creative individuals might develop programming for the existing cable networks TCI and other companies recently announced start-up funding for such a company called Think Entertainment headed by Shelly Duvall The industry is also experimenting with various home shopping formats and testing the appeal of these services among our subscribers

Before turning to some of the specific issues that might be raised before this Subcommittee, I would like to make one more point about programming TCI has always considered itself to be a particular friend of public broadcasting For many years, we spent hundreds of thousands of dollars to microwave PBS stations in the West to remote communities that had no local PBS outlet At the same time, we are exploring ways that TCI can help local PBS stations get on their feet in states, like Montana, that previously had to rely on an imported PBS signal

We will continue to be supportive of public broadcasting in the public interest, but also in our own parallel interest, since the PBS stations reach an audience of potential cable subscribers

C SPECIFIC ISSUES FACING THE CABLE INDUSTRY

Finally, Mr. Chairman, I would like to address some of the specific issues that are likely to come up during the hearing today

First, there are a number of issues involving the broadcast industry that routinely come up in forums of this sort, the most important of which is carriage of broadcasting stations by cable operators TCI supported the FCC "must carry" signal carriage rule that was recently invalidated by the Court of Appeals here in Washington You will recall the rule was loosely based on an inter-industry agreement Our trade association filed briefs in support of the rule on appeal and TCI itself was on a brief opposing a stay of the Rule pending its appeal Assuming appeals to the U S Supreme Court are unsuccessful, TCI would support a legislative solution to the "must carry" controversy as long as the legislation was again based on discussion among all affected industries and was tied to codification of cable's rights in other areas

As indicated by the controversy concerning the "must-carry" rule, particularly difficult broadcasting issues have arisen concerning cable carriage and channel placement Despite significant recent investments by cable operators to expand the channel capacity of existing systems, a large number of such systems are still limited to less than 36 channels The resulting limitations mean that cable systems sometimes simply cannot carry all the programming that they might wish

From the cable operator's perspective, these issues primarily involve marketing decisions--how can the limited channel capacity be used most effectively to attract and retain viewers to the cable system This involves weighing the benefits of various programming options, as well as considering how various channel positions could be used as part of marketing plans (e g , grouping various pay cable services on adjacent channels)

Not surprisingly, these considerations sometimes conflict with the interests of programming suppliers A common charge made by broadcasters and others is that cable companies which have investments in programming disproportionately carry these programmers and do not carry others That is not the case with TCI Those programmers in which TCI has a minority investment are no more likely to be carried on TCI systems than any of the others To us, subscriber appeal dictates carriage, not our investments

Similar issues are raised by channel placement For example, independent UHF stations have routinely asked federal authorities, in effect, to order their cable carriage on VHF cable Channels 2 through 13, assuming that these channels maximize their potential viewing audience In many cases, mandated VHF carriage on cable would create a clear windfall for broadcasters who bought and paid for a less valuable UHF station

Clearly, on-channel carriage, where a particular station will be found on the same channel both over-the-air and on cable, seems to be the best solution to most channel placement disputes However, in cases where the station's assigned broadcast channel is higher than the channel capacity of the cable system, a different solution must be found

A related problem occurs in major metropolitan areas, where there are several cable companies that may carry the same UHF station If each cable company carries the station on a different channel, the UHF station owner may find it more difficult to market his station throughout a metropolitan area Of course, this is a function of a fragmented cable industry, with many different operations in a metropolitan area Cable programmers face exactly the same problem

We have experienced such a situation in the San Francisco Bay area where TCI is one of many cable companies operating systems Many of our systems there have 36 channels KBHK, Channel 44, now cannot be carried on-channel on our systems and other systems with similar channel capacities TCI has attempted to accommodate Channel 44 by carrying it on cable Channel 22 in as many of our systems as we can The best solution in cases of this nature is for the cable companies and the broadcaster to work out a system of common channel placement through private discussion It is my understanding such discussions are underway in the Bay area with Channel 44

In addition to the broadcast issues discussed above, the Subcommittee is likely to hear discussions of the difficulties that alternative delivery systems allegedly have in obtaining rights to sell cable programming Although these are issues that should be addressed by the programmers themselves, TCI does offer the following comments

The statistics I have cited above should already indicate that in the HSD industry, there is a great deal of programming available to dish owners from many different sources at retail prices generally less than that which cable subscribers pay As long as there is a relatively secure encryption system in place, this will continue to be the case, for programmers will have the incentive to create new programming secure in the knowledge that they will be able to achieve a return on their investment On the other hand, if encryption security is breached, then TCI believes HSD programming availability will suffer In our view, no programmer will provide, nor can it be expected to provide, its product to a medium where that product is regularly and systematically stolen

TCI strongly endorses the programmers' rights to prevent breach of their sales contracts and blatent theft of their products We cannot ask our cable subscribers to pay for programming services that are available without any payment to their friends and neighbors

D <u>CONCLUSION</u>

This is a new industry, rapidly growing and rapidly changing As in any such industry, what was gospel yesterday can become heresy tomorrow To legislate or regulate in such a rapidly changing environment is to risk creating artificial rigidities that will work against consumer interests

Instead, consumer interests are best served by allowing the market to work its magic -- creating incentives to identify and satisfy consumer needs and desires Of course, individual producers and suppliers will not all prosper, but those who correctly perceive what the marketplace wants will do well

In the interim, there will be numerous disputes and points of contention or stress, and each of the relevant players -- cable operators, programmers, the creative community, commercial television networks, independent broadcast stations, public television stations, SMATV, MMDS, etc -- will have its own perspective, its own solution For our part, TCI is always willing to listen to those with different perspectives, working toward solutions that all can live with Hearings like this will help that process, and I will be glad to answer any questions you might have

Senator METZENBAUM Thank you, Mr Thomson You have heard the home satellite dish industry complain that some programming is available only through cable According to the October 1986 Channels magazine, TCI actively intervened to try to prevent programmers from directly selling to home dish owners Did not TCI then turn around and market its own package to dish owners?

Mr THOMSON I think the article is incorrect As a matter of fact, today the programmers do market directly to home satellite dish owners They sell more programming, approximately four times more programming than all of the cable operators do

It is true that we do market a home satellite dish package to dish owners in our adjacent areas But you must keep in mind that we and all other cable companies have been limited by market arrangements to only our franchise area and adjacent counties We are not allowed to sell nationally like the other third-party packagers are, and that is a tremendous competitive disadvantage for cable in serving this marketplace

Senator METZENBAUM Where does that limit come from?

Mr THOMSON From the programmers

Senator METZENBAUM From the programmers So that the programmers are restricting the competitive potential for your company?

Mr THOMSON You could put it that way But on the other hand, there is a number of national distributors which the programmers have authorized in one way or another to do business I am not saying that that is an unreasonable restriction They have a difficult situation to deal with because they have a lot of people who want to distribute their programming, as you heard today

Everybody can get access to movies from Hollywood What they want though is access to the HBO brand name That is the key And I have all the sympathy in the world for the HBO's and the Showtime's of the world trying to make their way through this thicket

Senator METZENBAUM I am sure they appreciate your sympathy, but I think they are doing pretty well without the sympathy, are they not?

It is my understanding that Netlink offered a contract to the National Rural Telecommunications Cooperative in connection with programming packages that the cooperative was offering to home dish owners Before the contract was completed, as I understand it, TCI bought a controlling interest in Netlink and the contract offer was withdrawn True? False?

Mr THOMSON Absolutely true And here is the circumstances Netlink—you want me to respond in detail, I take it, because it is a detailed story Netlink when they were first in business were not in any way associated with TCI Their intention at that time was to uplink, without restriction, network affiliates and let any dish owner that lived anywhere order these network affiliate signals

They came to TCI and requested financing and talked about a mutual business relationship We decided that we would want—that we thought it would be a good idea to finance them for reasons of our own The problem was that their method of business was under attack in Federal court here in New York State and also in Atlanta by the networks themselves because it represented an unlicensed distribution, even in areas where local affiliates showed network programming Consequently, when TCI got involved, we insisted that the previous business plan upon which their contact to NRTC had been based, be scrapped

Now we are in the process of actually negotiating with the networks for the right to use their signal and to distribute to "white area" dish owners Until those contracts are negotiated, we are not at liberty to entertain the request by others to distribute the programming As soon as those contracts appear in their final form, we will be happy to revisit that issue

Senator METZENBAUM When will that be?

Mr THOMSON That is hard to say It is up to the networks, to some extent We anticipate we will have more word on that in 3 or 4 weeks

Senator METZENBAUM TCI is rapidly developing an image as the monolithic king of the heap in this industry As a matter of fact, I think you are a leader in the trend toward vertical integration As I understand it, you hold an equity stake in a number of major programmers, including WTBS, CNN, Headline News, BET, Temple TV, the Fashion Channel, American Movie Classics, and Home Premiere

Several of the programmers which TCI controls in whole or in part refuse to deal with cable competitors True or false?

Mr THOMSON We are not ashamed of the fact that we have taken our subscribers money and used it to improve the quality and variety of programming Using the term vertical integration to describe the minority investments that we have in programming is probably not exactly correct We do not own any programmers We have no controlling interest in any programming entity We have no corporate objective to become a programmer Others do that job much better than we do

However, we have never had a subscriber complain to us about taking their money and using it to improve the quality and quantity of programming

Senator METZENBAUM That is really not the question, Mr Thomson You are not meeting the issue The issue is, it is not a question of whether you are taking your subscriber's money The subscriber has no control at all over what you do with your money If you want to take your money and buy a jet plane, you want to take a trip to Bermuda, that is your problem

The real question is vertical integration Vertical integration is a concern of this committee, and I do not think you are addressing yourself to that question, and I appreciate if you would

Mr THOMSON I am saying, Mr Chairman, that we have really no control over any of these programs We do not have a controlling interest over any programmer We essentially make four types of——

Senator METZENBAUM What percentage position do you have in CNN?

Mr THOMSON We have approximately 12 percent of all Turner, but we have a minority—all the cable companies together only have a minority interest in Turner Turner would, of course, have disappeared from the airwaves but for the cable investment in Turner

Senator METZENBAUM I could go through each of them that I mentioned, and what is the range of ownership position you have in each?

Mr THOMSON As I said, it is always less than 50 percent I would be happy to provide that for the record I will give you some idea——

Senator METZENBAUM You know as well as I do, you do not have to own 50 percent in order to have control General Motors was controlled for years by one family that had an infinitesimally small percentage position Generally speaking, most American corporations are controlled by individuals or groups that have far less than 50 percent

Mr THOMSON That may well be the case in general corporate life, but I would say to you that we neither have control in fact nor control in votes with these programmers

Senator METZENBAUM All right Thank you very much, Mr Thomson I want to thank the rest of the panel I appreciate your being here with us today

We will now proceed to our last panel, Gary Chapman, senior vice president, Freedom Newspapers, on behalf of the National Association of Broadcasters, from Riverside, RI, Milt Maltz, a friend of mine from Cleveland, Malrite Communications Group, on behalf of the Association of Independent Television Stations, from Cleveland, OH, Wendell Triplett, from WWAT–TV, Chillicothe, OH, and John Siegel, president of KBHK–TV, San Francisco, CA

We are very happy to have you with us Mr Chapman, would you be good enough to proceed, please?

STATEMENT OF A PANEL CONSISTING OF GARY CHAPMAN, SENIOR VICE PRESIDENT, FREEDOM NEWSPAPERS, ON BEHALF OF THE NATIONAL ASSOCIATION OF BROADCASTERS, RIVERSIDE, RI, MILTON MALTZ, MALRITE COMMUNICATIONS GROUP, ON BEHALF OF THE ASSOCIATION OF INDEPENDENT TELEVISION STATIONS, INC., CLEVELAND, OH, WENDELL TRIPLETT, WWAT-TV, CHILLICOTHE, OH, AND JOHN SIEGEL, PRESIDENT, KBHK-TV, SAN FRANCISCO, CA

Mr CHAPMAN Thank you, Mr Chairman First, I want to thank you for inviting me to testify today on the competitive issues of the cable television industry My name is Gary Chapman, and I am senior vice president of broadcasting for Freedom Newspapers, which owns five VHF television stations in five different States

I am also appearing on behalf of the National Association of Broadcasters, which represents 950 television stations, all the commercial networks, and over 5,000 radio stations I presently serve on the NAB television board of directors We welcome the subcommittee's interest in these important issues and commend you for holding these hearings

To summarize what has happened in the local video marketplace, an essentially level playing field has been radically tipped in favor of cable For purposes of copyright law, cable is treated mostly as a passive antenna device that simply retransmits signals Within the context of the must-carry litigation, however, cable is treated as an active editor which can wield the sword and shield of the first amendment So long as cable can exist under the best of both worlds treatment, it has the legal and regulatory upper hand

Policymakers should be troubled by this situation, especially those with jurisdiction over competitive issues These are the cards with which the local cable operators can play when he sits down with our television stations

In our markets, cable penetration runs from a low of 50 8 percent in Beaumont/Port Arthur, TX, to a high of 61 5 percent in Albany/Schenectady and Troy He can decide to carry our stations or not carry our stations As a result, the cable system have their thumbs on the scales of competition within the local video market

Through its carriage decision, the system directly can determine what its subscribers view, and indirectly can affect the quality of what nonsubscribers view Thus, it affects the overall competitive status of all local television stations whether they appear on the system or not

This subcommittee should question whether cable should be permitted to possess such power, much less exercise it He can cherry-pick a portion of our programs He will not have to bargain for or pay for their carriage rights, although he can seek payment from us for carriage He can decide to carry our stations on our channel numbers or he can ship them up to the equivalent of Siberia

He can bring the same network programming that is carried on our stations through the network affiliates licensed to larger cities relatively nearby our markets, such as the case of Providence/New Bedford He can bring in distant signals or superstations which also may duplicate the programs which our stations have paid a great deal to acquire the exclusive rights

Consider the experience of our Medford/Klamath Falls television stations We have purchased the rights to broadcast "Cheers," "Family Ties," and the new version of "Star Trek" in syndicated form Prior to 1980 when the FCC syndication exclusivity rule was in place, we would have been able to protect these exclusive rights by requiring local cable systems to delete these shows from any nonlocal signal that they were importing into our market

The circumstances are far different today now that synd-ex rule is gone Through cable's ability to import distant signals under the compulsory license, and our inability to protect our bargained for exclusivity, local cable systems are able to import stations from Portland, Oakland, Sacramento, each with these same three programs And additionally, some systems carry superstation WGN which airs "Cheers"

He competes with us for local and national advertising dollars He can make any and or all carriage decisions based on what makes him a better buy to the advertising community

For example, one of our stations operates in Albany/Schenectady/Troy television market In Albany, our station is carried on a system owned by ATC, whose parent is Time Time also owns 100 percent of HBO, 100 percent of Cinemax, 100 percent of Festival, 11 5 percent of superstation WTBS, 11 5 percent of CNN, 11 5 percent of Headline News, 16 percent of Black Entertainment Television And a similar situation also exists with Mr Thomson's company in Schenectady where a similar situation exists

Regulatory equilibrium between local television stations and cable must be restored At least two elements are needed for this restoration, some degree of must-carry protection for local television stations, and the reestablishment of the syndicated exclusivity rules Pending at the FCC——

Senator METZENBAUM Please wind up, Mr Chapman

Mr CHAPMAN [continuing] Is a proceeding which could result in the reimposition of the synd-ex rule The NAB strongly supports this result Also, the must-carry issue may be more problematic The NAB and other broadcasting interests are pursuing legal remedies available to us following the December decision in the court of appeals

The NAB believes that Congress also should consider legislation to implement some form of must-carry We feel that that will properly craft——

Senator METZENBAUM Mr Chapman, I have to cut you off

Mr CHAPMAN Thank you, Mr Chairman

[The prepared statement of Mr Chapman follows]

National Association of
NAB
BROADCASTERS

TESTIMONY OF
GARY R CHAPMAN
SENIOR VICE PRESIDENT, BROADCASTING
FREEDOM NEWSPAPERS, INC , RHODE ISLAND

BEFORE

THE SUBCOMMITTEE ON ANTITRUST, MONOPOLIES AND BUSINESS RIGHTS
OF THE SENATE JUDICIARY COMMITTEE

ON

COMPETITIVE ISSUES IN THE CABLE TELEVISION INDUSTRY

MARCH 17, 1988

Thank you for inviting me to testify today on competitive issues and the cable television industry. My name is Gary R. Chapman, and I am Senior Vice President, Broadcasting, for Freedom Newspapers, Inc., in Rhode Island. Freedom Newspapers owns 5 television stations in five different states.[1] From 1979 through 1984, I was General Manager of WLNE, Freedom's station in the Providence/New Bedford television market.

I also am appearing on behalf of the National Association of Broadcasters, which represents over 950 television stations, in addition to all of the major commercial networks and over 5000 radio stations. I presently serve on NAB's Television Board of Directors. We welcome the subcommittee's interest in these important issues and commend you for holding these hearings

Background

As you already have heard today, the status of the video marketplace in 1988 is dramatically different than it was just a few years ago. This is especially true regarding the relationship between local television stations and cable My testimony will focus on one aspect of that particular segment of the video marketplace, how the loss of the must carry rule affects the ability of local television stations to serve the viewers in their communities

Prior to 1980, cable and television broadcasters were on a relatively even footing. The Federal Communications Commission's must carry rule assured local television stations that they would be carried on the cable systems serving their markets For cable, the compulsory license granted by the 1976 Copyright Act entitled cable systems to retransmit local television stations without negotiating for the rights to do so, and without any payment to those local stations. This compulsory license also entitled cable systems to carry distant signals without negotiating for these retransmission rights, at rates set by the government

This statutory compulsory license reflected the FCC's existing regulatory structure. At that time, the FCC had other important regulations in place in addition to the must carry rule These included restrictions on the numbers of distant signals cable systems could import into markets, and protections against the importation of programs for which local stations already had exclusive rights (the "syndicated exclusivity" rule)

To be sure, this system was not without its flaws for both broadcasters and cable, and it perhaps was not the structure that would be created in a perfect world Whatever its flaws, however, the old system was far superior to the regulatory and legal conditions under which local television stations operate today.

By 1980, the FCC had eliminated the distant signal and syndicated exclusivity rules, but the must carry rule remained in place as an important counterweight to the compulsory license As you know, however, in 1985 the Court of Appeals for the D C Circuit threw out the FCC's original must carry rules on First Amendment grounds, and the same Court invalidated the FCC's revised must carry rules in December, 1987, again on First Amendment grounds.[2]

In what are perhaps now cliched Washington terms, an essentially level playing field has been radically tipped in favor of cable. For purposes of copyright law, cable is treated mostly as a "passive" antenna device that simply retransmits signals. Within the context of the must carry litigation, however, cable is treated as an active "editor," which can wield the sword and shield of the First Amendment So long as cable can exist under this "best of both worlds" treatment, it has the legal and regulatory upper hand. Policy makers should be troubled by this situation, especially those with jurisdiction over competitive issues

To the casual observer, must carry and the related cable issues might appear to be of relatively minor importance to my company's television stations. All of our stations are network affiliates, all are on the more advantageous VHF channels One might think that our stations are those most likely to be carried on local cable systems with or without must carry. Furthermore, if our stations are not carried, one might think they are the stations that viewers will most easily and willingly receive off-the-air Unfortunately, the real world is not that simple Carriage on cable, and cable's present ability to act as a gatekeeper over access to homes, is as important to our stations as it is to the UHF independent stations you will hear from today

Localism and the importance of cable carriage

Our nation's free, over-the-air television structure is erected on a foundation of local stations serving local communities. Rather than a system in which a greater number of regional stations could be established, Congress enacted a system through which the needs and interests of communities would be served by smaller numbers of local stations Congress' goal with localism was to ensure that each community of appreciable size would have at least one station to address community needs and interests, and to permit multiple stations in communities wherever possible This system is reflected throughout the Communications Act and FCC regulations, but finds its clearest expression in Section 307(b) of the Act.[3]

In return for their FCC licenses, television stations have statutory and regulatory obligations to their local communities Stations are obligated to identify, and serve with responsive programming, the needs and interests of those communities.

This system can not function properly, of course, unless local television stations have access to the viewers they are licensed and required by the FCC to serve. An "open gate" between local stations and their viewers must be preserved, for stations simply cannot respond to viewers that they cannot reach

Access to local audiences can be both enhanced by, and frustrated by, cable. As it originally developed, the cable industry was a means to facilitate reception of local over-the-air television stations. Indeed, cable first was called "community antenna television." Today, cable provides many additional kinds of programs, but retransmission of local television signals remains one of cable's most important attractions for subscribers

Once a home is connected to cable, however, that home becomes extremely dependent upon that cable for reception of local television stations. Even though these signals theoretically are available over-the-air, when a local television station is not carried on the cable system, cable subscribers effectively lose their ability to watch it. The cable becomes a gate, over which the local system has control.

NAB and other groups have documented in FCC proceedings why the "A/B switch," a mechanism that ostensibly selects between cable and over-the-air reception, is in fact inadequate as a substitute for cable carriage of local stations For many homes, this switch will not deliver adequate off-air reception, because the over-the-air signals are obstructed by tall buildings in urban areas, hilly terrain, or even foliage Many viewers subscribe to cable in whole or in part to get better reception of local television signals.

Even where off-air reception of local signals is possible, nearly all viewers must use an outdoor antenna with the switch In most cases, indoor antennas are inadequate Furthermore, outdoor antennas usually require substantial additional equipment in conjunction with the A/B switch

NAB's 1985 survey of cable subscribers revealed that hardly any cable subscribers had A/B switches Only 1% of subscribers had an A/B switch and an outdoor antenna. Many subscribers no longer had access to an outdoor antenna, either because they never owned one, they were told by the cable system that they no longer needed one, or they (or their cable system) removed the antenna once they subscribed. In many communities, outdoor antennas are prohibited or restricted, or viewers live in multi-unit buildings in which access to outdoor antennas is impossible or impractical. In addition, with increasing use of VCR's and other equipment that attaches to the television set, the installation and use of A/B switching devices has become exceptionally confusing and difficult.

In short, the overwhelming majority of cable subscribers would have to invest or reinvest in a costly and complex array of equipment to have access to local stations not carried by cable Once the equipment was installed, cable subscribers would have to use it correctly each time they wanted to view stations not carried on cable, rather than merely tune passively to whatever programming was on the cable. Cable systems thus have effective gatekeeper control over the availability of local stations to viewers these stations are licensed to serve.

The current nationwide cable penetration rate, the percentage of homes that subscribe to cable, is 50.5% of all television households.[4] For our stations, local cable penetration rates range from a low of 50.8 percent in Beaumont/Port Arthur, Texas, to a high of 61 5% in Albany/Schenectady/Troy, New York [5] That means that in every market we serve, more than half the homes are hooked up to cable If we are not carried on those systems, we immediately lose access to more than half our potential audience, and we must find some other way to reach those viewers.

Alternatives to cable do not exist

Carriage of stations on cable systems might not be such a crucial matter for local television stations if carriage alternatives were available. Such alternatives, however, do not exist in most communities. Cable systems almost never compete head-to-head with other cable systems in their franchise areas, a situation described by the cable industry as an "overbuild " (It is noteworthy that the cable industry uses a vaguely pejorative-sounding term to describe head-to-head competition.)

Some argue that cable is a natural monopoly in the economic sense -- that it simply is uneconomic for two systems to operate in the same area. Whether cable is a natural monopoly is essentially irrelevant, because in many communities cable has a legal monopoly, which the local franchising authority may grant under the Cable Act of 1984.[6] As a result, competition among cable systems is extremely rare. Presently, there are perhaps as many as 36 franchised cable systems (out of a nationwide total of approximately 6500) that face competition from other franchised systems

What about the other wire into the home -- provided by the telephone company? Some day telephone companies may provide video service to the home in competition with cable, but that day still is far away Many technological and policy hurdles must be crossed before video service via telephone systems is practicable.

Therefore, a television station denied carriage on the local cable system has no competing system to which it may look for carriage within a community Cable subscribers who are unhappy with the local television offerings on their system cannot threaten to take their business elsewhere Nor can the local government exercise much, if any, influence over whether local television stations will be carried on the local cable system The Cable Act severely limits the controls that local governments can exercise over the programming carried by the cable systems they franchise [7]

Cable's carriage decisions impact upon local competition

Thus, with the must carry rule gone, cable now has an important weapon at its disposal -- the discretion to carry or not to carry any or all local television stations, including the ability to require payment for carriage It is important to realize, however, that a cable system's refusal to carry a particular station affects not only what the system's subscribers view, but it also indirectly affects what will be viewed by non-subscribers. Simply put, a television station's audience size directly translates into revenue -- larger audiences attract larger revenues, through the sale of advertising time. If a station is not carried on cable, and thereby loses a substantial portion of its audience, it will lose revenue With less revenue, the station can not serve its community as well. The station will have less money to invest in equipment and programming. The attractiveness of its programming will lessen, as will its audience. Revenues will continue to decline, and the cycle will repeat.

Cable systems have their thumbs on the scales of competition within a local video market Through its carriage decisions, a system directly can determine what its subscribers view It indirectly can affect the quality of what non-subscribers view Thus, it affects the overall competitive status of all local television stations, whether they appear on the system or not This subcommittee should question whether cable should be permitted to possess such power, much less exercise it

Cable's discretion over channel-positioning can be used unfairly

The original must carry rule required, for the most part, "on channel" positioning. Now that the must carry rule is gone, cable also has virtually total discretion over where local television stations will be positioned on their systems Television stations' identities are created, in large part, around their channel numbers. While the cable channel on which a television station will be carried may not be as crucial to the station as carriage itself, the system's discretion over channel positioning can lead to competitive abuses.

Cable systems can favor some stations by transmitting them on-channel, while other stations can be shifted onto far less favorable channels, where subscribers are less likely to view them. By repositioning stations to less favorable channel positions and substituting cable networks on the more desirable channels, cable operators have the power to manipulate dramatically subscribers' viewing patterns A C. Neilsen studies are reported to show that viewership of cable networks can increase an average of 32 percent when cable networks are placed on cable channels 1 through 16. This discretion over channel positioning is especially relevant in the context of competition for advertising dollars, discussed below.

The compulsory license

Cable has many more legal and regulatory advantages over local television stations than just this crucial power over carriage and channel positioning. The compulsory license granted to cable by the Copyright Act of 1976 also provides huge competitive benefits for cable. As noted above, the compulsory license remains in place, even though the FCC regulations that were part of the balance struck by the 1976 Act have all but disappeared.

The compulsory license permits cable systems to retransmit the programming of television stations without negotiating for right to do so, and without the consent of either the station or the program owner. Cable systems can and do use this license to retransmit the signals of local stations, to import "superstations" (such as WTBS in Atlanta, WOR in New Jersey, or WGN in Chicago), and to import other distant independent or network-affiliated stations. Under this compulsory license, cable systems do not pay for the right to retransmit local programming, and pay only government-set rates for distant signals through the Copyright Royalty Tribunal, not marketplace rates.

Under today's circumstances, our stations have no right to insist upon carriage on local cable systems. These cable systems, however, can use the compulsory license to retransmit the programs of our stations, without our consent, or without payment A cable system can exercise its rights under the license to carry only a portion of our stations' programming -- we cannot insist that if any of our programming is carried, then all of it must be carried Under the compulsory license, a cable system would be permitted to "cherry pick" only those programs it wishes to carry, such as our highly-rated local news programs, and ignore the rest of our schedules.

Furthermore, these cable systems can use the compulsory license to import superstations and other distant network and independent stations. Again, under the license, this is done without the consent of, or negotiations with, these stations, at prices that are far below what might be negotiated under normal marketplace conditions

These rules mean that in the cable homes in our markets, we compete not only with other local stations and the multiple channels of cable programming carried on those systems, but also with a host of television programming imported from other markets In many cases, the programs carried on the imported stations compete directly with programs that we run on our own stations, both network and syndicated programming

While these imported stations enable the cable systems to cheaply provide additional viewing options for cable subscribers, they also siphon away local audiences Again, unlike cable, our stations' licenses carry with them the obligation to serve the needs and interests of our local viewers The revenue we generate to do so comes only from the size of the local audiences we can attract Our stations deserve a fair chance to compete with cable for the local audience. This competition should not be skewed by what in effect are cable's copyright subsidies

Network non-duplication and Syndicated exclusivity rules

The threat of inequitable competition caused by stations imported from distant markets affects both local independent and network-affiliated stations. For example, in Providence/New Bedford, our station is a CBS affiliate One of the non-local stations it competes with there on cable is the Boston CBS affiliate. For network affiliates, one of the few remaining FCC cable carriage rules -- the network non-duplication rule -- theoretically provides some protection from this type of imported competition, which can be especially harmful to affiliates located in communities within the shadow of a much larger market

Under these complicated rules, a qualifying network affiliate that is carried on a local cable system can, upon request, require the system to delete duplicated network programming In reality, however, this rule provides little protection for local network affiliates At most, it protects only the network portion of the station's schedule, not the remainder of its programming day More importantly, because the rule applies only to local affiliates carried on cable, a station will invoke the rule at its peril. Under today's rules, the quickest way for a cable system to resolve a network duplication problem is to drop the complaining station from its system Without some must carry protection, television stations cannot freely exercise even the few remaining regulations that protect the crucial concept of localism. Television stations must seek to "cooperate" with their local cable systems, which may have little incentive to be cooperative in return.

However, not even that minimal level of protection exists for syndicated programming carried by local stations -- both affiliates and independents. Consider the experience of our Medford/Klamath Falls station We have purchased the rights to broadcast Cheers, Family Ties, and the new version of Star Trek, in syndicated form As you realize, these popular shows are very desirable products for local stations, and we have paid handsomely for the exclusive right to broadcast them in Medford/Klamath Falls Prior to 1980, when the FCC's syndicated exclusivity rule was in place, we would have been able to protect these exclusive rights by requiring local cable systems to delete these shows from any non-local signals they were importing into our market.

The circumstances are far different today now that the syndex rule is gone. Through cable's ability to import distant signals under the compulsory license, and our inability to protect our bargained-for exclusivity, local cable systems also are able to import stations from Portland, Oakland, and

Sacramento, each of which carries all three of these shows In addition, these systems also carry superstation WGN, which airs Cheers. The audience we draw for these shows is substantially smaller because of this duplication. As a result, the value of our investments in these shows is much reduced. This problem exists to varying degrees with all syndicated programming in which our stations invest.

Protection for broadcasters' exclusive programming rights is essential if we are to be able fairly to compete with cable Cable recognizes how important exclusivity for its programming is to its competitive future. Unlike television broadcasters, cable is able to acquire exclusive rights to programming. As you already have heard today, it has fought hard to protect that exclusivity against competitors who seek to use its programming When broadcasters acquire exclusive programming rights, these rights also should be protected within the cable context

Incentives to act unfairly against local stations

Thus, cable has many legal and regulatory advantages over local television broadcasters The mere existence of these advantages should trouble communications and copyright policy makers Cable, however, increasingly has incentives actually to use those advantages.

As television station owners, our goal is to make our stations' programming as responsive to our viewers' interests as possible We want strong local programming -- news, public affairs, etc. -- that give our stations a distinct identity with the viewers As network affiliates, we want our network programming, both news and entertainment, to be as good as possible. We also want to air quality syndicated programming Cable would have you believe that their programming and carriage decisions are based only on the wants and needs of their subscribers, and the attractiveness of what our stations have to offer to those subscribers. Unfortunately, these are not the only factors that can enter into cable's decisions regarding whether our stations are carried, what other stations and programming services will be carried in competition with us, and where our stations will be placed in a given system line-up

Cable increasingly is competing with television for advertising dollars Although cable is a subscription service, many basic cable programming services also are supported by advertising As with network television programming, some of the advertising spots on these cable services are sold by the services, while they make other spots available for sale by the local systems that carry their programming

Cable's attractiveness to advertisers is growing Total cable advertising, national and local, was only $58 million in

1980. In 1987, total cable advertising was more than $1 billion With cable, both national and local advertising are growing at a substantial rate. Local cable advertising in 1987 was $215 million, a 269% increase from 1984, and a 30.0% increase from 1986.[8]

The mere fact that television increasingly faces competition from cable for advertising dollars is no cause for government concern If we have a fair opportunity, we will compete for advertising with cable as we do with other media. Cable has been given distinct legal and regulatory advantages over television, however, so that fair competition may not be possible Cable systems can be programmed in ways that make cable time a more attractive buy for advertisers than television time

The obvious way a system could encourage advertisers to buy advertising on cable rather than television is to refuse carriage to local stations that compete with the system for advertising The system could replace a local station with a distant signal that carries similar programming, but with which the system does not compete for advertising Even if local stations are carried, they can be placed on the less desirable cable channels, while distant stations and the favored cable channels can be placed on the more desirable channel locations

Cable systems increasingly are clustering popular television stations on channels nearby the channels of the cable services whose viewing (and hence advertising potential) the system wants to promote Fortunately, our stations have been popular enough -- primarily because of our strong local news programming -- that we are being used as anchors around which cable systems are clustering such cable programming. Many stations, especially smaller independents, are not always so fortunate in their channel positioning. There may come a time when our stations will not be granted favorable locations, either. As cable systems develop their own local news channels, complete with advertising, we may find ourselves subject to strikingly different carriage circumstances

In addition to the general proposition that all cable systems are increasingly competing with television for slices of the local and national advertising pie, certain cable systems have more direct incentives to favor cable programming over television programming Segments of the cable industry are becoming more vertically integrated -- some corporations that own cable systems also are becoming more involved with cable program production. Cable systems owned by such companies now may have direct incentives to favor their parents' programming over programs offered by television stations

For example, one of our stations operates in the Albany/Schenectady/Troy market in New York In Albany, our station is carried on a system owned by ATC, whose parent is Time, Inc. Time also owns 100% of HBO, 100% of Cinemax, 100% of Festival, 11.5% of the superstation WTBS, 11.5% of CNN, 11.5% of Headline News, 16% of Black Entertainment Television, and assorted other interests. In Schenectady, our same station is carried on a system owned by TCI. TCI also owns 50% of AMC, 10.1% of WTBS, 10.1% of CNN, 10.1% of Headline News, 14% of Discovery, 16% of Black Entertainment Television, 10.5% of the Fashion Channel, and assorted other interests [9]

This direct relationship between cable program production and distribution is one of the more troubling features of the bumpy competitive landscape over which local television stations must travel.

To summarize my testimony, these are the cards with which the local cable operator can play when he sits down with our stations: He is in at least 50% of the homes in our markets He can decide to carry our stations or not carry them He can cherry pick only a portion of our programs. He will not have to bargain for, or pay for, those carriage rights, although he can seek payment from us for carriage. He can decide to carry our stations on our channel numbers, or he can shift them up to the equivalent of the system's "Siberia." He can bring in the same network programming that is carried by our stations, through the network affiliates licensed to the larger cities relatively nearby to our markets He can bring in distant signals or superstations, which also may duplicate the programs for which our stations have paid a great deal to acquire "exclusive" rights He competes with us for local and national advertising dollars He can make any or all of his carriage decisions based on what makes him a better buy for advertisers than our stations

The equation between cable and local television stations should be rebalanced

Regulatory equilibrium between local television stations and cable must be restored. At least two elements are needed for this restoration -- some degree of must carry protection for local television stations, and reestablishment of the syndicated exclusivity rules

Pending at the FCC is a proceeding which could result in reimposition of the syndex rules NAB strongly supports such a result. We believe this would restore essential protections for any exclusive rights that broadcasters obtain in the marketplace for syndicated programming

The must carry issue may be more problematic NAB and other broadcasting interests are pursuing the legal remedies available to us following the December decision of the Court of Appeals

NAB believes that Congress also should consider legislation to implement some form of must carriage protection. We feel that properly crafted legislation could withstand a court challenge

It is premature to predict what form needed legislation should take. One option would be to condition cable's compulsory license on carriage obligations, which would be a matter within the jurisdiction of this committee. NAB currently is working with other broadcasting interests on the many questions involved with this issue. NAB's leadership also is working with representatives of the cable industry to determine whether there are possible areas for compromise.

NAB appreciates this subcommittee's interest in these important issues, and we would welcome the participation of the members in helping to resolve the thorny issues of must carry As I hope my testimony makes clear, some resolution is required, in order to return a much-needed element of fair competition to the local video marketplace.

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FOOTNOTES

1 WLNE-TV, Providence/New Bedford, RI; WTVC-TC, Chattanooga, TN; KFDM-TV, Beaumont/Port Arthur, TX; KTVL-TV, Medford/Klamath Falls, OR; WRGB-TV, Albany/Schenectady/Troy, NY

2. Quincy Cable TV, Inc. v. FCC, 768 F.2d 1634 (D.C. Cir 1985), cert. denied, 476 U.S. 1169 (1986); Century Communications Corp. v FCC, 835 F.2d 292 (D.C. Cir. 1987).

3. ". .the Commission shall make such distribution of licenses, frequencies, hours of operation, and of power among the several States and communities as to provide a fair, efficient, and equitable distribution of radio service to each of the same." 47 U.S.C. §307(b).

4 A.C. Nielsen Company, November 1987.

5. Albany/Schenectady/Troy - 61 5%; Beaumont/Port Arthur - 50.8%; Chattanooga - 53.2%, Medford/Klamath Falls - 58 2%, Providence/New Bedford - 58 3% Neilsen Station Index, November, 1987

6 47 U S.C. §621(a)(1).

7 For example, franchise fees paid to local authorities are restricted by §622; 47 U.S.C §622. Local regulation of subscription rates is restricted by §623; 47 U.S.C.§623. Local regulation of services, facilities, and equipment is limited by §624, 47 U.S.C. §624. Denial of franchise renewal is governed by §626, 47 U.S.C. §626.

8 Bob Coen, McCann-Erickson, New York.

9 Broadcasting, "Who Owns What With Whom In Cable Networking," November 23, 1987.

Senator METZENBAUM Mr Milton Maltz, Malrite Communications Group, on behalf of the Association of Independent Television Stations Mr Maltz is an old friend of mine I am happy to welcome you here

STATEMENT OF MILTON MALTZ

Mr MALTZ Thank you very much and good morning, Mr Chairman If I could accomplish one thing this morning it would be to focus the attention of Congress on the future of our American system of free and local broadcasting

I think we all agree that our free broadcast system is a national resource of inestimable value It serves all Americans, rich, poor, rural, urban Unfortunately, because of misguided competitive communications and copyright policies, free television is in jeopardy today at the hands of an unregulated monopoly

It was the Congress that created free broadcasting, from the 1927 Radio Act, to the 1934 Communications Act, to the 1964 all channel receiver legislation, Congress has stressed the substantial Government interest in the maintenance and encouragement of a healthy, free and competitive and local broadcast system

This morning, sir, I am looking for an answer to this question Do you still want free broadcasting, or does Congress wish to see in its place a system of pay TV? We urgently need the Congress to focus on this question

Now, the points developed in my testimony are very simple First, cable is a monopoly You do not have to take my word for that Ask the National Journal, the investment house of Bear-Stearns or read the 1974 Cabinet report to the President of the United States of America The ownership of these monopoly cable conduits is concentrating rapidly into the hands of fewer and fewer owners

Now, just last week two major cable companies merged to form the third largest cable company that will in turn be owned by the very largest cable operator, TCI It is my understanding there now is a cash flow of $1 billion in that organization, or a capitalized market value of between $10 and $16 billion

These giant cable conglomerates are integrating vertically into the ownership of programming services seeking access through their monopoly conduit And this vertical integration represents perhaps the greatest threat to competition in the television business today

Right now we have reached the point, sir, where it is virtually impossible to launch a new satellite-delivered program service without giving up a substantial of equity as tribute to gain passage through the cable gatekeeper

It is critical for the Congress to understand that as cable increases its program investments and its local advertising sales activity, the cable relationship with local broadcasters is undergoing dramatic transformation Suddenly, the local broadcaster is viewed principally as an unwanted competitor for viewer's attention and for advertising dollars If Congress does not act, cable operators will use their control over the monopoly conduit to drive away all competition from local broadcasters

There is substantial evidence of anticompetitive behavior New broadcast stations have met with a stonewall of resistance from cable refusing to carry their signals Existing stations have found their signals routed out of traditional channel positions and relegated to the upper tier, or what we call cable Siberia These local stations are then replaced with cable program services in which the cable operator holds an equity interest, and/or in which he is selling advertising time

One of the great ironies of this situation is that all the while as cable is beginning to undermine our free broadcast system, it is simultaneously living off that system Due to the largess of the Congress, the cable industry enjoys a Government-guarantee to freely use any broadcast programming that is chooses

The compulsory copyright license stands as a guarantee that cable will never be required to pay for the programming produced or purchased by local stations The continued existence of this compulsory license, coupled with the absence of local carriage, has created an unstable, untenable, one-way business relationship

I candidly advise this committee that the future of our American system of free local broadcasting is indeed in grave danger In 1988, the public does not own the airwaves, a handful of cable operators do

Mr Chairman, we need your guidance

[Material submitted by Mr Maltz follows]

TESTIMONY OF

MILTON MALTZ

CHAIRMAN OF THE BOARD & CEO

MALRITE COMMUNICATIONS GROUP

Thank you Mr Chairman My name is Milton Maltz I am the Chairman and Chief Executive Officer of Malrite Communications Group Our principal business activity is the operation of radio and television broadcast stations We currently operate domestic UHF Independent television stations in Cleveland and Cincinnati, Ohio, Rochester, New York, Jacksonville, Florida, and West Palm Beach, Florida I appear here today in my personal capacity and as the official representative of the Association of Independent Television Stations, Inc , commonly known as "INTV " INTV represents the interests of more than 180 Independent television stations across the country

It is not my purpose or intention today to attack the character or motives of the cable industry and its leadership As a businessman, it is difficult for me to criticize others who merely seek to exploit opportunities created by government policies That would be like scolding a child who had been negligently let loose in a candy store Instead, my testimony this morning will focus on the patchwork quilt of inconsistent and ill-considered government statutes, regulations and policies that have created the clear opportunity for the cable industry to begin the destruction of our system of free over-the-air broadcasting

Whatever quarrel one might have with a particular television program or category of programs, it is beyond question that our system of free broadcasting is a national resource of inestimable value to the American people If that resource is to be preserved, Congress must take at least two immediate actions First, Congress should condition cable's use of the compulsory copyright license privilege upon a cable operator's voluntary agreement to continue nondiscriminatory carriage of substantially all local free broadcasting stations Second, Congress should immediately investigate the siphoning of popular American television events from free over-the-air broadcasting to pay cable television channels The indisputable consumer interest in free television requires prompt Congressional action on these issues

I

THE CONGRESS SHOULD REQUIRE NON-DISCRIMINATORY CARRIAGE OF LOCAL FREE BROADCASTING STATIONS AS A CONDITION TO CABLE'S USE OF THE COMPULSORY COPYRIGHT LICENSE PRIVILEGE

A Cable has developed as a de facto monopoly

The starting point for our analysis is a simple fact that cannot be denied Cable television has developed as a *de facto* monopoly service The importance of the monopoly nature of cable is dramatically heightened by the fact that many consumers are totally reliant upon cable for their access to television signals

When the Cable Act of 1984 was being debated, the then President of the National Cable Television Association testified,

> "A consumer will have a couple of choices of cable companies There will be two cable wires running down the street " 1/

While I am sure that this representation to the Congress was made in gocd faith, it simply did not turn out to be accurate Of the 7,000 communities in America with cable television service, it has been estimated that approximately 30 or 4/10 of 1% are served by competing systems Stated another way, approximately 99 6% of all cable subscribers are served by monopoly systems

It is not only cable's critics that view the industry as a monopoly The distinguished *National Journal* (7/4/87 at p 1707), recently commended cable industry lobbyists for inducing "Congress in 1984, to, in effect, deregulate a monopoly " And, the respected investment banking firm, Bear Stearns, has described the cable operators' franchise as "A Monopolistic Annuity "

Cable advocates argue mightily that the availability of other forms of entertainment prevents cable from being considered a monopoly However, this claim is tantamount to arguing that the telephone company is not a monopoly because people can write letters, or that

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1/ Hearings Before the Subcommittee on Communications of the Committee on Commerce, Science and Transportation, United States Senate, 98th Congress, First Session (February 16-17, 1983), pgs 126-127 the electric company is not a monopoly because you can always cook with gas, or that the water company is not a monopoly because it sometimes rains

To shed some scholarly light on this debate, INTV, and other interested parties, commissioned the preparation of an economic study entitled "Does Cable Televison Really Face Effective Competition?" This study, prepared by economists Janusz A Ordover of New York University and Yale M Braunstein of the University of California at Berkeley is appended as Attachment No 1 to my testimony Professors Ordover and Braunstein detail the many factors which lead them to conclude that cable television systems currently do not face effective competition

Another useful resource on the issue of cable monopoly is the recent article entitled "Antitrust and Regulation in Cable Television Federal Policy at War with Itself" published in the prestigious Cardozo Arts & Entertainment Law Journal In this article (appended as Attachment No 2), author Glenn B Manishin, Esq explains how the FCC and the Department of Justice have adopted contradicting and inconsistent positions on the issue of cable competition The Department of Justice views cable as a "natural monopoly" and therefore finds it inappropriate to engage in traditional antitrust enforcement with respect to the industry On the other hand, the FCC views cable as subject to "effective competition" and therefore has deregulated the industry Unfortunately, the interests of consumers in securing the benefits of competition have been allowed to fall through the crack between these two agencies

B Rapid horizontal concentration and vertical integration now provide cable operators with a clear incentive for anti-competitive behavior

With the Justice Department standing politely to the side, concentration of ownership in the cable industry has proceeded at a furious pace The largest cable company, TCI, now has a choke hold on television access for approximately 10 million subscribers Just last week, two large MSO's, United Cable and United Artists Cablevision, announced a merger The merged company will be the third largest MSO and will be controlled by TCI, the largest cable operator

While the industry is concentrating horizontally, cable operators have moved rapidly to integrate vertically into the ownership of some of the program services seeking access to the home through the monopoly cable conduits Appended as Attachment No 3 is a recent trade press article that describes the trend toward vertical integration

This vertical integration has produced a profound change in the nature of the cable industry Cable operators are no longer merely passive and disinterested retransmitters of broadcast programming Through their equity interest, and through the sale of local advertising availabilities, cable operators now have a clear vested interest in the competitive success of <u>some</u> of the programming services seeking access through their conduit You don't need a Ph D in economics to figure out that the guy who controls a monopoly conduit is in a unique position to control the flow of programming traffic to the <u>advantage</u> of the program services in which he has an equity investment and/or in which he is selling local advertising availabilities, and to the <u>disadvantage</u> of those services, including local broadcasting stations, in which he does not have an equity position

As our laws stand today, a telephone company is prohibited from owning a cable system for fear that it might "favor[ing] its own or affiliated interest as against nonaffiliated interests " <u>Section 214 Certificates</u>, 21 FCC 2d 307, 324 (1970) And, a broadcast station is prohibited from owning a cable system to prevent it from gaining "a competitive advantage" over other stations <u>CATV</u>, 23 FCC 2d 816, 820 (1970) But, cable operators <u>are</u> permitted to integrate vertically, and use that integration to gain a competitive advantage over others seeking access through their monopoly conduit

The anti-competitive potential inherent in common ownership of the cable conduit and program services was clearly recognized in the 1974 "Cabinet Report to the President" by the Cabinet Committee on Cable Communications A copy of that report is appended as Attachment No 4 to my testimony The Cabinet Committee expressed its competitive concerns in the following terms

> "Cable's multi-channel technology, together with the economic imperatives of a medium that is a natural monopoly, could lead to an even greater concentration of power than exists in broadcast television When a single cable operator has the power to control the

> programming and information content of all the channels on his system, his monopoly power over the cable medium of expression is nearly absolute "

The solution chosen by the Cabinet Committee was a recommended separations policy The Committee described its proposal as follows,

> "We recommend adoption of a policy that would separate the ownership and control of cable distribution facilities, or the means of communications, from the ownership and control of the programming or other information services carried on the cable channels "

Somehow, the thrust of this compelling report was lost in the rush to pass the Cable Act of 1984 As a result, local broadcasters and consumers now face a vertically integrated monopoly cable industry with a clear incentive to engage in anti-competitive behavior For example, in New York City, 50 consumers recently were forced to bring a private antitrust action in order to gain access to program services other than those owned by their monopoly cable operator 2/

C <u>Despite some voluntary restraint, there is clear evidence of anti-competitive cable behavior</u>

As I stated at the outset of my testimony, it is difficult for me to be too critical of an entrepreneur simply for taking advantage of anti-competitive opportunities presented by our current legal and regulatory structure In fact, the cable industry deserves some credit for exercising admirable voluntary restraint under the circumstances Many cable operators have heeded the advice of their leaders not to invite re-regulation by precipitous action

However, there is now unmistakable evidence of the natural and inevitable anti-competitive consequences of our badly skewed cable marketplace Cable operators now view new commercial Independent broadcasting stations as little more than unwanted competition for viewers' eyeballs and advertisers' dollars As a consequence all across the country new stations have met with a virtual stonewall of opposition from cable operators who have refused to add these new stations to their service offerings For example, my company was forced to seek the intervention of a member of Congress in order to secure carriage of our Cleveland station on one area cable system

2/ Appended hereto as Attachment No 5 is a story from "The Village Voice" describing this litigation

Cable industry resistance has contributed significantly to the bankruptcy of 23 new Independent television stations

Existing stations have fared only marginally better All across the country, cable operators have shifted local free broadcasting stations out of their traditional cable channel positions The free broadcasters are typically relegated to undesirable channels at the upper end of the UHF spectrum ("cable Siberia"), which cannot even be received by all cable subscribers The desirable low number channel positions, formerly occupied by the local broadcasters, are now filled with cable program services in which the cable system owner has an equity interest, or in which he is selling advertising availabilities

These channel shifts cannot be defended on the basis of consumer preference In virtually every case, the cable program service which has replaced a local broadcaster has a lower audience rating than did the displaced station Since many consumers have no practical alternative to cable service, cable operators have been and remain free to make these channel shifting decisions without regard to consumer preferences Appended to my testimony as Attachment No 6 are copies of newspaper accounts of consumer complaints regarding these channel shifts

Cable operators also have engaged in the anti-competitive practice of "tie in" sales Previously, consumers had the option of purchasing only the retransmission of local free broadcasting signals Since deregulation however, the cable industry has engaged in what it, itself, describes as "tier meltdown " In the process, access to local broadcast stations is "tied" to subscription to other cable program services In other words, in order to gain access to their local broadcast stations, consumers are required to purchase the cable operator's program services The state of West Virginia, on behalf of its citizens, has recently brought an antitrust action to invalidate these "tie in" sales State of West Virginia v American Television & Communications, Cir Ct , WVA Civ Action No St-C-659 3/ Obviously, it places a great burden on consumers to require them

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3/ See Attachment No 7

to pay for cable program services, which they may not wish to purchase, just in order to gain access to their local free broadcast stations

D <u>The cable compulsory copyright license impacts heavily on these competitive issues</u>

The cable industry continues to enjoy the extraordinary privilege of a compulsory copyright license to use broadcast programming This license has two distinct parts relating to local and to distant broadcast signals The local compulsory license provides the cable operator with a government guarantee of <u>free</u> use of all of the programming purchased or created by local broadcasters The license is a government guarantee that a cable operator will never be denied the right to use the programming any local stations Nor can the cable operator ever be charged by any local station for the use of its programming

Cable operators pay for the use of cable program services, such as MTV, but do not have to pay for the use of local broadcast signals When you consider that cable subscribers spend most of their time watching broadcast signals, the value of this subsidy to the cable operator becomes clear Because of the compulsory license, cable has become a business that can never be required to pay for a major part of what it is that it sells to consumers

Some cable program services have begun to provide discounts in the charge they impose on the cable operator in order to secure more favorable channel positions The local broadcaster cannot "meet the competition" by offering a discount, since he is prohibited from imposing any charge in the first instance

The cable operator also receives a compulsory license to import the signals of distant broadcast stations For these distant signals, the cable operator pays a statutory license fee into a pool which is divided among copyright owners Local broadcasters must purchase their programming at marketplace prices Cable operators can secure the very same programs on distant signals for government prescribed discount prices The competitive inequality of this situation is both obvious and intolerable

E <u>Cable's use of the compulsory license for local signals should be conditioned upon a non-discriminatory carriage requirement</u>

Two different sets of mandatory local cable carriage rules have been declared unconstitutional by Appellate Courts Petitions for Supreme Court review of these decisions are now pending However, it seems prudent to explore a more constitutionally secure approach to the issue of cable carriage of local signals

Our Association supports an approach in which the cable operators' continued use of the free compulsory license for local signals would be conditioned upon his voluntary agreement to a reasonable non-discriminatory carriage requirement By agreeing to carry substantially all local stations, the cable operator would continue to enjoy a free compulsory copyright license to retransmit local signals On the other hand, cable operators who wished to do so would be free to discriminate in the carriage of local stations subject to normal copyright liability for those stations they wished to retransmit

The key to this approach is that cable operators clearly do not have a constitutional right to a compulsory copyright license to use broadcast programming By enacting such legislation, Congress would insure that the compulsory copyright license privilege it has created does not become an instrument for discrimination among local stations licensed to serve the same area

The Congress may also wish to prohibit the "tie in" sale of local broadcast retransmission services and cable program services Clearly, consumers should have the option of purchasing only broadcast retransmission services

II

CONGRESS SHOULD INVESTIGATE THE "SIPHONING" OF POPULAR EVENTS FROM FREE BROADCASTING TO PAY CABLE SERVICES

I have enormous respect for the new and diverse viewing alternatives that the cable medium has provided to the American public Cable provides consumers with choices previously unavailable including 24 hour news, coverage of Congressional proceedings and sporting events not previously telecast on free over-the-air broadcasting The availability of these additional viewing choices provides a clear benefit to consumers

However, consumers clearly will not benefit, but will be substantially harmed, if programming and events previously available for free on broadcast stations are "siphoned" away to pay cable services Plainly it does not benefit consumers to require them to pay for exactly the same program events which previously had been available to them for free

There is clear evidence that this process of "siphoning" has already begun Eleven NFL Football games which had been carried on free television in previous years were available only on a pay cable channel this past season Millions of working men and women were deprived of access to television coverage of these eleven NFL games If I have ever seen the head of the camel under the edge of the tent, this is it

Appended to my testimony as Attachment No 8 is an editorial from Cablevision Magazine which gleefully reports that the Congress did not react to the loss of these NFL games from free television As noted in the editorial, cable industry leaders now talk openly of "siphoning" the World Series, the Super Bowl and the Olympics from free television to pay cable channels

Last summer saw a drastic reduction in the number of Yankee baseball games on free TV The missing games were siphoned away to a pay sports channel while the cable industry continued to live off of the free broadcast system In October of this year, Turner Broadcasting Company is slated to commence a new cable program service to be called Turner Network Television ("TNT") As outlined in numerous press accounts (samples of which are appended as Attachment No 9 to this testimony), the goal of this new service is to siphon away exclusive coverage of major American events from free television Included on the target list are Major League Baseball, the Masters Golf Tournament, the Kentucky Derby, the Miss America Pageant and many other major events that are a part of the social fabric of this nation

Obviously, free over-the-air broadcasters such as Milton Maltz have an economic self-interest in preserving free broadcasts of these events However, our economic self interest does not in any way diminish the manifest public interest in assuring continued free over-the-air access to these staples of our American culture

The survival of free television is an issue which we believe should command the immediate attention of the Congress At the very least, Congress should commence an investigation into the prospect that the American people are about to be made to pay to see events which previously had been available to them for <u>free</u> Following that investigation, it may be possible to craft conditions upon the compulsory copyright licensing privilege and/or the antitrust exemptions heretofore granted to certain sports interests, as a means of assuring that consumers are not requried to pay for access to events which they currently enjoy for free

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Mr Chairman, I believe that you are well aware of the enormous respect that I hold for you and for your legislative record I would not insult you and your colleagues by sitting here this morning and making "Chicken Little" predictions I honestly believe that the future of free television is in serious jeopardy Our stations, our programming and our service to consumers cannot long withstand the relentless onslaught of anti-competitive behavior by unregulated monopoly cable systems I don't blame the cable entrepreneurs for seizing the opportunities available to them However, I do believe that the government has an obligation to review its competitive, communications and copyright policies to assure that consumers continue to have access to the free television services that represent an important part of life in American today Thank you

Attachment No. 1

Does Cable Television Really Face Effective Competition?

Janusz A Ordover
Professor of Economics
New York University

with the assistance of

Yale M Braunstein
Professor
University of California at Berkely

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Does Cable Television Really Face Effective Competition?

Janusz A. Ordover[1/]

Introduction

Is cable television a local monopoly or does it face effective intramodal and intermedia competition? An answer to this question must be given before sound public policy toward cable television can be devised. In 1985, the FCC concluded that cable television faces effective competition from broadcast television in those local communities where there are at least three off the air television signals available to television viewing households in any portion of a cable community. The Commission found that the availability of three broadcast television signals is enough to ensure an effective competitive constraint on the ability of a local cable system operator (CSO) to charge "noncompetitive" rates and to offer a less than desirable programming mix to subscribers.[2/] This "three signals" conclusion was used to implement the rate deregulation provisions of the 1984 Cable Act,[3/] that is, where effective competition in the form of three broadcast signals exists, cable firms may charge as much as they wish for basic service.

1/ Janusz A Ordover is a Professor of Economics at New York University Yale M Braunstein, Professor, University of California at Berkeley contributed to the preparation of this analysis.

2/ Implementation of the Provisions of the Cable Communications Policy Act of 1984, 50 Fed. Reg. 18637 (1985).

3/ The Cable Communications Policy Act of 1984, Publ. L 98-549, 98 Stat. 2779 (1984).

We have been asked to review critically the Commission's findings regarding the extent of effective competition between cable and broadcast television. Our analysis has two main purposes. First, to ascertain whether the methodology used by the FCC to reach its findings is consistent with widely accepted precepts of economic analysis, based on current conditions, and reflective of a sufficiently broad range of considerations. Second, to review the scant data from the deregulated cable markets in order to gauge the likelihood that cable faces competition where three broadcast signals are available.

We do not aim here to provide a rigorous statistical test of intermedia competition or to provide a detailed forecast of the likely effects of deregulation on the cable industry. Such an exhaustive undertaking would be impossible in the limited amount of time available to prepare this report. Nevertheless, we have reached certain conclusions. These are summarized as follows

> First, the analytic methodology used by the FCC to gauge the extent of effective competition between cable and broadcast television did not conform to widely-accepted economic methodologies.
>
> Second, the cable industry has been undergoing rapid structural and other changes which potentially cast doubt on the validity of the "three signals" finding (which was based on data from 1984 and earlier)
>
> Third, presumably because of its perception of broadcast TV as the main constraint on cable television, the FCC has understated the social value of alternative video technologies, such as wireless cable or MMDS, SMATV, and DBS.
>
> Fourth, the available, albeit scant data indicates that the only unambiguous gainers from cable

rate deregulation have been holders of local franchises

Fifth, future analysis of competition issues requires substantially more fact-finding and sounder methodologies than employed by the FCC

1. FCC's Analysis of Effective Competition Suffers From Fundamental Methodological Problems

A scrutiny of the analytic approach adopted by the Commission in support of its "three signal" rule reveals significant methodological flaws. These flaws cast grave doubt both on the validity of the conclusions and on the desirability of the rule itself. We shall argue that the methodology adopted by the Commission in deriving criteria for "effective competition" in the cable television market is not based on standard economic indicia or substitutability among various entertainment/information services.4/ In fact, it appears that the Commission first formulated the desired policy conclusion and then sought to develop data that, if it did not prove the conclusion, at least would not undermine the conclusion.

The Commission's major premise apparently is that cable television competes in a broadly defined "home video market" in which cable, over-the-air television, STV, MDS, SMATVs, and DBS, "all offer alternatives that appear to be perceived as substitutes."5/ This approach would be based

4/ Thus, we concur to some degree with the comments filed by the U S Dept. of Justice. *See* Comments of the U.S. Dept. of Justice, MM Docket No 84-1296, January 28, 1985

5/ This is a view advanced by economists Jonathan D. Levy and Peter K. Pitsch in their article "Market Delineation, Measurement of Concentration, F C.C Ownership Rules," p. 203, in V. Mosco (ed.), Policy essentially on the observation that a variety of media deliver "information and entertainment" to the public. Thus, the FCC's approach hypothesizes a broad market in which cable television allegedly competes for the viewers' attention and dollars against VCRs, AM-FM radio, movie theaters, print media, and so on. It appears, furthermore, that in constructing the relevant product market, the FCC failed to give adequate consideration to such important considerations as the multichannel capacity of cable systems and cable's ability to provide packages of programming to subscribers.

The Commission's approach begs a fundamental question which goes to the heart of public policy toward cable television. This is: Do alternative technologies for delivering video programming actually provide effective competition to cable? Effective competition cannot be engineered by assumption. Strength of competition has to be assessed using sound economic methods, such as those outlined below, which conform to the criteria suggested by the Department of Justice.

Instead, in its analysis the FCC merely assumed a broad product market in which cable television competes with broadcast television (and other media). It then proceeded to determine how much competition is needed in that product and

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Research in Telecommunications, Ablex Publishing Corp (1984), pp. 201-212. See also Levy and Pitsch, "Statistical Evidence of Substitutability Among Video delivery Systems," in E Noam (ed), Video Media Competition: Regulation, Economics, and Technology, Columbia University Press, (1985), pp. 56-92.

geographic market to offer effective competitive constraints on the market power of cable system operators. The Commission concluded that the theoretical presence of three broadcast television signals of adequate quality reception would sufficiently restrain whatever market power a cable system operator ("CSO") might have.

Apparently the number three was reached on the basis of empirical studies showing that adding a fourth broadcast TV station to a market does not have a statistically perceptible effect on basic cable subscription levels.[6/] This approach was pioneered some time ago by John Kwoka.[7/] He demonstrated that in certain instances the creation of a strong third-ranked firm out of two lesser-ranked firms could cause prices to fall despite an increase in measured market concentration. Regardless of the econometric and analytic merits or demerits of Kwoka's study,[8/] it is certain that his work did not answer what

6/ The Commission's order refers to a study by NCTA/CATA "providing factual support for a standard based on fewer than three signals " ¶ 97. It also cites Arbitron data showing that in two signal markets cable viewership of off-air signals was equal to or greater than off-air viewership of such signals. The opposite was found to be true of three signal and greater markets. ¶ 99. The report assumes that cable itself is the fourth competitor in a three-signal market. Interestingly, none of these findings goes directly to the issue of effective competition between cable and broadcast TV

7/ See J.E Kwoka, "The Effect of Market Share Distribution on Industry Performance," The Review of Economics and Statistics, 1, 1979, pp. 101-109.

8/ For a criticism of Kwoka's study, see W.F. Meuller and D.F. Greer, "The Effect of Market Share Distribution on Industry Performance Reexamined," The Review of should be the key question: whether the presence of three broadcast television stations in a geographical market ensures that prices and "clusters" of cable services offered by a CSO reasonably well approximate the social ideal. Kwoka showed only that a current level of price may fall following the creation of a strong third or fourth player. Kwoka's findings necessarily apply only to markets (or industries) that deviate from a fully competitive ideal[9/] so that the current level of price generates rents to the leading firms. This is because if the market were highly competitive (or fully contestable), the price could not fall any further as a result of increased concentration.

The relevance of the Kwoka-type analysis to the public policy issues regarding media market power is very limited. This analysis fails to consider whether three broadcast stations and one cable operator actually make for an adequately competitive market. Instead, it merely suggests that the presence of a fourth broadcast TV station does not necessarily make for a comparatively more competitive market than a market comprising three broadcast TV stations and one cable system

The FCC's conclusion regarding effective competition is thus troubling. It is also surprising in

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Economics and Statistics, 2, 1984, pp. 353-357.

9/ Kwoka's results also apply to markets which are not perfectly contestable. Baumol, W.J., J.C. Panzar, and R.D. Willig, Contestable Markets and the Theory of Industry Structure, Harcourt Brace Javanovich, 1982.

light of the availability of an appropriate conceptual method of analysis developed by the Antitrust Division of the Department of Justice in the 1982 Merger Guidelines.10/ In fact, this is the very methodology that the Department urged the FCC to adopt in implementing the Cable Act.

Conceptually, the Guidelines methodology can be readily applied to the problem of determining the degree of effective competition between cable television, on the one hand, and broadcast television (or other media) on the other hand 11/ In essence, following the Guidelines methodology,

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10/ DOJ Merger Guidelines methodology for constructing relevant product and geographic markets can be summarized in a sequence of steps. Step 1· determine a product or service whose pricing and quality are to be analyzed. Here, the relevant product or service may be basic cable or cluster of services provided by cable systems. Step 2: Determine the relevant suppliers in a given geographic area Here, the relevant supplier will be the monopoly cable franchise, in most cases Step 3 Determine which products or services constrain the ability of firms identified in Step 2 to profitably elevate the relevant prices above some chosen benchmark level by a small but significant amount for a nontransitory period of time. In most situations examined by the Antitrust Division, the hypothesized price increase used has been 10 percent and the nontransitory period of time has been pegged at two years. However, in some limited circumstances, the Division used smaller (5%) and larger (15%) price increases. Step 4· Construct the relevant market comprising firms identified in Steps 2 and 4. See, J A Ordover and R.D. Willig, "The 1982 Department of Justice Merger Guidelines: An Economic Assessment," 71 California L Rev 535 (1983), for a more detailed analysis of the pertinent methodology. 1982 Merger Guidelines, 47 Fed. Reg 28,493 (1982) and 1984 Merger Guidelines, 49 Fed. Reg. 26,823 (1984).

11/ For an example of application of the Merger Guidelines in video markets, see Lawrence J White, "Antitrust and Video Markets: The Merger of Showtime and the Movie Channel as a Case Study," in E. Noam (ed.), Video Media Competition: Regulation, Economics, and Technology," we would say that the availability of broadcast television contemplated under the Commission's standard offers effective competition to cable television if, following decontrol of basic rates, cable system operators would find it unprofitable to elevate basic rates by 10 percent and maintain them at this higher level (in real terms) for at least two years. It is theoretically possible, of course, that such a rate increase might be unprofitable in markets with three or more broadcast television stations (as the Commission asserts) and profitable in franchise areas in which there are fewer than three broadcast television stations. However, the analytic studies that are available suggest that the Commission's definition of effective competition is probably wrong.12/

Columbia University Press, (1985), pp. 338-363.

12/ A study by G. Kent Webb, The Economics of Cable Television, Lexington Books, (1983), found that basic cable penetration increases with the number of off-the-air channels it carries, suggesting that to some extent basic cable services and broadcast television are complements. However, improvements in the quality of broadcast television tend to reduce basic's penetration, other factors remaining the same. Thus, on this score, the two media are substitutes, at least to a limited extent. Webb's study strongly suggests that it is pay cable which competes with broadcast television. Obviously, to the extent that the potential subscriber must pay basic rates before obtaining premium services, the price of basic affects demand for premium services. It is difficult to know what one should make of Webb's results. From our standpoint, however, the key question is the price elasticity of demand for cable services as a "function of" the number and quality of broadcast television stations. Webb's results suggest that no matter what is the actual numerical value of this elasticity, it is likely to be small. A recent study by Browne, Bortz and Coddington, as reported in Cable TV Franchising, Paul Kagan Assoc., July 20, 1986, p.3, Indeed, the Commission may have misunderstood the most basic phenomenon of the cable industry. Namely, it is possible that broadcast TV viewers have been defecting to cable TV,13/ so that cable may be constraining broadcast TV, as the Commission appears to believe. Yet it does not follow necessarily that broadcast is effectively constraining cable television at current cable rates and program offerings.

How realistic is it that a price increase of a magnitude of ten percent in current subscription rates would prove unprofitable to a cable system operator? Some important insights can be obtained by making an assumption about a representative CSO's mark-up on average subscriber charges, that is, CSO's variable cost to price margin.14/ Straightforward calculations used for illustrative purposes show, for example, that when the cost to price ratio margin is one over three, a 10% rate increase would be unprofitable if it were to induce as much as fifteen percent reduction in penetration. The one over three cost to price ratio means that the variable cost (averaged among all disconnecting subscribers) would be a third of the average subscription

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supports this suggestion

13/ See, for example, M.O. Wirth and H. Bloch, "The Broadcasters The Future Role of Local Stations and the Three Networks," p. 121-122, in E. Noam (ed.), Video Media Competition: Regulation, Economics, and Technology, Columbia University Press (1985), pp. 121-137

14/ Note that an increase in a basic rate may induce some disconnections among those subscribers who also purchased pay tiers. It is for this reason that we must focus on an average mark-up.

rate.[15/] Inspection of the mathematical formula indicates that the higher the cost-price ratio, the less likely it is that a 10% price increase would prove unprofitable because of the number of disconnects it induced. [See Appendix A1 for calculations based upon various cost - price ratios and rate increases.]

The available data indicate that the variable cost components for basic services are a small percentage of revenue from basic, perhaps as low as 9%.[16/] On the other hand, these costs can be as high as 50% for premium programming services. In light of these facts, our illustrative ratio is not unreasonable. The available evidence also tends to suggest that price increases of this magnitude did not cause a substantial reduction in cable's penetration in those communities that already have cable, although the real magnitude of these price increases must be adjusted in some cases by accounting for changes in the offerings included in various basic (or first) tiers. (*See*

15/ The mathematics are as follows. The change in profits, denoted by dL = p q[(dp/p) + (dq/q)(1-[variable cost/p])], where p denotes subscription rates and q the number of subscribers. We fix dp/p at 0 1 or 0.15 and fix the price-cost ratio at some appropriate level and then calculate (dq/q) that would cause the change in profits to be negative

16/ Two caveats are necessary here. First, the variable costs are low because most of the investment is either sunk or fixed Consequently, long-run variable costs may be higher than those postulated in the text. Second, as discussed in section 1(b)(1), basic is undergoing an unprecedented transformation in the present marketplace.

section 2a *infra*.) As shown in Table 1, nationwide cable penetration increased in the first quarter of 1987.

2. FCC's Analysis of Effective Competition is Outdated In View of Significant Programming and Structural Changes in the Cable Industry

The FCC's 1985 conclusion is also potentially flawed because the market it examines is already antedated. A new picture of that market suggests strongly that cable has the ability to obtain monopoly rents. The most important elements of the new picture are "tier meltdown" and structural changes in the degree of horizontal and vertical integration.

a. Tier Meltdown.

During the last few years, CSOs have tended to include more attractive programming choices in the basic tier. This is in contrast with the early days of classic 12-channel cable systems when the basic service included principally (1) must-carry stations (the locally available broadcast TV signals), and (2) some locally originated programming. In fact, in many early systems only a single basic tier was available to subscribers

Subsequently, cable operators began using microwaves to import distant television signals for retransmission. With the advent of satellites, additional program offerings, such as HBO, The Movie Channel, Showtime, etc , were made available in cable systems on pay-per-channel basis. Cable systems acquired greater channel capacity which enabled them to increase their offerings. In turn, growing channel capacities stimulated new programming. Ironic, but pertinent for public policy, is the fact that channel space for new offerings is now scarce in some cable systems.

During that period, which lasted until quite recently, the economics of cable television pricing were driven by the presence of demand-interdependencies among various offerings of cable services. In particular, a CSO had to allow for the fact that changing the price of basic service increased the actual price (thereby reducing demand) for premium services. CSOs thus employed sophisticated price discrimination strategies that enabled them to maximize revenue from subscribers of different tastes. In addition, and perhaps of equal importance, because subscription rates for pay tiers were by the mid 1970s almost totally deregulated and were often not included in the base for franchise fees, the CSOs sought to shift as much programming as possible into higher (premium) tiers to maximize their pricing freedom and net revenue.

In the wake of the 1984 Cable Act, cable operators have begun to increase the number and variety of offerings that are included in basic. As a result of this new marketing strategy, the basic tier now offers not only retransmission (i.e., higher quality reception of broadcast TV), and local programming, together with a "right" to purchase higher tiers, but also increasingly varied and better quality programming. The ongoing simplification of the pricing of basic and premium services by cable systems is due to a combination of factors. The most important of these are:

(i) customer resistance to and confusion with complex tiering of services;

(ii) changing offerings as program suppliers enter and exit the supply side of the distribution chain, resulting in periodic realignments of tiers;

(iii) vertical integration of cable and program suppliers;

(iv) increased power of cable system operators in negotiations with franchising authorities This has resulted from two events: (a) the end of the "franchising wars," and (b) deregulation and preemption by Congress.

Overall, through increased clustering of offerings in basic tiers, the trend has been to reposition these tiers in the product space of information and entertainment services. It is difficult to determine with precision the consequences of that repositioning on effective competition among the providers of video-based entertainment and information. In our opinion, repositioning potentially has eased the constraint, if any, that broadcast television imposes on basic cable. This is because strategies designed to reposition products (here cable offerings) are primarily motivated by the desire to reduce the degree of head-on competition, not to enhance it. In brief, basic cable still subsumes broadcast, but its reshaping has made it a distinguishable product.

As a product, basic cable now is the <u>availability</u> 24 hours a day and seven days a week of all of the following news (including the specialties of financial, sports, weather, headline, feature, live, local, and general national news), sports (of different sports and multiple games within most major sports), children's variety, adult variety, religious offerings, shopping (ranging from fashionable clothes to bizarre geegaws), and movies. In terms of the continuous availability of this smorgasbord of programming, no three broadcast stations, even taken as a group, can compare; basic cable offers a distinct product.

Thus the product market that was considered by the FCC prior to its deregulatory rulemaking has changed. It is probably less competitive than it was then,[17/] but at least the Commission ought to re-examine the marketplace. In doing so, the Commission should use better methodologies, and should determine the implications of product repositioning and tier meltdown on the degree of effective competition among different modes of reaching the television-viewing public.

b. Structural Changes.

Perhaps of even greater consequences for public policy are the structural changes in the cable industry since the passage of the Cable Act of 1984 and the FCC's 1985 deregulation ruling. These structural changes include both

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17/ In the DOJ Comments, it was concluded at 18 that " . . . broadcast television is generally not a good substitute for the full range of programming and other services distributed by cable television These reasons include the large variety of video programming usually carried on cable systems (. . .) and the inability to market 'pay' services successfully over broadcast television." DOJ at 18.

increasing concentration in cable ownership and increasing vertical integration between CSOs, program distributors, and production companies. Concurrently with this trend towards increased horizontal concentration and tighter vertical links in the programming-distribution chain, cable system operators have at times implemented programming practices whose impact on competition is potentially suspect.

(i) Horizontal Integration.

Some consolidation of the ownership of cable systems took place prior to deregulation. It seems, nevertheless, that deregulation -- combined with favorable merger policy and a rising stock market -- greatly spurred the trend towards consolidation of ownership in the cable industry. Recent estimates indicate that of all cable subscribers (more than 40 million households), 46 percent are directly or indirectly controlled by 5 companies.[18/] In 1985, the top 50 companies accounted for 70 percent of the nation's nearly 35 million subscribers. The two major MSOs, Tele-Communications Inc (TCI), and American Television and Communications Corp (ATC), now control approximately over 30 percent of all subscribers, with TCI alone controlling 22 percent. The biggest MSO is TCI which owns 600 cable systems with approximately eight million subscribers in 44 states. The second largest MSO, ATC (a subsidiary of Time, Inc), owns 660 cable companies with 3.5 million subscribers in 32

18/ These figures are culled from various issues of Cablevision.

states. TCI alone has spent nearly $3 billion acquiring over 150 cable systems in the last three years.

It has been estimated that, in 1986, approximately nine billion dollars was spent on mergers and acquisitions by the largest MSOs. One industry official has commented that it would not be surprising to see as many as five to eight of the top 20 companies disappear through horizontal integration of the next five years.[19/]

This trend towards increasing concentration has not been appreciably slowed by the rising prices of the transactions. In 1986, the average per subscriber value of one company's acquisitions, for example, was $1399 and the cash flow multiple on a projected first year basis was 10.5. For another company, the average value per subscriber was $1254. In some key targeted cable areas, i.e , Florida and California, prices of $2000+ per subscriber are not uncommon. Prices in 1986 generally averaged between $1200 and $1300 per subscriber. However, prices ranged widely from $900-$1200 for the very few remaining classic (i.e., older systems with only small capacities which typically offer only broadcast stations) cable systems to $1500+ for large or underdeveloped systems. And by 1987, the per subscriber prices have gone into the $2000+ range, according to trade press reports In contrast, in 1984 (prior to cable deregulation), cable systems could typically be acquired for $800-$900 per

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19/ These estimates were reported in Cablevision, January 19, 1987 subscriber. As of late 1985, the going price was reported to be $1100-$1200. The strong per subscriber prices were also reflected in the average projected first year cash flow multiple paid for systems in 1986, the average of which ranged from 10.5 to 11.5.

There is very strong reason to suspect that deregulation made it possible for CSOs to better extract profits from their local franchises. To the extent that there is no evidence that, on average, CSOs were unprofitable (on a replacement cost basis) prior to deregulation, deregulation must be strongly considered as an important explanatory variable behind the increases in per-subscriber prices paid by the purchasers.

The available financial data on the sales prices of cable franchises can indirectly be used to obtain some estimates of the degree of monopoly power held by local cable franchises. One analysis looks at the ratio of the value of the productive asset in the financial market to its replacement value. This ratio is high when the asset has market power attached to it. In particular, in highly competitive markets the ratio -- denoted as the q-ratio -- should approximately equal one. Based upon an analysis of 153 recent sales of cable systems, Shooshan and Jackson Inc have calculated q-ratios for 1986 20/ Their study estimates

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20/ Shooshan and Jackson, Inc., "Opening the Broadband Gateway The Need for Telephone Company Entry into the Video Services Marketplace," (1987), Washington, DC, submitted in FCC CC Docket No. 87-266 the q-ratio for the cable industry as of December 1986 at 2.81.[21/] Obviously, in light of additional increases in the per subscriber acquisition prices in 1987, the value of the q-ratio has increased substantially as well [22/] The study concludes that the explanation for the high q-ratio is that the cable industry has excessive market power. Thus, these analysts conclude that although there are many potential and actual alternatives to cable, these alternatives do not adequately constrain the monopoly power of cable systems.

(ii) Vertical Integration

Another dramatic manifestation of structural changes in the cable industry is the growing degree of vertical integration "Forward" and "backward" vertical integration has been taking place. Thus, MSOs have been integrating into programming

Vertical integration by major MSOs into programming services is linked with the concentration of system ownership.[23/] This is because large MSOs have assured

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21/ This ratio is what Shooshan and Jackson call their middle-of-the-road estimate They also calculate two other estimates one with a high adjusted replacement cost and the other with a low adjusted replacement cost. The q-ratios for these estimates are 2 27 and 3 28, respectively. The q-ratio for a competitive market is equal to one Higher q-ratios occur in concentrated industries where there are barriers to entry and there are few mechanisms to reduce monopoly profits

22/ As we pointed out, however, the general increase in stock market prices over the 1984-87 period contributed to the increases in the calculated q-ratio.

23/ See, e g Lawrence J White, "Antitrust and Video Markets: The Merger of Showtime and the Movie Channel as a Case Study," in E. Noam (ed.), Video Media

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captive subscribers which reduces the risks of substantial investments in programming.

Interestingly, for a programmer the audience base provided by cable is more secure than is the audience when the programming is delivered via broadcast. An advertising-supported delivery technology must be sensitive to the size of the viewing audience for every minute of programming. By contrast, the analysis for a CSO of the value of any programming turns on whether a particular service increases penetration, not how much (or even whether) anyone watches that service. Another way of making this point is to note that the product delivered by cable to consumers is the continuous availability of a range of programming, but the product broadcast TV claims to its advertisers that it delivers to consumers is an audience measured by the number that actually watches a given program. The audience size obviously fluctuates more widely than does the number of subscribers.

At the same time, vertical integration may be welcome to a programmer that has experienced the substantial buying power (monopsony power) of large MSOs, with their unchallenged grip over cable subscribers. Indeed, it is well-known that large MSOs frequently pay dramatically lower per subscriber fees than those paid by smaller systems.

Competition: Regulation, Economics and Technology, Columbia University Press, (1985), pp. 338-363.

This is not the place to explore in detail the extent of vertical integration in the industry and the ongoing changes. However, as can be seen from Tables 2 and 3, several of the largest MSOs are owned by media corporations who are among the largest cable programmers Many of the cable system operators and the program packagers also have interests in program production and other aspects of distribution. Furthermore, data indicate that subscribers to the cable systems operated by vertically integrated firms are most likely to subscribe to each firm's jointly-owned pay service.24/

Economists generally presume that vertical integration and vertical business practices are driven by efficiency considerations 25/ However, whether a quest for efficiencies fully explains vertical integration in the cable industry, as well as some other programming practices, has yet to be fully explored. Indeed, economists have recently

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24/ See B.M. Compaine, Who Owns the Media, Second edition, White Plains. Knowledge Ind Publ (1982). See also, Shooshan and Jackson, Inc , Economic Analysis of Concentrated Ownership of Cable Systems, Washington, D.C., 1986, and "Cable TV: The Issues," Consumer Reports, September 1987.

25/ See, e g , M.K Perry, Vertical Integration: Determinants and Effects, Bell Corporation (Belcore) Research Paper (June 1987) and M.L. Katz, Vertical Marketing and Franchising Agreements, UC Berkely Bus School (September 1987) both forthcoming in R. Schmalensee and R. Willig, Handbook of Industrial Organization, North-Holland Publishers (1988).

pointed out that, at least in principle, vertical practices can have anticompetitive horizontal consequences.[26]

Thus, for example, through vertical integration MSOs may deny programming to alternative cable technologies, such as MMDS ("wireless cable"), which constitute a head-on threat to cable's control of the local market.[27] Such anti-competitive tactics are easier to carry out when a distributor (a large MSO, for example) also owns an important programming source.[28] In addition, as the MSO becomes larger, the more credible become its threats to disadvantage the program vendor at the distribution level if it refuses to cooperate with the distributor's programming tactics. Such a disadvantage could be produced, for example, by placing the vendor's program on a high channel, where it is less likely to be viewed by subscribers, or by refusing to carry the service. Other tactics could include overpricing a particular program or not including it in the optimal tier.

26/ See T.G. Krattenmaker and S.C. Salop, "Anti-competitive Exclusion: Rising rivals' costs to achieve power over price," 96 Yale L. J 209-295, (1982); and J.A Ordover et al., "Non-price anti-competitive behavior by dominant firms toward the producers of complementary products," in F. Fisher (ed.), Antitrust and Regulation, MIT Press (1985).

27/ See, "Cable Television v. The Alternatives· A Study in Antitrust," prepared by the Office of Congressman Charles E. Schumer (Sept. 14, 1987), for an argument that incumbent MSOs have prevented entry of new cable distribution technologies.

28/ D.T. Scheffman and P.T. Spiller, "Buyers and Entry Barriers," Federal Trade Commission, Bureau of Economics Working Paper No. 154, August 1987.

Another business strategy of CSOs is, in effect, the sale of channel placement to programmers by means of obtaining from program vendors a discount from the price in exchange for preferential placement. Because broadcast television stations cannot sell their programming to cable at any market-related price, they do not have at present an efficient mechanism for competing with other programmers for valuable channel assignments.

To the extent that the FCC may be correct that independents actually compete for viewers and advertising revenue with cable systems,29/ the decisions to move these stations to higher channels should at the very least raise some concern. This is because the need to ensure that the pursuit of legitimate business objectives -- which includes maximization of profits from distribution of programming -- by cable systems should not undermine the public policy objective of securing a wide range of programming choices for cable subscribers and other television audiences. On the other hand, to the extent that broadcast television programming is valuable to cable systems, perhaps it should be placed on equal footing with other programming products in its ability to compete for valuable channel location This is especially important for the local stations that are no

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29/ National cable advertising revenues, although small in proportion to those of broadcast networks, have been increasing rapidly Revenues were $546 million, $735 million and $930 million from 1984 through 1986 respectively. Estimates for 1987 advertising revenues are $1.142 billion, a 10 percent increase over 1986.

longer protected by must-carry rules and for whom exclusion or suboptimal channel placement could amount to a financial death sentence.

It is not our view that regulation of the MSOs' programming decisions is necessarily a desirable public policy. It is our opinion, however, that in light of the structural changes in the cable industry, such programming decisions can assume consequences which did not previously exist. To the extent that they do, they raise serious public policy concerns.

3. The FCC Has Paid Insufficient Attention to Alternate Delivery Technologies

It seems clear that aside from direct head on competition from another wired cable system -- as it exists in overbuilds --- the most plausible constraint on the market power of local cable franchises should come from alternative delivery technologies such as MMDS or wireless cable, SMATV, and DBS.30/ The available evidence suggests that these alternative cable technologies have not yet made significant inroads into the "video marketplace." The troublesome possibility, however, as recent developments in the cable industry strongly suggest, is that entry impediments have increased rather than decreased in the post-deregulation marketplace.

30/ Direct competition from cable systems owned and operated by fiber-optics-using telephone companies has yet to materialize. Its future is mired in complex legal and regulatory battles.

Interestingly, the FCC has expressed little interest in facilitating entry of these technologies. Indeed, having found that broadcast television offers an effective constraint on cable in many local franchises, the Commission paid mere lip service to alternative technologies which allegedly are inferior from the engineering standpoint to standard cable. The Commission's stance however, confuses economic benefits with engineering assessments. From the social standpoint, the relevant benefits from those alternative technologies have to be related to the associated costs. For example, the fact that some of these technologies can offer fewer channels of programming than state-of-the-art cable systems is not enough to dismiss them from the marketplace. In many respects, these technologies entail fewer sunk costs, are less expensive to install, and are cheaper to maintain than are standard cable systems. In addition, their presence in the marketplace would afford additional competition to incumbent CSOs which could inure to the benefit of cable subscribers.

4. The Effect of The 1984 Cable Act on The Cable Industry: Who Has Benefitted?

It is too early to render a definitive judgment on the social benefits engendered by the FCC's implementation of the effective competition provisions of the 1984 Cable Act However, the available data indicate that so far the only unambiguous beneficiaries of the Act have been the owners of cable systems. The advantages for consumers are unclear, at best

The owners of cable systems plainly have benefitted through increased prices paid by buyers for the existing cable systems. Cable system owners have also benefited from the ability to raise basic subscription rates without interference from regulatory authorities. Subscribers have suffered as a result of these price increases, at least to the extent that these price increases exceed the benefits from additional programming that the operators are now increasingly including in the basic tier [31/]

Tables 4 and 4a show the history of average monthly basic cable rate increases since 1979.[32/] During the period 1979-1985, the average rate increase granted to operators requesting rate increases was between 13.6 percent and 17.8 percent (with an average increase of 15 3 percent over the period) above the old rates. In 1986, the average basic cable rate had increased 20 percent above the old rates for those operators that had increased their basic rates. For the first half of 1987, cable operators, no longer subject to rate regulation, have increased their basic cable rates by approximately 24 percent. In a 1986 survey of 282

31/ A recently released study by National Cable Television Association (NCTA) shows that from December 1986 to June 1987, basic subscribers in a surveyed sample received an additional 1.6 channels in their basic package, going from 27.3 to 28.9 channels "Rate Deregulation: Cable Industry Pricing Changes and Service Expansion in a Deregulated Environment," NCTA, Washington, D.C. (November 1987).

32/ The data are estimates of Paul Kagan Associates as reported in their publications, Cable TV Franchising and the Kagan Census cable operators, the Cable Television Administration and Marketing Society found that 75 percent of those surveyed planned rate increases ranging from relatively low increases to more substantial increases (30 percent) On average, the expected increase would be 18 5 percent 33/

In a more recent survey conducted by the National League of Cities of 233 franchising authorities covering 274 franchises serving 4.68 million subscribers, it was found that 82 6 percent of the cable operators surveyed increased their basic rates In 40 4 percent of the rate increases, the number of services included in basic services also increased. In the other 42 3 percent where the number of services was not increased, the average increase of basic rates was 27 5 percent Of the 42.3 percent that did not increase the number of services, however, 17 3 percent decreased their pay service rates. Of the remaining cable operators surveyed, 14.4 percent did not change their basic service rates while only 2 percent reduced their rates 34/ Even a recently released study of the deregulated cable industry by National Cable Television Association found that, in a sample of 598 responding cable systems35/ which reach

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33/ This is reported by Laura Landro, "Cable TV's New Freedom Promises Higher Prices - but More Services," _Wall Street Journal_, p 31, C4, Dec. 12, 1986

34/ National League of Cities, _Impact of the Cable Act on Franchising Authorities and Consumers_, Washington, D C , September 18, 1987

35/ The overall response rate was 23% There is no evidence one way or the other whether the responding cable systems were significantly different from those which

16% of cable households, the average basic rate increased by 10.6% since January 1987. NCTA's estimates appear to be very low in comparison with those reported by other sources.

Table 4 also compares annual industry average basic cable rates to the average rate increases for those systems granted increases in the same year. (See also Figures 1-3). During the period 1979-86, rate increases for the average system obtaining a rate increase were approximately 3 percent to 5 percent higher than the industry average. In 1985, the average system that obtained a rate increase was almost equal to the industry average. While 1987 figures are not yet available, it seems likely that the rate increases for those operators raising their rates will be higher than the industry average as the number of rate changes has also increased significantly. In 1986, for example, there were rate changes in 566 communities in 40 states. In contrast there have already been 968 rate changes in 45 states in the first half of 1987.[36/]

Accompanying the relative price changes, a survey by the National League of Cities also shows that there was a reduction in the number of basic service tiers in 1987. Approximately 17 percent of the MSOs surveyed reduced their basic service tiers; 80.8 percent offered no change, and only 2.3 percent actually increased the number of basic service

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failed to respond to the questionnaire.

36/ Estimates of Paul Kagan Associates, Cable TV Franchising News Roundup, September 31, 1987, p 2.

tiers. Prior to deregulation, 57.7 percent of the cable operators offered only one basic service tier; 25.7 offered 2 tiers; 11.3 percent offered 3 tiers; and 5.4 percent offered 4 or more tiers. After deregulation, 71 2 percent offered one basic tier; 18.1 percent offered two tiers, 6.2 percent offered 3 tiers and 4 percent offered 4 or more tiers.

Thus, the available evidence strongly points to increased basic rates in the deregulated marketplace. In addition, as Paul Kagan observes, CSOs pushed through substantial rate increases in anticipation of full deregulation in January of 1987 As stated in The Pay TV Newsletter, "[w]ith anticipation of full deregulation in January 1987, cable operators took the lid off basic rates in 1985. According to KAGAN CENSUS data, operators hiked basic rates by a record 11% ..."[37/] And, as we noted in Table 4, substantial rate increases took place in 1986. Indeed, over the past two and a half years, basic rates increased by about a third, substantially in excess of increases in the CPI.

It is important to note that it is not possible to use the surveyed data on prices to test whether the FCC's "three signal" rule for estimating effective competition is valid. First, neither the National League of Cities nor the NCTA relates price changes in particular franchises to the number of available broadcast television signals, which is the key issue here Second, the NCTA study neglects the fact

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37/ The Pay TV Newsletter, Paul Kagan Associates, May 30, 1986, p 4 that basic rates increased rapidly during 1985 and 1986. Third, the studies do not indicate whether the basic rates in the regulated environment were substantially below monopoly levels. Indeed, if these rates were close to monopoly levels, deregulation would not have a significant impact on basic rates. Nevertheless, the fact that rates have been increasing rapidly suggests that some previously unexploited pricing power is now available to CSOs.

5. The FCC Can And Should Do Better Analysis Than That Which Resulted in The "Three Signals" Finding

This synopsis suggests that the short history of the deregulation of cable is far from a picture of unambiguously procompetitive behavior Deregulation was not required to bring financial health to a sickly business, as it did for the railroad industry for example. In fact, prior to deregulation cable companies were in sound financial positions (especially if they were able to renege on promises made during franchise bidding wars). Also, deregulation did not bring lower prices to a mass of cable subscribers, as it did in the airline industry.[38] In fact, subscription prices appear to have risen substantially even after making allowance for expansion of programming included in basic service And, finally, deregulation did not induce the entry of new competitors as it did in the airline industry. In fact, the alternative cable technologies are finding the

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38/ See, e g., S. Morrison & C. Winston, "The Economic Effects of Airline Deregulation," The Brookings Institution (Washington, DC), 1986.

deregulated environment largely inhospitable to entry and expansion. Under these circumstances, as implemented by the FCC, the 1984 Cable Act may have been unwise legislation In any event, the radical changes in the marketplace to which the Act has contributed demonstrate that the Commission's conclusions about competition for cable are, at a minimum, based on out-of-date information and poor methodology

Table 1
U S Cable Penetration
(1985 1987)

	Total Systems	Percent Increase	Basic Subscribers	Percent Increase	Pay Units	Percent Increase	Homes Passed	Percent Increase	Total Franchised Homes	Percent Increase
1985	6675		30759556		25599448					
1986	7546	0 13	36931375	0 20	27042372	0 06	52171078		47023634	
1987*	7836	0 04	38762246	0 05	28637268	0 06	55477512	0 06	49890122	0 06

* As of April 1 _1987

Source Television and Cable Factbook 1985 1986 and 1987 Editions

Table 2

Pay Cable Packager--Cable System Operator Ties
(1978-79 Data)

Corporate Owner	Pay Cable Packager	Number of Affiliates	Subscribers	Cable MSO	Number of Systems	Subscribers
Time, Inc	Home Box Office	800	2,000,000	ATC[1]	94	714,000
(Joint Venture)	Showtime	260	650,000	Teleprompter	110	1,110,000
				Viacom	30	360,000
Warner	Star Channel	17	105,000	Warner	140	576,000
TOTALS		1077	2,755,000		374	2,760,000
% OF NATIONAL TOTALS[2]			84%			19%

Source Braunstein (1980)

Notes:

[1]Does not include Manhattan Cable (94,000 subscribers)

[2]Based on 14,500,000 cable subscribers and 3,300,000 pay subscribers

Appendix A1

Rate Increase (Percentage)	Cost/Price Ratio 1/1.5	1/2	1/3	1/4	1/10	1/20
1	3	2	1.5	1.3	1.1	1.1
10	30	20	15.0	13.3	11.1	10.5
25	75	50	37.5	33.3	27.8	26.3
50	150	100	75.0	66.7	55.6	52.6
75	225	150	112.5	100.0	83.3	78.9
100	300	200	150.0	133.3	111.1	105.3

To read this table, the first column represents various rate increases. Reading horizontally for each respective rate increase are the percent reductions in market penetration required to make the rate increase unprofitable. For example, a 10 percent rate increase would be unprofitable if it were to induce a 20 percent reduction in market penetration with a cost/price ratio equal to 1/2. $(20 = (10/[1 - (1/2)]) = (10/[1 - (vc/p)])$.

Table 3

Pay Cable Packager--Cable System Operator Ties
(1984 Data)

Corporate Owner	Pay Cable Packager	Number of Affiliates	Subscribers	Cable MSO	Number of Systems	Subscribers
Time, Inc	Home Box Office	5,000	12,500,000	ATC	463	2,400,000
(Joint Venture)[1]	Showtime/	3,100	5,000,000	Viacom	19	752,000
	The Movie Channel	2,900	3,000,000	Warner Amex	n/a	1,383,000
TOTALS		11,000	20,500,000			4,535,000
% OF NATIONAL TOTALS[2]			100%			15%

Sources: <u>Broadcasting Cablecasting Yearbook</u> and <u>Television & Cable Factbook</u>

Notes

[1]Owners of combined Showtime/The Movie Channel joint venture
- Viacom 50%
- Warner Amex 31%
- Warner Communications 19%
- (one of the owners of Warner-Amex)

[2]Based on 30,000,000 cable subscribers and 20,500,000 pay subscribers

TABLE 4

Year	(1) Average Old Rate	(2) Average Rate Increase Granted*	(3) Average Percent Increase (By Year) [(2) (1)]/(1)	(4) Rate of Increase of Basic Rates	(5) Industry Average Basic Rate	(6) Industry Percent Increase (By Year) [(5) (1)]/(1)	(7) Rate of Increase Industry Rates	(8) Percentage of Difference [(2) (5)]/(5)
1979	6 75	7 76	14 96		7 53	11 56		3 05
1980	7 03	8 08	14 94	4 12	7 85	11 66	4 25	2 93
1981	7 32	8 36	14 21	3 47	8 14	11 20	3 69	2 70
1982	7 70	8 88	15 32	6 22	8 46	9 87	3 93	4 96
1983	7 92	9 22	16 41	3 83	8 76	10 61	3 55	5 25
1984	8 31	9 79	17 81	6 18	9 20	10 71	5 02	6 41
1985	9 00	10 23	13 67	4 49	10 24	13 78	11 30	0 10
1986	9 51	11 41	19 98	11 53	11 08	16 51	8 20	2 98
1987 **	10 26	12 70	23 78	11 31	N/A	N/A	N/A	N/A

* For 1979 through 1986 rate/system increases granted by local authorities
In 1987 basic rate increases were deregulated
** First six months of 1987 only

(1) Rate/system
(2) Includes tiers
(5) Rate/subscriber

Source Paul Kagan Associates Cable TV Franchising various issues

Notes to accompany Table 4

The table compares annual average basic cable rates (rate/subscriber) to the average rate increases for cable systems that were granted rate increases (rate/system) in the same year

Columns 1-4 summarize data for just those cable systems that were granted rate increases Column 1 shows the average basic rate prior to the rate increases, Column 2 shows the average rate increase that were granted for 1979-1986 Column 3 shows the percentage increase in basic rates in any year for those systems that had rate increases granted Column 4 calculates the percentage change of the average rate increase granted by local authorities over time

Column 5 shows the annual average basic cable rate (rate/subscriber) for the period 1979-1986 Column 6 shows the percentage increase of annual average cable rates for each year calculated using the average old rate as the standard of comparison This calculation will differ slightly from that in Column 3 since it calculates the average basic rate of all cable systems (i e including those which did not have rate increases granted and those which had not applied for a rate increase in any particular year) Column 7 shows the increase of the annual average basic rate over time

Column 8 shows the difference between the average rate increase granted to cable systems (Column 3) and the annual average basic rate (Column 6) It shows that, between 1979 and 1986, the average cable system that was granted a rate increase charged approximately 3 - 5 percent more than the industry average

TABLE 4A

Year	(1) Average Old Rate	(2) Average Rate Increase Granted*	(3) Average Percent Increase (By Year) [(2) (1)]/(1)	(4) Rate of Increase of Basic Rates	(5) Industry Average Basic Rate	(6) Industry Percent Increase (By Year) [(5) (1)]/(1)	(7) Rate of Increase Industry Rates	(8) Percentage of Difference [(2) (5)]/(5)
1986	9 51	11 41	19 98	11 53	11 08	16 51	8 20	2 98
1987(i) **	10 26	12 70	23 78	11 31	12 70	23 78	14 62	0 00
1987(ii) **	10 26	12 70	23 78	11 31	12 27	19 59	10 74	3 50
1987(iii)**	10 26	12.70	23 78	11 31	12 10	17 89	9 16	5 00

1987(i) Estimated 1987 industry average equal to average rate increase
1987(ii) Estimated 1987 industry average 3 5 percent less than the average rate increase
1987(iii) Estimated 1987 industry average 5 0 percent less than the average rate increase

* For 1979 through 1986, rate/system increases granted by local authorities
In 1987, basic rate increases were deregulated
** First six months of 1987 only

(1) Rate/system
(2) Includes tiers
(5) Rate/subscriber

Source Paul Kagan Associates, Cable TV Franchising, various issues.

Table 4A uses the data in Table 4 to calculate estimates of the annual industry average basic cable rate in 1987 Using the average rate increase of those cable systems that had increased their basic rates in the first six months of 1987 as a benchmark, we calculate three estimates of the average basic rate for 1987 The different estimates depend upon assumptions of how much the annual average basic rate will differ from the average rate increase for those cable systems that increased their rates Since this difference averaged between 3 and 5 percent throughout the period 1979-1986, the first estimate is made on the assumption that the annual basic rate will be the same as the average rate increase of those systems that raised their rates, the second is that the annual average rate will be less than the average rate increase by 3 5 percent, and the third is that the annual average rate will be less than the average rate increase by 5 percent These estimates seem reasonable in light of the increasing number of rate increases that have already taken place in 1987 In 1986, for example, there were rate changes in 566 communities in 40 states and the average cable system that was granted a rate increase charged roughly 3 percent more than the industry average basic rate In contrast, there were 968 rate changes in 45 states in the first half of 1987 [1] Therefore, the larger percentage of all cable systems increasing their rates would tend to make the average rate increase by cable systems that have raised their rates closer to the industry average in 1987

In a recent survey of cable rate deregulation by the National Cable Television Association (NCTA),[2] the average basic service rate that an average subscriber paid in July 1987 was found to be $13 11 The NCTA study shows that the rate increase for the cable systems surveyed had increased by 10 6 percent between December 1986 and July 1987 Using their estimate of the average basic rate in July 1987 the increase of the industry annual average basic rate over that which prevailed in 1986 would then be 18 3 percent (significantly higher than our relatively conservative estimates) In contrast, in 1985-1986 the industry annual average basic rate had increased by only 8 2 percent

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1 Estimates of Paul Kagan Associates, Cable TV Frinchising News Roundup, September 31, 1987, p 2

2 National Cable Television Association, Rate Deregulation, Cable Industry Pricing Changes and Service Expansion in a Deregulated Environment, November 1987

Figure 1: Average Rate Increases Granted
Versus Changes in the
Consumer Price Index (CPI)
By Year (1979-1987)

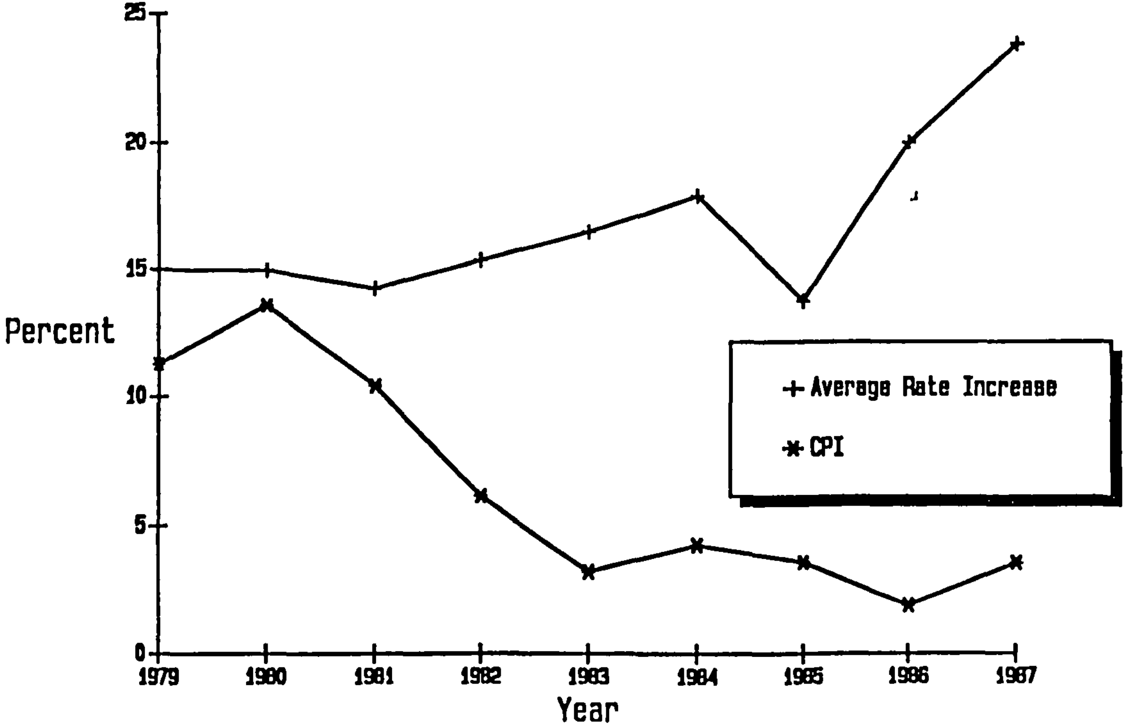


Figure 2: Industry Average Rates/Subscriber (1979-1987)

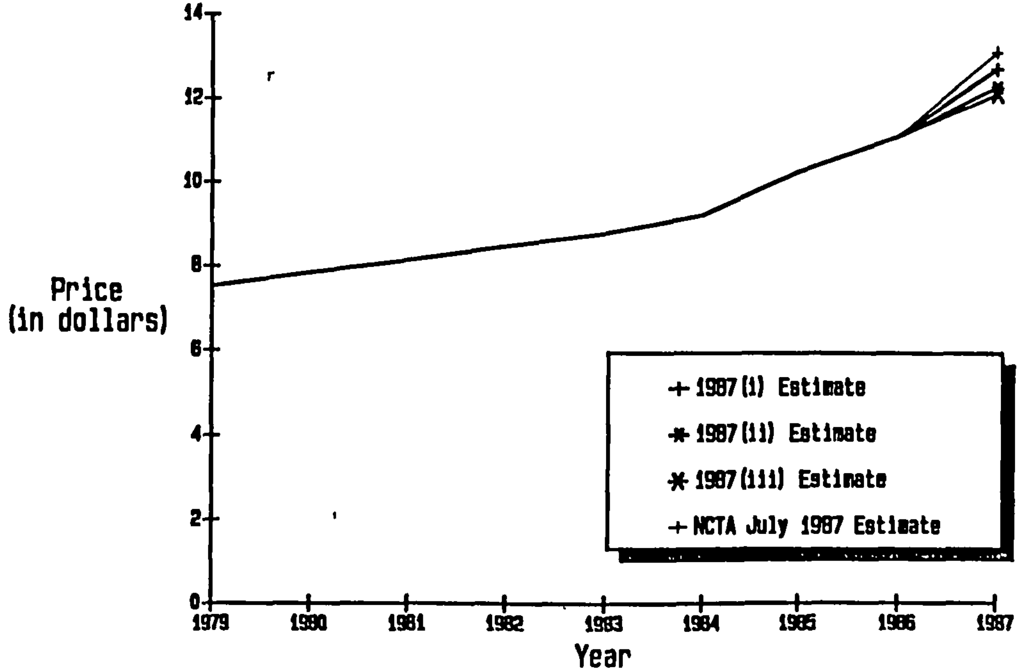
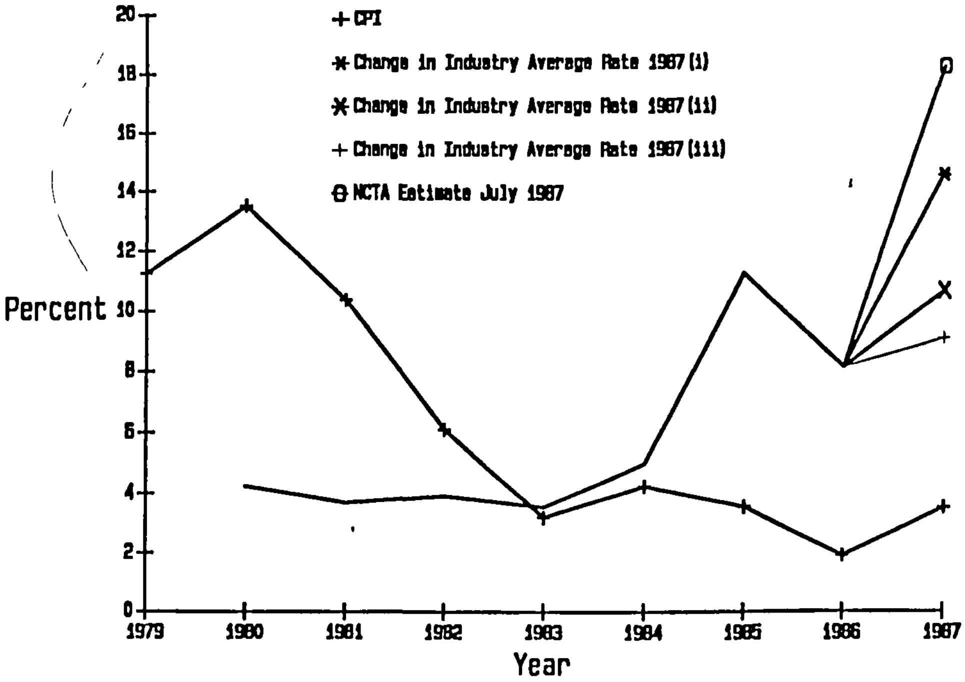


Figure 3: Percentage Increase of the Industry Average Basic Rate Using Different Estimates of the 1987 Industry Average (1979-1987)



Attachment No. 2

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ANTITRUST AND REGULATION IN CABLE TELEVISION: FEDERAL POLICY AT WAR WITH ITSELF

By
GLENN B MANISHIN

ANTITRUST AND REGULATION IN CABLE TELEVISION FEDERAL POLICY AT WAR WITH ITSELF

GLENN B MANISHIN*

I INTRODUCTION

Although antitrust law and regulation often conflict,[1] one situation in which the two should presumably function in harmony is natural monopoly[2] Where a single firm can most efficiently supply all the demand in a given market, antitrust has often given way, in large part, to regulation[3] Electric utilities, for example, are generally considered natural monopolies, and as a consequence, are both protected against competitive entry and subject to universal service obligations[4] While the antitrust laws cer-

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[1] *See e g* MCI Communications Corp v AT&T, 708 F 2d 1081 1100-11 (7th Cir) (discussion of cases regarding the conflict of antitrust law and regulation) *cert denied* 464 U S 891 (1983) United States v AT&T 461 F Supp 1314 1321 (D D C 1978) 1 P AREEDA & D TURNER ANTITRUST LAW ¶ 223d (1978) Comment *The Application of Antitrust Law to Telecommunications* 69 CALIF L REV 497 (1981)

[2] Natural monopoly can be defined in nontechnical terms as a market characterized by high economies of scale such that a single firm will be the most efficient supplier of goods or services in the long run at any given level of demand *Report on Regulatory Reform by the Industrial Regulation Committee of the American Bar Association Section of Antitrust Law* 54 ANTITRUST L J 503 506 516 (1985) [hereinafter *Regulatory Reform Report*] The economic definition of natural monopoly is considerably more complicated *See e g* Baumol *On the Proper Cost Tests for Natural Monopoly in a Multiproduct Industry* 67 AM ECON REV 809, 809-10 (1977) The typical assumption is that in a market conducive to natural monopoly only a single firm can survive *Regulatory Reform Report supra* at 506 *see also* Fishman v Estate of Wirtz 807 F 2d 520 532 (7th Cir 1986) (professional basketball in any major city is a natural monopoly since only one team can practically survive)

[3] In [natural monopoly] markets traditional utility-type rate regulation is imposed to maintain prices and output at levels that are supposed to approximate the results of effective competition *Regulatory Reform Report supra* note 2 at 506

[4] The electric power industry is regulated at both the state and federal levels *See* 16 U S C § 824 (1982) Other industries in which the natural monopoly rationale have served to justify public utility regulation include railroads oil and gas pipelines and telephone service *Regulatory Reform Report supra* note 2 at 506 *see generally* S BREYER REGULATION AND ITS REFORM 15-35 (1982) As in other industries the precise boundaries of the natural monopoly in the electric power industry have been the subject of dispute *See e g* City of Cleveland v Cleveland Elec Illuminating Co 538 F Supp 1306 (N D Ohio 1980)

tainly apply to efforts to extend natural monopoly power,[5] antitrust and regulation have achieved a workable equilibrium, one firm serves the entire market and its rates are constrained by regulation, typically by prescribing the firm's prices or rate of return [6] In short, the traditional *quid pro quo* for the *market failure* of natural monopoly is regulation [7]

In cable television, however, harmony has yet to be achieved Developments over the past several years have established a legal environment in which cable television is largely subject to neither antitrust nor regulation First, in implementation of the Cable Communications Policy Act of 1984 ("Cable Act"),[8] the Federal Communications Commission (' FCC") determined that virtually all cable television systems face "effective competition," precluding municipal rate regulation [9] Second, in aspects such as system design and channel deployment, the Cable Act preempts the major means of nonrate cable regulation through restrictions on enforcement of franchise terms [10] Finally, after spending nearly

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[5] *E g* Otter Tail Power Co v United States, 410 U S 366 (1973) City of Mishawaka v American Elec Power Co , 616 F 2d 976 (7th Cir 1980) *cert denied* 449 U S 1096 (1981)

[6] *See supra* note 3 The natural monopoly justification for regulation can be used strategically by firms and legislatures to promote their own interests it may be used to shelter a firm from competition and permit subsidized rates for some classes of consumers R NOLL & B OWEN THE POLITICAL ECONOMY OF DEREGULATION 53-65 (1983)

[7] Some have argued that an unregulated natural monopoly is preferable to an inefficiently regulated natural monopoly *See* Kahn *The Passing of the Public Utility Concept A Reprise in* TELECOMMUNICATIONS REGULATION TODAY AND TOMORROW 3-37 (E Noam ed 1983) Posner, *Natural Monopoly and its Regulation* 21 STAN L REV 548 (1969) Still others have argued that contestable" natural monopoly markets will behave competitively *See* Panzar & Willig *Free Entry and the Sustainability of Natural Monopoly* 8 BELL J ECON 1 (1977) However the traditional public utility model generally remains valid

[8] Pub L No 98-549 98 Stat 2780 (codified as amended at 47 U S C §§ 521-59 (Supp III 1985))

[9] *See infra* text accompanying note 66-69 Section 623(b)(1) of the Cable Act, 47 U S C § 543(b)(1) (Supp III 1985), directed the FCC to promulgate, within 180 days, 'regulations which authorize a franchising authority to regulate rates for the provision of basic cable service in circumstances in which a cable system is not subject to effective competition " The rules ultimately adopted by the FCC prohibit municipal rate regulation for more than 99% of all cable systems Brief for Intervenors National League of Cities at 13, ACLU v FCC, 823 F 2d 1554 (D C Cir 1987) (No 84-1666) [hereinafter National League of Cities Intervenor s Brief]

[10] For example, section 624(b) of the Cable Act, 47 U S C § 544(b)(2)(b) (Supp III 1985), provides that municipalities may seek and enforce programming requirements only for 'broad categories of video programming " This provision prevents enforcement of franchise terms that commit the cable system to carry specified programming services Similarly, section 625(a)(1), 47 U S C § 545(a)(1) (Supp III 1985) provides that cable systems can modify extant franchise agreements if (a) provisions relating to facilities or equipment are "commercially impracticable' or (b) with regard to programming services the "mix, quality, and level' of service is maintained Section 625(b) 47 U S C § 545(b) (Supp III 1985), grants a right to judicial review of denied requests for franchise modification and section 625(c), 47 U S C § 545 (c) (Supp III 1985) allows a cable system to drop programming services if the copyright payment is substantially increased and "has not been specifically compensated for by rate increases Finally,

two years examining both the phenomena of cable system "clustering"[11] and mergers between "overbuilds",[12] the Department of Justice (the "Department") announced in April 1985 that it will defer to municipalities on cable mergers and generally refuse to apply the Clayton Act[13] in light of cable's "natural monopoly characteristics "[14]

Although the FCC and the Department have often disagreed,[15] their positions regarding cable are incompatible The FCC has apparently concluded that cable systems generally *are not* natural monopolies, and therefore should not be regulated If so, then antitrust laws should be enforced vigorously to preserve both actual and potential competition in cable television, particularly to prevent mergers among overbuilt systems However, the Department will not challenge these mergers[16] because it concludes that cable systems generally *are* natural monopolies

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Section 626 47 U S C § 546 (Supp III 1985) provides procedural rules for municipal consideration of franchise renewals, and requires franchises to be renewed if, *inter alia* the cable system has ' substantially complied with the material terms' of the franchise and its quality of service has been reasonable in light of community needs Section 626(e) 47 U S C § 546(e) (Supp III 1985), also grants a right to judicial review for cable systems of refranchising decisions

The Cable Act's legislative history clearly indicates that the purpose of these sections was to provide stability *and certainty* to the renewal process H R REP No 934, 98th Cong 2d Sess 25 (1984) (emphasis added) [hereinafter HOUSE REPORT] The Act in effect creates a presumption of franchise renewal The actual impact of these provisions however has yet to be tested significantly in the market While there are indications that refranchising competition may increase over time *see id* at 22 *Rights Wars Growing in Cable TV*, Wall St J Aug 25 1982 at 21, col 2 there is no clear trend *See infra* text accompanying notes 115-16

[11] Clustering ' is the consolidation of cable systems in adjoining or nearby municipalities *See* Note *Product Market Definition For Video Programming* 86 COLUM L REV 1210, 1217 (1986)

[12] Overbuild is the term used in the cable television industry to describe situations in which two or more competing cable systems serve all or part of the same geographic area Nishimura v Dolan 599 F Supp 484 489 n 4 (E D N Y 1984)

[13] 15 U S C § 12 (1982) Section 7 of the Clayton Act prohibits mergers and acquisitions 'against unlawful restraints and monopolies in any market *Id* at § 7

[14] *See infra* text accompanying notes 72 73

[15] *See e g* United States v AT&T 552 F Supp 131 170 187 (D D C 1982) *aff'd sub nom* Maryland v United States 460 U S 1001 (1983) The Department of Justice s [hereinafter Department] 1986 support of proposed legislation introducted by Senator Dole *see* S 2565 99th Cong , 2d Sess (1986) that would have transferred jurisdiction of the *AT&T* decree to the FCC, *see e g* Remarks by Douglas H Ginsburg Assistant Attorney General, Antitrust Division before the Computer and Communications Industry Association (July 17 1986) appeared designed at least in part to mend the rift between the agencies arising from the *AT&T* litigation *See also* Report and Recommendations of the United States Concerning the Line of Business Restrictions Imposed on the Bell Operating Companies by the Modification of Final Judgment, United States v Western Elec Co No 82 0192 (D D C filed Feb 2 1987) (recommending major modifications to the *AT&T* decree and increased reliance on FCC regulation)

[16] Nor has the Department indicated any real willingness to address other current competitive issues in cable television *See infra* notes 79 103, 120-24 132-34 and accompanying texts

As a result, current federal policy effectively applies neither regulation nor antitrust to cable television

The conflict between the FCC and the Justice Department is perhaps the clearest example of the present disarray in cable television policy, but it is not the only one The Supreme Court has recently entered the fray, under the guise of the first amendment, suggesting that cable competition can be *mandated* under certain circumstances by the Constitution [17] A number of federal courts have applied the antitrust laws to cable mergers and cable franchising competition [18] While the Department has decided to defer to municipal competitive decisions on cable, the Federal Trade Commission has threatened to sue municipalities for restricting competition in industries such as taxi cabs [19]

The issue whether cable is a natural monopoly is the subject of debate among economists,[20] but it is somewhat less relevant than the issue of who should make that determination, i e, whether the FCC, the Department, the federal courts, states, or municipalities should set competitive and regulatory policy in cable televsion Another issue concerns whether competitive structure of local cable markets should be decided by the market itself Indeed, if municipalities can determine the number of cable firms that can serve a market, thereby "preempting" the Department's antitrust enforcement role, arguably they should also determine the degree of regulation appropriate to that market, in effect preempting the FCC The answers to these questions may not be easy If they remain unresolved, however, the internal tensions in federal cable policy may spark something few observers want a new round of lobbying on Capitol Hill and, perhaps, a new legislative solution that satifies no one [21]

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[17] *See* City of Los Angeles v Preferred Communications, Inc, 476 U S 488 (1986) *see infra* text accompanying notes 104-14 For a discussion of this case along similar lines *see* Comment *Do Cable Operators Want Free Speech or a Free Market? Preferred Communications Inc v City of Los Angeles* 6 CARDOZO ARTS & ENT L J 161 (1987)

[18] *See infra* notes 96-101 and accompanying text

[19] *See In re* City of New Orleans, 3 Trade Reg Rep (CCH) ¶ 22,149, at 22 997-98 (May 10 1984)

[20] *See, e g* B OWEN & P GREENHALGH, COMPETITIVE POLICY CONSIDERATIONS IN CABLE TELEVISION FRANCHISING (1985), A SMILEY, DIRECT COMPETITION AMONG CABLE TELEVISION SYSTEMS (1986) Noam *Economies of Scale in Cable Television A Multiproduct Analysis*, *in* VIDEO MEDIA COMPETITION REGULATION, ECONOMICS AND TECHNOLOGY (E Noam ed 1985), *see also* Nadel, *Cablespeech for Whom?* 4 CARDOZO ARTS & ENT L J 51 62 n 62 (1984) (fewer than 50 cable system overbuilds in existence), "Range Wars" *Cable Television Business*, Sept 15, 1985, at 21-24 (discussing cable overbuilds)

[21] During the first session of the 99th Congress, Senator Danforth then Chairman of the Commerce Committee reportedly suggested that ' Congress might be forced to redress some imbalance in the rules governing must-carry, franchise exclusivity cable system concentration and other matters COMMUNICATIONS DAILY Aug 1, 1986, at 3

II A TALE OF TWO AGENCIES

The FCC's approach to cable television has evolved considerably over the years In the industry's early history, the FCC imposed a number of restrictive regulations upon cable systems [22] These regulations were premised on the fear that cable's widespread growth could threaten the economic viability of broadcast television, and correspondingly, the FCC's long-standing broadcast policy favoring localism [23] With the collapse of this rationale however, the FCC was forced to reconsider its protectionist approach Subsequent changes included preemption of municipal rate regulation of "pay" cable programming,[24] repeal of the syndicated exclusivity and distant signal rules,[25] and finally preemption of restrictions on the "retiering" of system channel deployment [26]

The FCC's evolving regulatory approach to cable television roughly corresponded to the evolution of the cable industry itself Cable began as community antenna television (or CATV)—

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[22] These restrictive regulations included limitations on cable carriage of broadcast television signals guaranteed exclusivity for syndicated programming carried by local independent broadcast stations mandated nonduplication by cable systems of broadcast network affiliates and restrictions on cable system channel capacity *See generally* S RIVKIN CABLE TELEVISION A GUIDE TO FEDERAL REGULATIONS (1974) The FCC s policies [i]n combination effectively halted the growth of cable television in major markets 1 C FERRIS F LLOYD & T CASEY, CABLE TELEVISION LAW ¶ 5 05, at 5-12 (1987)

[23] *See generally* Note *The Collapse of Consensus Effects of the Deregulation of Cable Television* 81 COLUM L REV 612 615 17 (1981)

[24] Clarification of Cable Television Rules Notice of Proposed Rule Making and Inquiry, 46 F C C 2d 175 para 84 (1974) Establishment of Cable Television Subscriber Rates Notice of Inquiry 58 F C C 2d 915 para 2 (1976) Pay cable services which do not carry advertising and frequently offer movies charge a monthly fee for service in addition to the rate charged for the standard package of basic cable channels Home Box Office a service of Time Inc was the first commercially successful pay cable service *See infra* text accompanying notes 28-33

[25] Cable Television Syndicated Program Exclusivity Rules 79 F C C 2d 663 (1980) *aff d sub nom* Malrite T V of N Y v FCC, 652 F 2d 1140 (2d Cir 1981) *cert denied* 454 U S 1143 (1982) These rules required cable systems to 'black out syndicated programming if a local independent broadcast station, carried by the cable system had an exclusive contractual right to that programming and limited the number of nonlocal broadcast stations cable systems could carry *Cf* Geller v FCC 610 F 2d 973 (D C Cir 1979) (per curiam) The FCC recently proposed that the syndicated exclusivity rule be reimposed suggesting that it is anticompetitive and may give cable an unfair advantage over broadcast television 3 FCC Rule Making Rep (CCH) ¶ 21,045 (1987)

[26] Community Cable TV Inc , Memorandum Opinion and Order, 95 F C C 2d 1204 paras 18, 21-22 (1983) *reconsideration* 98 F C C 2d 1180, paras 13, 19, 23 (1984) This FCC decision permitted cable systems to move programming services among different 'tiers," *e g* from the basic tier to an intermediate expanded tier for which an additional monthly fee is charged regardless of any contrary provisions of municipal franchises For a discussion of tiering *see* 2 C FERRIS F LLOYD & T CASEY, *supra* note 22 ¶ 17B 03[1][c][i], at 17B-20-21 Although many cable systems provide various tiers of basic cable service pay services are generally not available unless the consumer also subscribes to a basic service *See* Friedman v Adams Russell Cable Services-N Y Inc 624 F Supp 1195 (S D N Y 1986)

a rudimentary means of collecting broadcast television signals for retransmission in areas where over-the-air reception was negligible or poor[27] The introduction of Home Box Office,[28] however, ushered in an era during which a host of new satellite-delivered programming services were developed specifically for distribution over cable[29] These services initially consisted exclusively of studio-produced movies airing before network television first-run exhibition, but later expanded to include the well-known, advertiser-supported "basic"[30] cable services such as ESPN CNN, and MTV,[31] frequently limited to a single subject and providing round-the-clock programming, and "superstations"[32] such as Atlanta's WTBS[33] As a result, by the late 1970's, cable system size had increased geometrically, sometimes to 100 channels or more, and competition for cable franchise awards created substantial incentives for even larger systems with increasingly elaborate "bells and whistles"[34] With a seemingly inexhaustible supply of programming, favorable tax treatment,[35] and extraordinarily high cash flow, the industry's future appeared virtually unlimited[36]

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[27] 1 C Ferris F Lloyd & T Casey *supra* note 22 ¶ 5 03 n 6 at 5-5

[28] *See supra* note 24

[29] *See e g*, Home Box Office Inc v FCC 567 F 2d 9 (D C Cir) (per curiam) (vacating anti-siphoning rule for pay cable) *cert denied* 434 U S 829 (1977)

[30] *See supra* note 26 Section 602(2) of the Cable Act defines basic cable service as 'any service tier which includes the transmission of local television broadcast signals 47 U S C § 522(2) (Supp III 1985) *See* House Report, *supra* note 10 at 40 As noted below the FCC s redefinition of basic cable service was reversed on appeal by the D C Circuit *See infra* note 51

[31] ESPN is the Entertainment and Sports Programming Network, now owned by ABC CNN is the Cable News Network a service of Turner Broadcasting Systems MTV is Music Television a music video programming service, owned by Viacom

[32] Superstations are broadcast television stations distributed to cable systems nation wide by satellite *See* 2 C Ferris F Lloyd & T Casey, *supra* note 22 ¶ 17B 02[3][c] at 17B-10

[33] More than forty satellite-delivered cable television programming services are available nationwide *See* Quincy Cable TV Inc v FCC, 768 F 2d 1434, 1452 (D C Cir 1985) *cert denied* 106 S Ct 2889 (1986) Scrambling of Satellite Television Signals Report and Order 104 F C C 2d 1444 1448-49 (1986)

[34] This colloquial term of art in the cable industry denotes extra' features, such as sophisticated local origination facilities and two-way data transmission capability that many cable television companies offered to municipalities to induce the award of a franchise Extremely heated franchising competition among cable companies and a number of instances in which cable systems could not supply all of the "bells and whistles' required by their franchising commitments were the principal reasons cited by Congress to support restricting municipal authority to seek (or enforce) certain types of franchise obligations *See* House Report *supra* note 10, at 21-22.

[35] *See* 1 C Ferris, F Lloyd & T Casey, *supra* note 22, ¶ 29 01, at 29-2 Until it was eliminated in 1987 the investment tax credit provided cable systems with generous federal tax deductions for the capital costs of system construction In addition many cable systems even among the largest cable companies, are organized as limited partnerships with the attendant tax advantages associated with that form of ownership

[36] The balance may now have swung too far in the other direction favoring cable at

In contrast to the FCC, throughout the 1970s, the Department viewed cable television with almost benign neglect. Although the Department participated in a number of FCC rulemakings, its antitrust enforcement efforts in television focused largely on a series of monopolization lawsuits against the three broadcast networks.[37] As the decade came to a close, however, the Department began to take a more active antitrust interest in the cable industry. In 1980, the Department successfully challenged the formation by a number of leading movie studios of "Premiere," a new movie-driven pay cable service with exclusive first-refusal rights to the studios' output.[38]

The Department's enforcement activity in cable television shifted shortly thereafter from cable programmers to system operators. Beginning in mid-1983, the Department initiated a series of antitrust investigations, covering a half dozen transactions over the course of nearly two years,[39] into the competitive effect of cable system acquisitions, mergers and "swaps."[40] Initially concerned primarily with the phenomenon of clustering and its effects on franchising competition, these investigations were later expanded to include mergers among overbuilt systems[41] and, eventually, well-publicized transactions between several of the

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the expense of other media. One FCC Commissioner has criticized the disequilibrium resulting from federal policies which may give cable television an unwarranted competitive edge in the program delivery market . . . [and have] helped to create the potential for cable to bottleneck reception of off-air and satellite programming. Amendment of Part 76 of the Commission's Rule Concerning Carriage of Television Broadcast Signals by Cable Television Systems, 1 F.C.C. Rcd. 864, 915 (1986) (statement of Commissioner Dawson).

[37] *E.g.*, United States v. National Broadcasting Co., 449 F. Supp. 1127 (C.D. Cal. 1978) (entering consent decree).

[38] United States v. Columbia Pictures Indus., Inc., 507 F. Supp. 412 (S.D.N.Y. 1980), *aff'd*, 7 Media L. Rep. (BNA) 1342 (2d Cir. 1981). The Premier venture was disbanded following the issuance of a preliminary injunction. Three years later, similar antitrust problems arose in the merger of Showtime and The Movie Channel, two leading pay cable programmers. Under threat of a Department lawsuit, the merger was restructured to eliminate several movie studios as participants in the post-merger venture. *See, e.g.*, 2 C. FERRIS, F. LLOYD & T. CASEY, *supra* note 22, ¶ 24.09[3][c], at 25-27; N.Y. Times, Aug. 13, 1983, § 1, at 29, col. 1; N.Y. Times, July 19, 1983, § D5, col. 5.

[39] In October 1985, James Mooney, then President of the National Cable Television Association, described the Department's "rather consistent interest" in cable system transactions, but observed that the "Justice [Department] is not warming up its paddy wagon to come get us." *Mooney Issues Warning on Antitrust Issues*, Multichannel News, Oct. 21, 1985, at 11, col. 3.

[40] These transactions, which are often structured as like-kind exchanges for tax purposes, involve the exchange of cable systems among cable television companies. The transaction involving Phoenix, Arizona discussed throughout this Article is one example of such a swap. *See infra* text accompanying notes 70-73.

[41] Two of the Department's 1984 investigations focused on mergers between directly competing systems in Slidell, Louisiana and Bryan/College Station, Texas. *See* Multichannel News, Apr. 15, 1985, at 4, col. 1.

largest multiple system operators ("MSOs")[42]

The Department's antitrust policy toward cable television was still in the formative stage when the prospect of cable legislation arose in Congress[43] Commencing with Senate Bill No 66, the initial bill introduced by Senator Goldwater,[44] the Department opposed restricting the scope of municipal regulatory authority over cable on the ground that this could undermine the effectiveness of franchise competition The Department reasoned that in the absence of direct competition between cable systems, competition for the franchise itself served as a surrogate for the competitive discipline of the market[45] The concerted lobbying of the cable industry, however, coupled with the intuitive appeal of a handful of instances of overreaching by municipalities in the franchising process, were apparently persuasive The Administration did not advance the Department's objections to Senate Bill No 66 and, in fact, took no public position on the bill[46]

In the summer of 1984, a negotiated compromise between the National Cable Television Association ("NCTA") and the National League of Cities[47] revived the legislation, which had stalled in the Senate, and returned the focus in cable television to the FCC The Cable Act, passed initially in the House and barely amended in conference eliminated Senate Bill No 66's standard for rate deregulation of cable systems the existence of four broadcast stations serving the community[48] The Cable Act instead delegated the issue to the FCC, directing the FCC to deter-

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[42] Multiple System Operator ("MSO") is a cable industry term denoting a company that operates more than one cable television system For the past five years or more, the two largest MSOs have been Tele-Communications, Inc ("TCI") and American Television & Communications Corp ("ATC"), a subsidiary of Time, Inc

[43] Although the Department investigated a number of cable television system mergers and acquisitions in 1983 and 1984, *see Closed Circuit Hounds Loose* BROADCASTING July 9 1984, at 9 each of these was either approved by the Department or voluntarily withdrawn by the parties

[44] S 66 98th Cong 1st Sess (1983) *See also* S 2172, 97th Cong, 2d Sess (1982) 129 CONG REC S325-26 (daily ed Jan 26, 1983) (statement of Sen Goldwater), 128 CONG REC 3358-61 (1982)

[45] The Department's reasoning on this point was hardly unconventional *See e g* Posner *supra* note 7 at 562 (emphasizing ability of municipalities "to drive a hard bargain with the would-be monopolist")

[46] The Department's objections were forwarded to the Office of Management & Budget as part of the established process of review by executive branch agencies of proposed legislation and bills passed by Congress The Administration did not explain publicly why it declined to take a position in support of or in opposition to S 66

[47] *See* 130 CONG REC H10 435, H10 440, H10,442 (daily ed Oct 1 1984) 130 CONG REC S14 284 (daily ed Oct 11, 1984)

[48] *See* S 66 98th Cong 1st Sess § 607 (1983) S REP No 67 98th Cong 1st Sess 22-23 (1983)

mine in what circumstances rate regulation is appropriate [49] Existing franchise provisions permitting rate regulation would be grandfathered until January 1, 1987, after which regulation would be authorized where "a cable system is not subject to effective competition" pursuant to Commission-promulgated rules [50]

The "effective competition" debate before the FCC was acrimonious Yet it hinged less on considerations of appropriate regulatory policy and more on the antitrust-oriented issue of product market definition [51] Beginning from the somewhat tenuous premise that the Act was intended to deregulate most cable systems,[52] the FCC proposed that where four nonduplicated broadcast signals are available, the "subscriber's ability to disconnect" provides effective competition for cable television [53] The cable industry supported this proposal in full measure, contending that a host of alternative distribution media—including videocassette recorders ("VCRs"), subscription television ("STV"),[54] satellite master antenna television ("SMATV"),[55]

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[49] Cable Act § 623 47 U S C § 543 (Supp III 1985) *see* HOUSE REPORT *supra* note 10 at 24-25 65-68 *supra* note 9

[50] Cable Act § 623(b) (c) 47 U S C § 543(b) (c) (Supp III 1985)

[51] Two issues of statutory interpretation—the scope of basic cable service for which the Cable Act authorized regulation (*see* Cable Act § 602(2) 47 U S C § 522(2) (Supp III 1985)) and the validity of the FCC s decision preempting restrictions on retiering (*see* Community Cable TV Inc 98 F C C 2d 1180 (1984)) were also the subject of considerable debate For a discussion of the Commission s redefinition of basic cable service see ACLU v FCC 823 F 2d 1554 1565-70 (D C Cir 1987) *Compare* HOUSE REPORT *supra* note 10 at 40 *with* National League of Cities Intervenor s Brief *supra* note 9 at 35 36 With regard to retiering see Cable Act § 625(d) 47 U S C § 545(d) (Supp III 1985) (the HOUSE REPORT defines basic cable service as any service tier while the FCC in *Community Cable* restricts basic service to a single tier of service) HOUSE REPORT *supra* note 10 at 24 130 CONG REC S14 286 (daily ed Oct 11 1984) (Act does not affect legal challenge to FCC s 1984 retiering decision)

[52] *See* Implementation of the Cable Communications Act of 1984 50 Fed Reg 18 637 18 650 n 69 (1985) (to be codified at 47 C F R pts 1 63, 76 & 78) (Congress intended to significantly deregulate the provision of cable service), HEARINGS BEFORE THE SUBCOMMITTEE ON COMMUNICATIONS OF THE COMMITTEE ON COMMERCE SCIENCE AND TRANSPORTATION UNITED STATES SENATE 97th Cong 2d Sess 193 (1982) (statement of Mark Fowler FCC Chairman) (presumption that the marketplace environment in which cable television operates is competitive)

[53] Implementing the Provisions of the Cable Communications Policy Act of 1984 in MM Docket No 84-1296 FCC 84-612 Notice of Proposed Rulemaking 49 Fed Reg 48 765 48 771 (1984) (to be codified at 47 C F R pts 1 63 & 76)

[54] STV is a broadcast service generally using UHF frequencies to distribute pay television programming *See* Subscription Television Inc v Southern Cal Theatre Owners Ass n 576 F 2d 230 (9th Cir 1978) One example of STV is Oak Industries ON TV which at one time was a popular service in Southern California The STV industry has suffered a serious decline in recent years however since it is unable to compete with the multichannel programming diversity cable provides 2 C FERRIS F LLOYD & T CASEY *supra* note 22 ¶ 18 05 at 18 9

[55] SMATV is essentially a private cable system serving apartment complexes and other multiple dwelling units *See* D BRENNER & M PRICE CABLE TELEVISION § 13 01

multipoint and multichannel multipoint distribution services ("MDS" and "MMDS"),[56] direct broadcast satellite ("DBS"),[57] low-power television ("LPTV"),[58] and satellite or "television receive-only" earth stations ("TVROs")[59]—had developed to present effective competition for the delivery of video programming by cable systems [60] The industry maintained that cable existed within a far broader market and did not enjoy monopoly power [61]

Despite Congress' admonition that the existence of alternative distribution media nationwide was an insufficient basis on which to presume that a cable television system is subject to effective competition in any specific market,[62] few industry mem-

(1986) SMATV is a good example of a technology that on the surface appears to be a substitute for cable television but in reality is not competitive in many markets Some respected commentators believe that there is a large potential market for SMATV which will assure that cable does not hold a monopoly 2 C Ferris F Lloyd & T Casey, *supra* note 22 ¶ 19 10 at 19-19 Yet the 1982 National Association of Broadcasters study (*id* ¶ 21 02 n 1 at 21-3) clearly states that SMATV offers only a selective threat and is somewhat threatening to franchised cable *in markets where it becomes available before cable became entrenched* H Howard & S Carroll SMATV Strategic Opportunities in Private Cable 179 (1982) (emphasis added) *See also infra* note 130 (cable programmers have refused to deal with SMATV systems)

[56] MDS is a point-to-multipoint microwave technology frequently used to distribute pay television services in areas such as Washington D C that are not served by a cable television system *See* D Brenner & M Price *supra* note 55, § 16 04[1][a] to [3][a] MMDS is a multichannel MDS service authorized by the FCC pursuant to lottery that has yet to be introduced commercially in most major markets *Id* § 16 04[4][b]

[57] DBS is a satellite service that involves the transmission of TV signals from the earth to high-powered stationary satellites that permit reception by equipped individual homes *See* National Ass n of Broadcasters v FCC 740 F 2d 1190 1195 (D C Cir 1984) DBS is not yet in commercial operation *See id*

[58] LPTV is a newly authorized UHF broadcast service using transmitters of lower power than those traditionally required for UHF stations

[59] TVROs are the formal name for home earth stations and are known colloquially as satellite dishes or home satellite dishes (HSDs) *See* Scrambling of Satellite TV Signals Notice of Inquiry 104 F C C 2d 1444 (1986)

[60] These comments and arguments are summarized in the FCC s decision *See infra* note 67

[61] Some parties absurdly stretched this position *See e g* Comments of Farrow Schildhause at 3, MM Docket No 84-1296 (F C C filed Jan 29 1985) (cable competes in a market that includes movie houses newspapers radio stations colleges and universities legitimate theatres mail and express services, telephones, stadiums local opera societies and sports teams houses of religious worship and more) Even more restrained members of the industry however continue to maintain that the relevant product market necessarily includes not only video programming delivered by means other than cable [television] such as broadcast television MDS SMATV and VCRs but also other sources of news information and entertainment which themselves compete with video sources Reply Memorandum of the Time Defendants at 5 n 5 New York Citizens Comm on Cable TV v Manhattan Cable TV Inc 651 F Supp 802 (S D N Y 1986)

[62] House Report *supra* note 10, at 25, 66 (The Commission s standards should apply on a community-by-community basis since the presence nationwide of various telecommunications services does not speak to the availability of such services in a particular community The Committee thus does not intend that [the Commission should] impose nationwide deregulation as it has attempted to do in other rulemakings) *Id* at 66

bers offered more than a broad-brush approach to the issue The Department, for its part, proposed a set of far more restrictive criteria The Department argued that the "alphabet soup" of alternative delivery technologies had failed to develop as predicted by the cable industry and were effectively confined to relatively small niches in most markets[63] According to the Department, the economics of broadband cable television systems, specifically the ability to deliver a large number of programming channels at a relatively low cost per subscriber, coupled with the growing array of satellite-delivered cable programming available from few, if any, alternative delivery technologies, often resulted in cable systems enjoying significant market power[64] In short, the Department had concluded that cable television is a distinct product market[65]

Not surprisingly, the Department's proposal attracted heated opposition from the cable industry In April 1985, both the proposal and its underlying analysis were summarily dismissed by the FCC[66] Relaxing its proposed standard, the FCC concluded that "alternative sources of video programming do, in fact, offer competition to cable services"[67] and that "a

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[63] In the present technological and economic setting the likelihood of successful future entry by alternative media simply is too speculative to effectively constrain the present pricing behavior of cable operators Reply Comments of the U S Dept of Justice at 13 MM Docket No 84 1296 (F C C filed Feb 11 1985) For an extensive discussion of the limits to which the alphabet soup ' of alternative delivery technologies has made competitive inroads on cable television see *The New Order Passeth* BROADCASTING Dec 10 1984 at 43 see also Noam *Local Distribution Monopolies in Cable Television and Telephone Service The Scope for Competition* in *Telecommunications Regulation Today and Tomorrow* 351 359 (E Noam ed 1983) (a closer look at each of these ostensible competitors reveals that cable s significant technological and economic advantages will probably make it the dominant medium of the future barring unforeseen technological or regulatory developments) *Cf* Quincy Cable TV Inc v FCC 768 F 2d 1434 1439 n 8, 1450 (D C Cir 1985) (noting cable s virtually unlimited channel capacity) *cert denied* 106 S Ct 2889 (1986)

[64] *See* Comments of the U S Dept of Justice at 3 5, MM Docket No 84-1296 (F C C filed Jan 28 1985) [hereinafter DOJ Comments]

[65] *See id* at 23 n 43 (cable systems are likely to be able to exercise significantly greater power over price than is required under the [Department s] Merger Guidelines to conclude that a group of products or services constitute a relevant market) *id* at 16 n 26 (the distinctive competitive characteristics of cable television is the ability to deliver a relatively large number of video channels in a given market at a relatively low cost per channel) According to Charles F Rule then Acting Assistant Attorney General for Antitrust the Department considers cable television to be a relevant product market and the franchise area to be a relevant geographic market for antitrust purposes Freeman *Justice Adopts Hands-Off Stand on Clustering Systems* Multichannel News, Apr 15 1985 at 4 col 3 [hereinafter *Hands-Off Clustering*]

[66] Amendment of Parts 1, 63 and 76 of the Commission's Rules to Implement the Provisions of the Cable Communications Policy Act of 1984, 50 Fed Reg 18 637 18 649-50 (1985) *reconsideration* 104 F C C 2d 386 (1986) *aff d in part rev d and remanded in part* ACLU v FCC 823 F 2d 1554 (D C Cir 1987)

[67] 50 Fed Reg at 18 649

cable system will be considered to face effective competition whenever the franchise market receives three or more unduplicated broadcast signals "[68] While not expressly ground in antitrust analysis, the Commission's position is clear cable television competes within a broad "video programming" market and is generally not a monopoly, much less a natural one [69]

While the "effective competition" rulemaking was pending before the FCC, the Justice Department's antitrust investigations continued The Department intensively reviewed (for more than eight months) a proposed transaction which was, at that time, one of the largest cable system mergers on record, the "swap" between two major MSOs of cable systems in eight markets valued at approximately $200 million, including the two directly competing, overbuilt systems in Phoenix, Arizona and a nearby suburb [70] In light of the prominence of the Phoenix overbuilds,[71] it was widely assumed that the Department's decision on

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[68] 50 Fed Reg at 18 650

[69] In affirming the FCC s three-station rule for cable deregulation the D C Circuit did not review the underlying competitive and economic findings asserted by the Commission stressing rather the relatively short time frame within which Congress directed the agency to complete its rulemaking [and that it] fully anticipate[s] that the Commission will carefully monitor the effects of its regulations and make adjustments where circumstances so require *ACLU* 823 F 2d at 1565 Indeed, as several parties pointed out the FCC s belief that a cable system does not gain significant market advantage by offering satellite-delivered non-broadcast programming services 50 Fed Reg at 18 650 was squarely contradicted by the record, which demonstrate[d] that the cable industry experienced explosive growth only after offering these various non-broadcast services Brief for Intervenors National League of Cities, *supra* note 9 at 25 Moreover the Commission s exclusive focus on ' local broadcast television [does] not reflect the economic realities of basic cable service [specifically] the fact that basic cable service is marketed and priced as a package that frequently includes far more than must carry and local access channels DOJ Comments *supra* note 64, at 29 As the D C Circuit has recognized in a related context [c]able television and ordinary commercial broadcast television operate on the basis of wholly different technical and entrepreneurial principles *Quincy Cable TV*, 768 F 2d at 1438

[70] *See Times Mirror Storer Trade Eight Systems in Largest Swap Ever* Multichannel News July 9 1984 at 1 col 1 The transaction involved nearly 200 000 subscribers and arose in the first instance because the firms ha[d] been locked in a competitive overbuild situation in Paradise Valley Arizona, an affluent Phoenix suburb *Id* at 34

[71] As the chief cable officer for Phoenix stated in 1984, ' if you want to test competition this is the best place to do it,' [since there are] three companies [that] operate in the city, and about 10% of Phoenix households can receive service from either Times Mirror or Storer ' *Phoenix May Deregulate Rates & Basic Service*, Multichannel News Apr 23 1984 at 21 col 4 In Phoenix, the award of a multiple franchise followed the failure of the incumbent franchisee to build out its system and was in turn followed by one of the most rapid construction schedules of any major American city Other overbuilds have followed this pattern *See, e g*, Nishimura v Dolan, 599 F Supp 484 488-489 (E D N Y 1984) (Huntington, New York) There are also indications that in light of rate deregulation, overbuilds will increasingly be encouraged by cities as a means of constraining cable television rates *See Cable Industry Faces Increased Threat of Overbuilds* Multichannel News Sept 21 1987, at 20, col 1, *Patrick Warns Cablers to Steer Clear of Battle with Cities on Overbuilds*, COMMUNICATIONS DAILY May 21 1987 at 2 *FL Utility Unit Begins Cable System Overbuilds* Multichannel News Aug 4 1986 at 1 35 col 1 *NYT Exec*

the Phoenix transaction would crystallize its antitrust enforcement policy for cable television.

Unknown to most, however, the Department became increasingly concerned with the relationship between the roles of municipal and federal government in cable system transactions and the federalism implications of antitrust enforcement decisions. In April 1985, just two weeks before the FCC adopted its final "effective competition" rules, the Department terminated its investigation into the Phoenix transaction. In an unusual step, the Department issued a press release announcing that it would generally decline to challenge consolidation of competing systems in light of cable's "natural monopoly characteristics" and, instead, would defer to the decisions of municipalities as franchisors.[72] As the Department's press release explained:

> [W]here the relevant local government has the authority to deny transfer of a cable television franchise and thereby to prevent consolidation of overbuilt franchises, the Department will generally rely on the municipality's decision and will not bring suit to prevent consolidation unless unusual facts indicate that an exception should be made.
>
> A single firm may be able to provide cable service at lower cost than two or more competing firms. However, cable operators may not necessarily be forced by competitive pressures to return to consumers the benefit of efficiencies that result from consolidation and, in addition, a combination of overbuilt franchises can at least in the short run, result in higher prices to consumers.
>
> The local government responsible for a cable franchise decision usually is in the best position to evaluate the preferences of their citizens in the face of these potentially conflicting economic effects.[73]

Sees Overbuilds in Areas with Classic Systems Multichannel News Mar 3 1986 at 29 col 1; *San Diego Proceeding with Overbuild Strategy* CABLEVISION, July 8, 1985 at 11-12. *See also* COMMUNICATIONS DAILY Feb 2 1987 at 13 (if cable industry continues to prevail on first amendment grounds against municipal franchising authorities it could alienate cities to the point that they would grant franchise overbuilds.)

72 Department of Justice Press Release (April 1 1985) [hereinafter DOJ Press Release]. *See* 2 C FERRIS F LLOYD & T CASEY *supra* note 22 ¶ 24 06[4] at 24 20 1; COMMUNICATIONS DAILY April 2 1985 at 2. *See also Hands Off Clustering supra* note 65 at 4 (interview of then Acting Assistant Attorney General for Antitrust Charles F Rule). The Department conceded that because of the extent of the overbuild the transaction would eliminate substantial competition' in Paradise Valley. DOJ Press Release at 2.

73 DOJ Press Release *supra* note 72 at 2-3 (statement of J Paul McGrath, Assistant Attorney General Antitrust Division).

III THE POLICY CONUNDRUM

The degree to which actual and potential competition exists among cable systems in any given market, or between cable and alternative video delivery technologies, is a complex issue necessitating a detailed examination of market-specific evidence Regardless of one's conclusion as to the existence and economic feasibility of competition, however, it is clear that the competitive policies articulated by the FCC, the Department, and the Congress are almost entirely inconsistent On the fundamental policy of the role of municipalities in the regulatory process, each approaches the issue from contradictory premises

The FCC's prophylactic three-station standard for "effective competition," sacrificing accuracy in favor of administrative simplicity,[74] leaves no room either for countervailing market-specific evidence or municipal discretion Coupled with the FCC's prior rulings preempting state and local authority over pay cable rates and cable system tiering,[75] the standard suggests that the FCC believes local government is essentially incompetent to make the economic judgments on which to predicate regulatory decisions or, if given such authority, would likely opt for parochial solutions restricting cable's development Whether such an approach can weather the Supreme Court's recent retrenchment of the FCC's power to preempt state regulation[76] is unclear What is evident is that the FCC places little faith in municipalities as policy makers

The Department has articulated precisely the opposite conclusion It will decline to prosecute an otherwise meritorious action against a merger of cable systems under the Clayton Act if the municipalities involved approve the necessary franchise transfers [77] In the Department's view, not only are municipalities competent to make economic judgments on cable's regulatory

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[74] The FCC's similar decision to discontinue deciding cable franchise fee disputes arising before enactment of the Cable Act, was reversed Yakima Valley Cablevision Inc v FCC, 794 F 2d 737 (D C Cir 1986) The FCC's decision in the effective competition rulemaking was affirmed in part and reversed in part ACLU v FCC 823 F 2d 1554 (D C Cir 1987)

[75] *See supra* notes 24 26 and accompanying texts

[76] *Compare* Louisiana Pub Serv Comm'n v FCC 106 S Ct 1890 (1986) (state regulation of depreciation rates was not preempted by FCC regulations) *with* Capital Cities Cable v Crisp 467 U S 2694 (1984) (state regulation of retransmission by cable television system was preempted)

[77] Ironically the Commission has reemphasized that it will not review cable system mergers and acquisitions under the antitrust laws but rather will defer to the antitrust enforcement decisions of the Justice Department Group W Cable Inc ¶¶ 18-19 Mimeo No 4808 (released May 27 1986) (acquisition of Group W by TCI ATC and other MSOs) *Accord* Policy Regarding Character Qualifications in Broadcast Licensing

and competitive treatment, but since local government "is in the best position to evaluate the preferences of their citizens,"[78] such judgments should be given preclusive effect Indeed, the Department has seemingly abandoned all antitrust activity with regard to cable mergers since approving the Phoenix "swap" and apparently will even decline to review cable transactions absent some affirmative invitation by the affected municipalities[79] While the welfare effects of cable system consolidation may be ambiguous in the Department's view, the practical consequences of its deferral policy are clear Federal antitrust enforcement has been effectively jettisoned

Congress has appeared to steer a middle course, confirming municipal competence to set regulatory policy while limiting the breadth of its discretion In the franchising area, for example, the Cable Act provides that while cities may establish a prior franchising requirement some substantive franchise provisions are unenforceable[80] The Act also places significant procedural restrictions on the ability of municipalities to refuse franchise renewals and grants a right to judicial review[81] In the area of rate regulation, Congress similarly provided that municipalities have the competence to regulate rates, but reserved to the federal government the power to define when that authority may be exercised[82]

On the merits, there are a number of substantial policy issues arising from the fact that despite whatever natural monopoly characteristics they enjoy, "cable operators may not necessarily

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in Docket No FCC 85 648 102 F C C 2d 1179 at para 44 (1986) Teleprompter Corp Memorandum Opinion and Order 87 F C C 2d 531 para 21 (1981)

[78] DOJ Press Release *supra* note 72 at 3

[79] Senator Metzenbaum Chairman of the Antitrust Subcommittee of the Senate Committee on the Judiciary has indicated an interest in examining the issue of cable industry concentration and the Department's merger policies in cable television *See* COMMUNICATIONS DAILY Feb 23 1987 at 7

[80] *See supra* note 10 (discussion of franchising restrictions) Section 621(a) of the Cable Act 47 U S C § 541(a) (Supp III 1985) allows municipalities to grant 1 or more franchises Although Congress suggested that the Act's franchising provisions permit municipalities to determine the number of cable operators to be authorized to provide service in a particular geographic area HOUSE REPORT *supra* note 10 at 59 Congress specifically did not intend to revise the antitrust laws *Id* Indeed the Ninth Circuit has stated that these provisions violate the first amendment Preferred Communications, Inc v City of Los Angeles, 754 F 2d 1396 1411 n 11 (9th Cir 1985) *aff'd*, 476 U S 488 (1986)

[81] *See supra* note 10

[82] Cable Act § 623 47 U S C § 543 (Supp III 1985) In light of the growing number of consumer complaints regarding cable rate increases after rate deregulation became effective on January 1, 1987 there have been suggestions that Congress may step in and revise this balance *See Markey Warns Cable to Exercise New Rights Cautiously* COMMUNICATIONS DAILY Feb 25 1987, at 3

be forced by competitive pressures to return to consumers the benefit of efficiencies that result from consolidation "[83] It may not be correct to assume, for example, that regulatory and antitrust enforcement policy in cable should follow the traditional model for natural monopoly Even if cable television is a natural monopoly in *every* market, it could plausibly be argued that cable is nevertheless sufficiently different from such essential services as electricity, gas, and local telephone service that treatment as a utility is unwarranted Similarly, while cable's natural monopoly characteristics may give cable systems market power in a significant number of markets, regulation involves costs and burdens different from, and often greater than, antitrust enforcement It may therefore be justifiable to tolerate a greater degree of market power before imposing regulation than before using the antitrust laws to restrict mergers and acquisitions among cable systems [84]

The problem, though, is that these subtle policy issues have only rarely been raised and have never been decided The fallout of the FCC's virtually complete deregulation of cable rates, coupled with the Department's antitrust policy of nonenforcement, is that cable is treated like a utility for antitrust purposes but treated as a competitive industry for regulatory purposes Ironically, therefore, while a city can determine that a single cable firm will best serve its citizens, it is stripped of the ability to limit the welfare loss arising from monopoly pricing While a city can, according to the Department, create or sanction a monopoly in cable television, it cannot, according to the FCC, regulate that monopoly This policy conundrum means that neither federal nor local government has discretion to apply a compromise between the competitive and public utility models to cable television

From a federalism perspective as well, the FCC and the Department are acting at cross-purposes If municipalities are in the best position to determine the structure of local cable markets, they should also be in the best position to determine the level of regulation appropriate to that market In other words, if the federal government is going to defer to municipalities on cable antitrust issues, it should similarly defer on cable regulatory issues In terms of municipal authority to protect the health, safety, and welfare of consumers, if a city decides its police power justifies limiting cable to a single firm, for example, to avoid pole

[83] DOJ Press Release *supra* note 72 at 3
[84] *See* DOJ Comments *supra* note 64 at 15 n 25

attachment problems or the repeated inconvenience of underground cable construction, there is little apparent justification for precluding the city from regulating the firm to whom it awards the franchise

Since the Department has already applied its laissez-faire policy toward cable system consolidation for more than two years, it is unlikely that its current leadership will reconsider that policy in light of the FCC's preemption of municipal ratemaking authority However, there are a number of compelling reasons for reconsideration First, under the "state action" exemption to the antitrust laws,[85] municipalities may grant an exclusive franchise, or deny a franchise to a potentially competing system, only if state law has clearly articulated and affirmatively expressed a policy of displacing competition [86] Municipalities enjoy no inherent right to create a monopoly in any industry [87] The Department's deferral rule, however, applies regardless of applicability of the state action exemption This approach effectively produces a balkanization of the antitrust laws,[88] with their applicability to cable acquisitions depending fortuitously on the localities involved in any specific transaction

Second, the Department's approach is clearly inconsistent with its enforcement policies in most other industries For example, the Department can (and sometimes has) approved mergers

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[85] The state action exemption is a judicially created doctrine that finds its genesis in the Supreme Court s decision in Parker v Brown, 317 U S 341 (1943) With regard to application of the state action doctrine to municipalities *see* Community Communications Co v City of Boulder, 455 U S 40 (1982) City of Lafayette v Louisiana Power & Light Co 435 U S 389 (1978)

[86] *See e g* Town of Hallie v City of Eau Claire, 471 U S 34 (1985)

[87] Even if a city enjoys state action immunity moreover there is little reason to extend that protection to decisions on mergers Although one court has applied the state action doctrine to section 7 of the Clayton Act 15 U S C § 18 (1982 & Supp III 1985), *see* Cinc 42nd St Theatre Corp v Nederlander Org , Inc , 790 F 2d 1032 (2d Cir 1986) that court misapplied the doctrine Congress surely did not intend that Delaware for example should be able to immunize otherwise unlawful mergers between Fortune 500 firms from antitrust scrutiny Moreover whether or not municipal action for approval of a merger is exempt from antitrust liability, the merger itself may still violate the antitrust laws *Cf* City Communications Inc v City of Detroit 650 F Supp 1570 (E D Mich 1987) (even where state action doctrine immunizes city from antitrust liability for its award of exclusive cable franchise state action immunity does not extend to private defendants)

[88] *Cf* Brief for the United States as Amicus Curiae at 15 Town of Hallie v City of Eau Claire 471 U S 34 (1984) (No 82-1832) (What *City of Boulder* recognized was that the sheer number of municipalities and other state instrumentalities that may engage in anticompetitive activities creates a significantly greater risk to the Sherman Act s procompetitive values than that created by granting immunity to the states) For a contrasting view see Easterbrook, *Antitrust and the Economics of Federalism* 26 J L & ECON 23 (1983) Brennan *Local Government Action and Antitrust Policy An Economic Analysis* 12 FORDHAM URBAN L J 428 429 n 137 (1984)

and joint operating agreements between newspapers in the same city despite the opposition of municipal governments In other instances in which anticompetitive effects are localized, such as price-fixing among retailers and bid-rigging among contractors, the Department apparently does not even consider the views of local governments There is no indication, moreover, that the Department gives any weight to "federalism" principles in any other aspect of merger policy [89] Only in cable does the Department rely on "the preferences of citizens"[90] to determine whether competition or monopoly is the appropriate market structure Furthermore, in the largest and most visible of its recent enforcement actions, the Department litigated against and eventually dismantled the Bell System "despite the fairly clear-cut 'preferences of the citizens'"[91]

The *AT&T* [92] case well illustrates a final deficiency in the Department's cable competition policy If the issue is whether an industry is a natural monopoly in a given geographic market, the proper way to resolve that question is the marketplace [93] It has never been presumed that competition may be eliminated by merger even if the market is a natural monopoly Rather, the test for natural monopoly is the market itself If, in fact, competition is not sustainable, only one firm will survive the discipline of competition [94] Indeed, where the evidence is ambiguous, as in

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[89] Although the Department's Phoenix decision relied in part on the fact that municipalities may have the power to prevent consolidation a similar argument can be made with respect to most antitrust violations which generally contravene state antitrust statutes It would be surprising for the Department to decline to bring an antitrust lawsuit merely because a state government had the power to but did not act to prosecute the alleged violation

[90] *See supra* text accompanying note 73

[91] Owen *Cable Competition at Sufferance of Cities* Wall Street J May 9 1985, at 28 col 3

[92] United States v AT&T 552 F Supp 131 (D D C 1982) *aff'd sub nom* Maryland v United States 460 U S 1001 (1983)

[93] Thus in cable television monopolistic characteristics may lawfully arise only through an elimination bout *in* the market not by a City-run auction *for* the market Brief of Tele-Communications, Inc Time Incorporated and the New York Times Company as Amici Curiae at 30 City of Los Angeles v Preferred Communications Inc 476 U S 488 (1986) (No 85 390) (emphasis in original)

[94] The ABA Section of Antitrust Law has suggested that competition in a natural monopoly will by definition, be socially wasteful or futile and therefore that legislators and regulators should make the decision whether a market is a natural monopoly Regulatory Reform Report *supra* note 2, at 516 It is clear, however that the market conditions establishing natural monopoly arise only in the long run *Id* In the short run even if eventual monopoly is inevitable competition provides an important guarantee that the winner [of competition for the market] will be the most efficient and responsive competitor thus benefitting consumers during the period of competition and perhaps afterward as well Owen *Regulatory Developments in Cable Television Regulation* Regulatory Reform Industry Regulation Committee Newsletter 1 A B A SEC ANTITRUST L 5 (Dec 1985)

AT&T itself, the Department has not hesitated in the past to enforce the antitrust laws to maintain potentially competitive markets."[95]

This conclusion is reinforced by the courts' approach to antitrust law and cable competition. If cable's "natural monopoly characteristics" preempt antitrust, it would make little sense for the courts to have considered whether Boulder, Colorado violated the antitrust laws by granting an exclusive franchise,[96] whether a collusive agreement to award a cable franchise in Houston, Texas unreasonably restrained competition,[97] whether an incumbent franchisee in Jefferson City, Missouri monopolized the market by anticompetitive conduct during a refranchising battle,[98] or whether a merger of cable systems in Cobb County, Georgia substantially lessened competition.[99] No court has ruled that natural monopoly is a defense to an antitrust violation.[100] Rather, even *if* the market is a natural monopoly, attempts to limit competition to *become* the monopolist—whether in the franchising process or by means of merger or consolidation—are proscribed by the antitrust laws.[101] The final irony, of course, is that in cable television the fruit of franchising competition, the franchise agreement itself, is largely unenforceable under the Cable Act.[102] Since municipalities can no longer function effec-

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[95] AT&T's defense, for example, centered on its alleged efforts to preclude so-called "creamskimming" by long-distance competitors, a slightly more sophisticated version of a natural monopoly defense. *See* United States v. AT&T, 552 F. Supp. 131, 161-62 (D.D.C. 1982), *aff'd sub nom.* Maryland v. United States, 460 U.S. 1001 (1983).

[96] Community Communications Co. v. City of Boulder, 455 U.S. 40 (1982).

[97] Affiliated Capital Corp. v. City of Houston, 700 F.2d 226 (5th Cir. 1983), *aff'd*, 735 F.2d 1555 (5th Cir. 1984) (en banc), *cert. denied*, 106 S. Ct. 788 (1986).

[98] Central Telecommunications, Inc. v. TCI Cablevision, Inc., 610 F. Supp. 891 (W.D. Mo. 1985) (upholding $36 million verdict against TCI), *aff'd*, 800 F.2d 711 (8th Cir. 1986), *cert. denied*, 107 S. Ct. 1368 (1987). *See* H.R.M., Inc. v. Tele-Communications, Inc., 653 F. Supp. 645 (D. Colo. 1987) (alleging monopolization by one of two cable systems competing in Kearney, Nebraska).

[99] Cable Holdings of Georgia, Inc. v. Home Video, Inc., 572 F. Supp. 482 (N.D. Ga. 1983).

[100] Calls by architects of the "Chicago school" of antitrust for the creation of a "natural monopoly defense" in merger litigation have gone unheeded. *See* Posner, *supra* note 7, at 585-87.

[101] *E.g.*, Fishman v. Estate of Wirtz, 807 F.2d 520, 533, 535 (7th Cir. 1986); Affiliated Capital Corp. v. City of Houston, 700 F.2d at 234 ("[i]f there is to be no competition within a given territory, competition is only possible before the franchise is granted."); Omega Satellite Products Co. v. City of Indianapolis, 694 F.2d 119, 127 (7th Cir. 1982) ("[T]he antitrust laws protect competition not only in but for the market—that is, competition to be the firm to enjoy a natural monopoly."). *See also* TV Signal Co. of Aberdeen v. AT&T, 1981-1 Trade Cas. (CCH) ¶ 63,944, at 75,864 (D.S.D. 1981).

[102] *See, e.g.*, Tribune-United Cable of Montgomery County v. Montgomery County, 784 F.2d 1227, 1231 (4th Cir. 1986) (Cable Act creates a "federally protected right to modification of commercially impractical [franchise] agreements."). Even those opposing application of the traditional public utility model to cable have stressed that "the

tively as surrogate consumers, the central premise of the Department's Phoenix policy collapses

IV The Emperor's New Clothes

Two recent developments suggest that the sands of federal policy toward cable television may be shifting The first, familiar to industry observers, is the application of the first amendment to municipal franchising decisions The second, proceeding on a somewhat slower track, is the growing trend toward national and regional concentration among MSOs—sparked in part by the industry's aggressive pace of mergers and acquisitions following the Justice Department's approval of the Phoenix transaction [103]

A *Amendment 1 or Section 2?*

In *Preferred Communications, Inc v Los Angeles*,[104] a potential entrant challenged the municipality's auction-type franchising process Preferred alleged that Los Angeles' award of an exclusive cable franchise violated the first amendment [105] The city, predictably, replied that physical scarcity of pole attachment and conduit space, "economic scarcity" of the medium itself, and the disruptive effect of cable system construction justified restricting cable service to a single company [106] On appeal from the district court's dismissal of the complaint, the Ninth Circuit reversed

The Ninth Circuit held that none of these justifications sufficed to limit access by cable systems Since Preferred alleged that space was available on the poles, the court rejected that basis for excluding a competitor [107] With respect to "economic scarcity,"[108] the court ruled that even if natural monopoly provided "a basis for some degree of government regulation,"[109] it could

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opportunity of local government representing the subscribers to drive a hard bargain with the would be monopolist may be a viable alternative to conventional methods of regulation Posner *supra* note 7 at 562 *See* Easterbrook *supra* note 88 at 32 Under the Cable Act however the bargain is now considerably softer as a matter of law

[103] In 1986 340 cable system mergers and acquisitions involving more than six million subscribers were consummated Daniels & Associates a cable brokerage firm estimated that the volume of cable transactions nearly doubled from any previous year and equaled the total from 1980 through 1983 *See* COMMUNICATIONS DAILY Feb 19 1987 at 9 One of the largest transactions ever was TCI s $1 25 billion acquisition of United Artists Communications, an MSO serving 740 000 subscribers *See* Multichannel News July 21 1986 at 1

[104] 754 F 2d 1396 (9th Cir 1985) *aff d* 476 U S 488 (1986)

[105] *Id* at 1399

[106] *Id* at 1402

[107] *Id*

[108] *Id* at 1404

[109] *Id* at 1405

not justify the elimination of all competition, particularly where it was alleged that "competition for cable services is economically feasible '[110] Similarly, while the police power justifies some regulation of cable systems, the court held it cannot support the outright exclusion of firms from the market [111]

The Supreme Court's opinion in *Preferred* is ambiguous because of the case's procedural posture, the underlying facts were never litigated While confirming that cable television enjoys some modicum of first amendment protection, the Court affirmed and remanded for resolution of the factual issues [112] Although the Court declined to decide whether cable falls within the much-criticized *Red Lion* doctrine,[113] however, it seems apparent that absolute exclusion of cable entry likely violates the Constitution, *if there is space on the poles*

The irony is clear While the Department refuses to enforce the antitrust laws in cable television, either against municipalities or merging cable firms, the first amendment may mandate that competition be permitted—even where a city affirmatively sanctions a cable monopoly The Ninth Circuit's express rejection of natural monopoly as a justification for excluding potential entrants demonstrates, consistent with the lack of a "natural monopoly defense" to the antitrust laws, that the market should determine whether or not a monopoly is natural

In short, *Preferred* really should be viewed as an antitrust case in first amendment garb [114] Indeed, in some ways, it conflicts with first amendment principles, since the ability to restrict entry

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[110] *Id* at 1404-05

[111] *Id* at 1411

[112] City of Los Angeles v Preferred Communications Inc 476 U S 488 (1986)

[113] Red Lion Broadcasting Co v FCC 395 U S 367 (1969) In *Red Lion* the Supreme Court upheld the FCC's fairness doctrine on the ground that physical scarcity of the broadcast medium justified greater restrictions on broadcasters first amendment rights than other members of the press The viability of the *Red Lion* doctrine has recently been called into question *See* Meredith Corp v FCC No 85-1723 (D C Cir filed Jan 17 1987) Fairness Doctrine Obligations of Broadcast Licensees 102 F C C 2d 143 (1985)

[114] The Ninth Circuit did conclude that the state action antitrust exemption authorized the city to limit its franchise to a single firm Nonetheless the effect of *Preferred* is that under the first amendment, competitive principles override municipal authority even where state action provides immunity under the Sherman Act Indeed the court discussed the issue of cable as a natural monopoly ' *only* in the constitutional context *Preferred* 754 F 2d at 1404-05 As discussed above furthermore the critical issue is who decides whether competition should be permitted the courts using the first amendment have acted where the Department declined to act *See also* Group W Cable Inc v City of Santa Cruz, No C 84-7456-WWS (N D Cal Sept 9 1987) (permanent injuction issued against municipality based on first amendment) Pacific W Cable Co v City of Sacramento 798 F 2d 353 (9th Cir 1986) Tele-Communications of Key West Inc v United States 757 F 2d 1330 (D C Cir 1985) Carlson v Village of Union City 601 F Supp 801 (W D Mich 1985) Century Fed Inc v City of Palo Alto 579 F Supp 1553

depends primarily on the content involved, *i e*, what is transmitted over the cable It has never been seriously contended that a city or state may not exclude competition for local telephone service Thus, the only functional way to distinguish cable systems and telephone companies is that the latter provide two-way communication It is difficult to conclude, however, that the first amendment should turn on how wires are used to communicate

B *Concentration and Competition*

There has been a striking increase in concentration among MSOs in recent years This trend raises a variety of new regulatory and competitive issues, only some of which are addressed in the pending petition for FCC rulemaking to establish rules governing MSO concentration [115]

Identifying the manner in which MSOs compete presents one issue While it is clear that franchising competition has often been heated, it is not clear that, with most major franchises already awarded, refranchising competition will prove either substantial or effective As a matter of merger policy, therefore, it may be premature to impose quantitative or relative limits on MSO cable system holdings Nonetheless, concentration in cable raises other potentially significant competitive issues, both horizontal and vertical

As MSOs increase *regional* concentration of cable systems, cable is likely to become a stronger competitor in the television advertising market, able to offer advertisers the audience

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(N D Cal 1984) *See generally* Note *Access to Cable Natural Monopoly, and the First Amendment* 86 COLUM L REV 1063 (1986)

Interestingly the major MSOs now suggest that they support the use of first amendment principles to encourage direct competition among cable operators *See* Brief of Tele-Communications Inc Time Incorporated and the New York Times Company as Amicus Curiae at 27-28 City of Los Angeles v Preferred Communications, Inc, 476 U S 488 (1986) (No 85-390) (Even assuming that cable is usually a natural monopoly the First Amendment dictates that the choice of which company is to receive the monopoly in this form of communication must be made by competition in the marketplace of ideas—not be municipal officials) *Id* at 27-28 (Whatever the current technological limit to the number of systems may be it is well above four) *id* at 16 ('[T]he tendency toward monopoly if present at all may well be attributable more to governmental action than to any natural economic phenomenon) (citing Quincy Cable TV, Inc v FCC 768 F 2d 1434 1450 (D C Cir 1985) *cert denied*, 106 S Ct 2889 (1986))

[115] Petition for Rule Making Amendment of Part 76, Subpart J of the Commission s Rules and Regulations Relating to Multiple Ownership of Cable Television Systems, RM 5475 (Feb 21 1986) *See* I C FERRIS F LLOYD & T CASEY *supra* note 22, ¶ 9 23 at 9 53 *MPAA Leads Charge in Urging Limits on Cable Ownership* Multichannel News, July 28 1986 at 1 (Motion Picture Association of America supports MSO concentration limits) *cf* CATV Multiple Ownership 91 F C C 2d 46 (1982) (rejecting limits on MSO concentration)

volumes now generally possible only on broadcast television[116] Consequently, cable systems could gain an incentive, acting either unilaterally or through cooperative advertising "interconnects,"[117] to impede competition from broadcast stations for advertising, for example, by denying local stations carriage[118] *Preferred* suggests that there is room in the continuing first amendment dispute over the must-carry rules[119] for such competitive issues

Horizontal MSO concentration may also intensify competitive concerns arising in the acquisition of programming Although the trend may be pro-competitive, as any MSO market power would offset that enjoyed by the dwindling number of programming distributors, it is questionable whether cable programmers can exert significant economic pressure on cable operators If systems drop their services, satellite-delivered programmers will lose their most important outlet Indeed, coupled with vertical integration by MSOs (which itself seems on the rise), horizontal concentration could increase incentives for anticompetitive practices aimed at nonintegrated competitors[120] Several antitrust lawsuits arising out of the refusal by vertically integrated MSOs to supply programming to competing cable systems,[121] or to carry satellite-delivered services offered by competing programmers,[122] are pending

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116 *See* COMMUNICATIONS DAILY Feb 19 1987, at 3 (National Association of Broadcasters warns that [c]able poses potentially serious threat to broadcasters in local retail advertising)

117 Interconnects are technical or reciprocal arrangements among cable systems that provide advertisers access to all systems involved *See* C FERRIS F LLOYD & T CASEY *supra* note 22 ¶ 5 04(d) at 5-12

118 Wodlinger Broadcasting Co v MTV Networks Inc No H-85-5811 (S D Tex filed 1985) (UHF station with music video format alleges antitrust violation arising from denial of carriage and advertising access by vertically integrated MSO) *cf* Midland Telecasting Co v Midessa Television Co 617 F 2d 1141 (5th Cir) (reversing dismissal of antitrust claim arising from refusal of cable system to carry VHF station that competed with system s parent broadcasting companies) *cert denied* 449 U S 954 (1980)

119 *See* Quincy Cable TV, Inc v FCC, 768 F 2d 1434 (D C Cir 1985) *cert denied*, 106 S Ct 2889 (1986) Amendment of Part 76 of the Commission s Rules Concerning Carriage of Television Broadcast Signals by Cable Television Systems, 1 F C C Record 864 (1986) In partially resurrecting a modified version of its must-carry rules, which had been invalidated in *Quincy Cable* the FCC found that a competitive market may not lead cable operators to carry all of the television signals that can be received off-the-air in their communities [and that] satellite programmers' current primary means of access to viewers is through cable systems *Id* at 881 In early 1987 the FCC stayed the new modified must-carry rules *See* 3 FCC Rulemaking Rep (CCH) ¶ 23 112 (1987)

120 *See* United States v Columbia Pictures Indus Inc 507 F Supp 412, 424 (S D N Y 1980) Kahn *supra* note 7 at 24 Noam *supra* note 20 353

121 *E g* Nishimura v Dolan 599 F Supp 484 (E D N Y 1984) Mobile Cablevision v Group W Cable No 86-0043-H-S (S D Ala filed Jan 10 1986)

122 *E g* New York Citizens Comm on Cable TV v Manhattan Cable TV, Inc 651 F Supp 802 (S D N Y 1986) (denying motion to dismiss monopolization claim against

These issues cannot be dismissed as mere long-run concerns, but it appears they will not be addressed in the FCC's MSO concentration proceeding [123] That proceeding, however, has already produced at least one surprise The Department, in opposing regulatory restrictions on horizontal concentration, repeatedly emphasized the role of antitrust law in policing anticompetitive mergers [124] While the Department did not cite, let alone harmonize, its decision in the *Phoenix* case, one may wonder whether there has been a retrenchment Given the Department's failure to act on recent large MSO mergers, however, its reliance on antitrust enforcement exhibits a rather hollow ring

V THERE AND BACK AGAIN

Those without an understanding of cable television history may find that history repeated in policy issues likely to arise in the future A case in point is scrambling [125] While the headlines abound with the political battles between satellite dish retailers, cable operators, and cable programmers over scrambling,[126] a key competitive issue has not been resolved Indeed, if cable systems including vertically intergrated MSOs, control the retail distribution of satellite-delivered programming, then the definition of the product market applicable to cable[127]—the basic source of the conundrum in antitrust and regulatory policy—may make a practical difference

The antitrust concern is that, whether or not alternative distribution technologies are now "effective competition" for cable

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vertically integrated MSO arising out of refusal to carry unaffiliated pay cable services) For a discussion of a 1983 lawsuit regarding the refusal by Group W which at that time was a vertically integrated MSO operating a competing cable news service, to carry CNN see 2 C FERRIS F LLOYD & T CASEY *supra* note 22 ¶ 24 07[3] at 24-24

[123] *See supra* note 115 and accompanying text

[124] Comments of the United States Department of Justice In the Matter of Amendment of Part 76 at 2 7, 8 9 RM 5475 (F C C filed July 21, 1986) In a curious offhand remark the Department also opined that the proposed limits on MSO concentration might unnecessarily confuse the relationship between the antitrust laws and FCC regulations (for example by raising questions of primary or exclusive jurisdiction) that might actually weaken the antitrust laws ability to prevent anticompetitive acquisitions *Id* at 2

[125] Scrambling is the coding or encryption of satellite television signals so that receipt is possible only through purchase and use of specialized equipment *See* Cable Act § 605 47 U S C § 605 (Supp III 1985)

[126] *See e g* *Gore Seeks FTC Probe of Cable Program Marketing to Dish Users* COMMUNICATIONS DAILY Feb 24 1987 at 2, Ivey, *Angry Dish Owners Try to Fight Off Scrambled Signals* BUS WK Jan 13, 1986 at 120

[127] If and when these antitrust issues reach the courts [i]t is quite clear [that the issue of product market definition] will be heavily litigated [and] is likely to lead to difficult and potentially conflicting decisions 2 C FERRIS F LLOYD & T CASEY *supra* note 22 ¶ 24 09[2] at 24-25 to 24-26 I

systems, the industry appears determined to grant cable systems the exclusive right to "descramble" satellite-delivered programming For example, in 1985, NCTA proposed that a consortium limited to cable operators would market decoders to satellite earth station owners [128] Yet, while this approach remedies some fairly obvious antitrust concerns,[129] there is little reason to believe that vertically integrated MSOs will allow unaffiliated dish retailers or SMATV or MDS operators to distribute satellite programming also carried on owned-and-operated cable systems [130] A little strategic anticompetitive behavior, therefore, could go a long way to ensure that cable retains its inherent economic advantage as a multichannel, broadband distribution medium [131]

The Department has apparently continued its lengthy and well-publicized antitrust investigation into the distribution of satellite programming [132] While it appears that there may be no

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[128] *See Voting Problems Antitrust Experts Praise NCTA s Scrambling Plan* Multichannel News Aug 5 1985 at 3, col 1

[129] For example, earlier proposals included express provisions that would have prohibited cable systems from marketing descrambled satellite programming within the franchise areas of any other systems *Id*

[130] For a discussion of several antitrust cases involving the refusal of cable programmers to sell to SMATV operators see 2 C FERRIS F LLOYD & T CASEY *supra* note 22 § 24 09[4] at 24-30 For examples of cable operators efforts to preclude competition from satellite dish retailers SMATV operators and other potentially competitive technologies see e g Rollins Cablevue, Inc v Saienni Enter 633 F Supp 1315 (D Del 1986) Air Capital Cablevision Inc v Starlink Communications Group Inc 601 F Supp 1568 (D Kan 1985)

[131] *See A Cable Cartel?* FORBES, Feb 10 1986 at 82 N Y Times, Jan 13 1986 at A16 col 1

[132] *See e g Justice Continues Inquiry into Scrambling SMATV/MMDS Policies* Multichannel News Dec 22, 1986, at 1 Throughout 1986 and 1987 however the focus of scrambling issues appeared to be moving away from the Department s antitrust investigation and toward the regulatory and legislative arenas The FCC began its own inquiry into scrambling issues eventually reporting that markets are evolving [which will] likely prove efficient and workably competitive Scrambling of Satellite Television Signals and Access to Those Signals by Owners of Home Satellite Dish Antennas 2 F C C Record 1669 1671 (1987) There was also increased activity in Congress *See Senate Committee Blisters Cable Industry*, Multichannel News Aug 4 1986 at 6 In 1986 Senator Gore introduced a bill to require cable programmers to market to dish owners and to preclude discrimination against non-cable distributors of decryption technology S 2823 99th Cong 2d Sess (1986) Senator Gore argued that it does not take a year-long general study by [the] Justice Department or the FCC to realize that the distortions in this marketplace are severe and need immediate remedy We simply cannot wait forever for those agencies to study the problem to death 132 CONG REC S9 898 (daily ed July 30 1986) (statement of Sen Gore) This bill was defeated by a close 54-44 vote near the end of the 99th Congress *See* 132 *Cong Rec* S14 674 (daily ed Oct 2 1986) Opposition to the bill was based in part on the ground that it was premature because the cable industry's market power is being studied by the FCC and allegations of unlawful collusive conduct is under active investigation by the Justice Department 132 CONG REC S14 671 (daily ed Oct 2 1986) (remarks of Sen Wilson) Shortly after the FCC s 1987 report bills similar to Senator Gore s 1986 legislation were introduced into both houses of Congress *See* S 889 100th Cong 1st Sess (1987) H R 1885 100th Cong 1st Sess (1987) Senator Gore characterized the FCC s conclusions as cursory

easy answers to these issues under prevailing antitrust law—and little direct precedent in reported cases—scrambling could eventually become the Department's vehicle for limiting the reach of its *Phoenix* decision If *Phoenix* represents a judgment by the Department that antitrust essentially does not apply to cable television, then cable systems could squelch "intermodal" competition[133] from alternative delivery technologies with little restraint In that event, of course, the dispute about the product market will have proved irrelevant, even if the FCC's broad video programming market were correct, cable will have monopolized

Without access to the evidence, it is impossible to decipher the precise issues now being examined by the Department or assess the competitive reasonableness of restrictions involved in the various scrambling scenarios implemented since 1986 [134] This much appears self-evident, however Whether cable systems are subject to competition depends on the nature and number of alternative programming sources available in the market in question [135] If anticompetitive means are used to exclude some of that programming, serious antitrust issues are presented Even if cable is a natural monopoly, therefore, it must abide by the antitrust laws in its relations with competitors—at least some of them, some of the time

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and ideologically colored *Satellite Fair Marketing Bills Introduced in House Senate* Multichannel News Apr 6 1987 at 38 col 2 In July 1987 the Department suggested that its investigation into scrambling was continuing but offered little hope of quickly reaching a definitive conclusion *See infra* note 134

[133] This term refers to competition among different modes of delivering goods or services *e g* between cable systems and alternative delivery technologies such as SMATV *See* Scrambling of Satellite TV Signals Notice of Inquiry 104 F C C 2d 1444 para 2 (1986)

[134] In July 1987 the Department announced that its scrambling investigation had not of date uncovered any significant evidence of collusion among cable programmers or cable operators *Hearings Before the Subcomm on Telecommunications and Finance of the House Comm on Energy and Commerce* 100th Cong 1st Sess 2-3 (1987) (statement of Charles F Rule Acting Assistant Attorney General) The Department s investigation into restrictions imposed on the distribution of scrambled programming which is typically limited only to cable system operators apparently continues In the mean time at least one antitrust suit has already been brought by those involved in the home earth station market alleging that cable programmers have conspired to restrain competition from third-party packagers of satellite programming Personal Preference Video v Home Box Office Inc No CA-40-86-235-K (N D Tex filed Mar 25 1986)

[135] *See* HOUSE REPORT *supra* note 10 at 66 (effective competition determined by consider[ing] the number and nature of services provided [by the cable system] compared with the number and nature of services available from alternative sources and if so at what price)

Attachment No 3

Vertical Integration

The business behind the boom in cable programing

The setting is the Denver office of the chief executive of a major MSO On the other side of the desk is some one with a "great idea" for a new cable programing service

Programer It's a goldmine

CEO Mmmmm

Programer Well, we ll give operators an equity interest

CEO Mmmmm.

Programer OK, we'll give you 51% ownership, but not a dime more

CEO Mmmmm

Programer OK OK, you can have 80%, but I've got to have 20% to meet payroll

An exaggeration? Yes But in the past 18 months cable operator ownership and equity participation—the foot soldiers of vertical integration—have rapidly become the quid pro quo for launching new services

There are a number of reasons why this method of financing/distribution has come into vogue Cable operators see equity participation as a way to insure that services they feel their subscribers want will see the light of day It gives cable operators greater or in some cases total control over the service As industry proponents call for cable-exclusive programing to differentiate themselves owning programing services takes on more allure For many years and to a lesser extent today the cable industry has been criticized for relying on warmed over network or syndication reruns Flush with cash from the completion of most system construction and freed from local rate regulation, cable operators have the money to plow back into programing And they are using some of that money to take equity stakes in programing services

But although cable operators look at equity as a way to acquire a wider range of programing and much that otherwise might not be produced critics see the same development as an attempt by cable operators to hoard product and an example of an insensitivity to exclusivity arrangements that have helped cable prosper

Programers who have tried to launch services in the past 18 months have found the shelf space dwindling Channel capacity is as tight today on cable systems as it was in the early 80 s Although the situation is expected to ease somewhat by the early 1990 s, as the last of the major urban builds are finished and system upgrades continue cable operators are wondering how many more services can be added since in the end consumers wind up paying for them

Today s capacity crunch which threatens to postpone the launch of the one of the industry s most solidly backed services Turner Broadcasting System s Turner Network Television is causing potential programers to offer equity stakes to operators to insure carriage Most of the equity ventures that have launched in the last year and a half have a telemarketing feature such as the Travel Channel The Fashion Channel and the QVC Network But other services have launched although on a much lower scale without equity offerings the Consumer Discount Network and Movietime for example You TV and Teleworld are also on the drawing boards for launch next year but neither came out of the blocks with equity participation ast part of its company structure

An equity deal is wonderful for initial distribution and it secures a lot of different fronts says Sheri Herman vice president sale and marketing Fashion Channel which launched with 65 equity cable operator partners But work still has to be done on a day to-day basis to make sure it s a working partnership If you don t have that the best equity deal in the world won t matter

David Meister Financial News Network director has launched services with and without equity In reality what you have no matter what the piece of paper between the two entities is an inherent partnership in the promotion of a cable programing service to the consumer says Meister In that process a deal is going be made whether you call it equity revenue sharing affiliate fee commission or whatever If it isn t a reasonable and fair deal the whole thing breaks down

Cable operators although coming from a different perspective also find that the equity-carriage element is a very important part but that aspect alone won t carry a service Still, some operators are more bullish than others when it comes to ownership or equity participation Bob Redella vice president programing and investments for Cox Cable lists what s important for getting a new service off the ground All the pieces really have to fit The service has to be quality It has to have a continuous flow of programing It has to have good management It has to have the necessary finances and finally it has to have carriage Cox has taken a strong position in program service ownership through the Discovery Channel Home Premiere Television and its own home shopping service America s Shopping Club But

Financial News Network s Meister

Fashion Channel s Herman

ATC's Dressler

the key question in launching a new service said Redella whether equity or ownership stakes are involved is Is the programing of quality value for the consumer?

Taking a bit more cautious approach is American Television & Communications the second largest MSO We are not out looking for equity positions in cable services said Fred Dressler vice president of programing We under stand why people are offering equity but it s our position that we'd rather make decisions on the value of the product and not the value of the invest ment

While we're on the subject

An extended discussion on the approaches of various MSO s to owner ship in program services and an examination into why programers offer equity in order to gain distribution continues on page 66 A list of the principal regional sports programing services many owned by cable MSO s appears on page 67

Who owns what with whom in cable networking

Basic services

Network	Subscribers	Ownership
ESPN	44 300	Capital Cities/ABC (80%) RJR Nabisco (20%)
WTBS	41 642	Turner Broadcasting (Ted Turner 65% Time Inc [ATC] 11 5% **TCI** 10 1% **UA** 4 8% **United** 3 2% **Warner** 1 8%)
CNN	41 642	Turner Broadcasting (Ted Turner 65% Time Inc [ATC] 11 5% **TCI** 10 1% **UA** 4 8% **United** 3 2% **Warner** 1 8%)
USA	39 000	MCA (50%) Paramount (50%)
MTV	37 100	MTV Networks Inc (Viacom)
Nashville	36 000	Gaylord Broadcasting
CBN	35 834	Christian Broadcasting Network
Nickelodeon	35 800	MTV Networks Inc (Viacom)
Lifetime	32,300	CC/ABC (33%) **Viacom** (33%) **Hearst** (33%)
Weather Chan.	31 053	Landmark Communications (for mer parent of TeleCable)
Nick at Nite	31 000	MTV Networks Inc (Viacom)
Headline News	28 352	Turner Broadcasting (Ted Turner 65% Time Inc [ATC] 11 5% **TCI** 10 1% **UA** 4 8% **United** 3 2% **Warner** 1 8%)
FNN	27 000	Infotech (20%) Dr Earle Brian (15%)
A&E	27 000	CC/ABC (33%) NBC (33%) **Hearst** (33%)
Discovery	25,600	**TCI** (14%), **United** (14%) **Cox** (14%) **Group W** (14%) **New-house** (14%) management, New York Life Co Allen & Co (30%)
C-SPAN	23 000	**Cable operator supported**
VH-1	22 900	MTV Networks Inc (Viacom)
WGN	22,481	Tribune Broadcasting
Score	19 800	Infotech (20%) Dr Earle Brian (15%)
CVN	19 000	COMB Co (50%) **18 cable oper ators** (50%)
BET	15 000	Bob Johnson (51%) BET presi-dent, **TCI** (16%) **HBO** (16%) **Taft** (16%)
HSN I	13 500	Home Shopping Networks Inc.
C-SPAN II	12,500	**Cable operator supported**
Tempo TV	12,500	**TCI** (pending owner)
Telshop	11 000	Infotech (20%) Dr Earle Brian (15%)
QVC Network	10 747	QVC Network (65%) **Comcast** (14%) **cable operators** (21%)
Inspirational	10 700	PTL Club
Learning Chan.	10 300	Infotech (40%) Appalachian Com-munity Service Network (40%) of ficers and employes (20%)
WWOR	10 100	MCA
Silent Network	10 100	Silent Network Inc
Video Mall Net.	10 000	Video Shopping Mall (Goodway Marketing 80%)
Trinity	7 200	Trinity Broadcasting Network (nonprofit)
Eternal Word TV	7 100	Eternal Word Television (nonprof it)
Fashion Channel	7 000	Charlie Gee (32%) **65 cable op-erators** (25%) **TCI** (10 5%) **United** (10 5%)
Country Music	6 700	Jim Guercio (principal owner)
Acts	6 000	Southern Baptist Convention
Travel Channel	5 700	TWA Marketing (100%) after equi ty offering TWAM will hold 63% **cable operators** 37%
HSN II	4 200	Home Shopping Networks Inc
Movietime	3 200	Employes (30%) Mabon Nugent & Co SRK Management Loeb Partners and Hallmark (70%)
Shop TV	2,500	JC Penney (63%) STN (37%)
WPIX	2 471	Tribune Broadcasting
Hit Video USA	2 100	Wodlinger Broadcasting
KTVT	1 891	Gaylord Broadcasting
Nostalgia	1 400	**Cooke Cablevision** (9%) **Tele-Cable** subsidiary has small per centage largest single owners
Liberty	1 049	Liberty Broadcasting Network (nonprofit)
Consum. Disc. II	1 000	Entertainment Marketing Inc
Sky Merchant	1 000	Jones Int l (parent of **Jones Inter cable**)
America's Shop.	1 000	**Cox Cable**
Galavision	900	Univisa
Gospel Music Net.	844	GMN Ltd
Motivation Net.	600	Rock Christian Network (nonprofit)
CDN I	526	Entertainment Marketing

Pay services

Network	*Subscribers*	*Ownership*
HBO	15 000	**Time Inc**
AMC	7 000	Rainbow Program Enterprises **(Cablevision Systems)** 50% **TCI** 50%
Showtime	5 300	**Viacom**
Cinemax	4 100	**Time Inc.**
Disney	3 175	Walt Disney Co
Movie Channel	3 000	**Viacom**
Playboy	520	Playboy Enterprises
Bravo	500	RPE **(Cablevision Systems)**
Festival	30	**Time Inc**

*Estimate Showtime does not breakout figures for Showtime/The Movie Channel

Pay per view services

View Choice I,II	4 000	**Viacom**
Request TV	2 500	**Daniels, United Cable, Centel, Heritage, American,** major motion picture studios
Home Premiere	2 300	**ATC Cox, TeleCable, Continental and Newhouse 20%** each
Cable Video Store	40	General Instrument

Bold face in right-hand column indicates cable operator ownership or ownership by company with cable systems in separate subsidiary

*CVN—The ownership by **18 cable operators—American ATC Adam Corp., Cablevision Colony Continental, Cooke Daniels & Associates Heritage Newhouse Rogers Sammons TCI Times Mirror, United Artists United Viacom Warner**—is based on percentage of subscribers committed to service

Telshop—FNN is offering equity to **cable operators** (500 000 shares) FNN will retain two million shares

QVC Network—It is presenting owned by the public (65%) **Comcast** (14%) and **cable operators** (21%) When cable operators exercise warrants on 483 000 shares of preferred stock, redeemable for 10 shares of common stock, another 4 83 million shares will be added to the approximately 10 million shares outstanding At that point, cable operators would own approximately 8 5 million shares of the 15 million shares outstanding or 56% of the service The largest in that group would be **TCI** (2 150 000)

Fashion Channel—Among the larger cable operators with an equity stake are **Adelphia American, ATC Barden Bresnan Cablevision Industries Centel Century Colony Commonwealth Cablesystems Continental Cooke Cox, Daniels Enstar First Carolina Harron Hauser, Heritage Lenfest, Maclean Hunter Marcus Media General, Newhouse, Omega Post Newsweek, Prestige Sammons Scripps Howard, Simmons Susquehanna Sutton Capital Taft, TeleCable TCI Times Mirror Triax, UA, United United Video Cablevision Viacom** and **Warner**

** **Travel Channel—The final equity offering is to be placed by Dec 1 whereby TWA Marketing will retain 6 million shares and **cable operators** will be offered 3 5 million

****Shop TV—It has equity commitments from **30 MSO s** representing 3 3 million subscribers MSO s will receive 1% equity in the service for each million homes they commit to Cable operators who have major stakes in other shopping programs such as TCI United and Comcast, are not a part of Shop Among the MSO s whose systems are carrying Shop TV are Cablevision Systems Rogers Continental and Warner

TVRO's win round one on regulation

Commerce passes Gore-Ford bill, major fight expected on floor, it permits third parties to distribute cable program services to dish owners

The home satellite dish industry scored an initial victory last week when the Senate Commerce Committee adopted legislation (S 889) to regulate the TVRO marketplace Still final Senate passage is not a given indeed the battle is apt to intensify as it heads for a final floor vote Proponents are hoping to see it move before Congress adjourns and are already laying the groundwork for House consideration

Despite Commerce s action (it was approved by voice vote) there was some dissention The Communications Subcommittee chairman Daniel Inouye (D-Hawaii) thinks the measure is wrong headed and promises to fight it on the floor Inouye could be joined by Bob Packwood of Oregon the ranking Republican on the subcommittee who although absent from the debate (he was a participant in the White House-congressional budget summit) is known to oppose the bill as it was reported from committee Ted Stevens (R-Alaska) also has problems with it

S 889 would mandate that cable programers permit any qualified third party—inside and outside the cable industry—to distribute their services to dish owners (To assuage some concerns this provision was modified to allow reasonable programer judgments to be made in qualifying distributors) Proponents of the bill believe competition among multiple third party distributors would keep prices of programing low enough to satisfy dish owners and bolster the sagging home satellite industry by making dish ownership more attractive to consumers

Even those who favor S 889—Senators Pete Wilson (R-Calif) and Larry Pressler (R S D) for example—indicated they ll seek further refinements Senator John Kerry (D-Mass) expressed doubts about the need for such a bill and according to staff may offer some amendments A lot of work has to be done It s not over said one Senate aide

The controversial measure pits cable against the home satellite industry and has been the subject of a massive grass roots campaign by dish owners dealers and manufacturers for several years they failed by a vote of 55 to 45 to pass a TVRO bill in the Senate last year But this time proponents feel the numbers are on their side This is far from over but we re really on the right track said Fred Finn president of the Home Satellite Television Association The Satellite Broadcasting & Communications Association applauded the committee s actions and is hopeful the momentum will carry over to the House side said President Chuck Hewitt

Senators Al Gore (D-Tenn) and Wendell Ford (D-Ky) the legislation s principal sponsors (along with Dale Bumpers [D-Ark]) were equally pleased Following the vote Gore told reporters he is confident the measure will receive full Senate approval I am very pleased with where we are today said Ford who added those win them all s [an obvious reference to cable s numerous legislative and regulatory victories] are going to lose one

Cable was not viewing the committee s action as a terminal blow It was a case of the opponents choosing not to have the fight in committee but on the floor said National Cable Television Association President Jim Mooney Nor does Mooney think the bill will be enacted because he said it is fundamentally flawed It is a solution in search of a problem and we will continue to oppose it

Some MSOs pre-empting FNN's shopping service

By RICHARD TEDESCO
Staff reporter

NEW YORK—By adding six hours of home shopping to its daily schedule Financial News Network has sparked dissatisfaction among some multiple system operators carrying the cable TV service

Some operators, in fact, are pre-empting the home shopping segment, which is called TelShop

"FNN is a fine financial service," says Nimrod Kovacs, vice president of programing and marketing for United Cable Television which is among the MSOs refusing to carry TelShop "but we don t carry FNN for shopping services."

Several MSOs affiliated with FNN complain that they weren't officially notified before the TelShop home shopping service was dropped into the midnight-to-6 a m time (ET) slot on the FNN schedule in early August FNN denies the allegation

TelShop faces competition from the already established Home Shopping Network and from the Cable Value Network.

Several MSOs, including United Cable, have equity positions in the latter venture and aren t willing to carry the rival TelShop service

As Mr Kovacs sums up, "We don t want to bombard the subscribers with home shopping services. (And) we want to support the services where we have an equity interest."

Other MSOs that are partners in the CVN venture include Tele-Communications Inc American Television and Communications Corp , Daniels & Associates, Rogers Cablesystems and Warner Cable Communications.

Continental Cablevision one of the big players not participating in CVN has also remained cool to TelShop

"We re discussing it with them " says Robert Stengel, Continental's vice president of programing "and we ve told them we're not pleased with the way they went about it, in changing the programing that way "

Adds Patrick Mellon, director of programing for Telecable Corp "To offer cherry-picked or part-time services for the subscriber would confuse them and cannibalize the services."

Despite the seeming obstacles to its plunge into home shopping FNN executives voice optimism about TelShop and say they ve heard no MSO complaints

Arnold Rosenthal, FNN s senior vice president of affiliates and marketing says the TelShop universe is big enough to handle the new home shopping service

"There s enough profit for anybody to prosper with 10 million homes," Mr Rosenthal says. "Our systems are the big systems."

Mr Rosenthal says MSOs carrying TelShop on at least some of their systems include Storer Communications, Cox Cable, United Artists Cablevision and Jones Intercable

Meanwhile, FNN is moving even deeper into home shopping The cable service announced last week that it will seek channel space for a 24-hour TelShop operation and will deliver it via its own transponder

The six hours of TelShop programing will continue to run as scheduled as part of regular FNN programing #

Attachment No 4

WEEKLY **Television Digest**

A TELEVISION DIGEST WHITE PAPER

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Full Text

Cable Report to the President

By the Cabinet Committee on Cable Communications

Issued Jan 16 1974 Members of Committee Clay T Whitehead Director of the Office of Telecommunications Policy chairman Leonard Garment Herbert G Klein Presidential Advisers Peter G Peterson Secretary of Commerce Elliot L Richardson Secretary of Health Education & Welfare George Romney Secretary of Housing & Urban Development

OFFICE OF TELECOMMUNICATIONS POLICY

EXECUTIVE OFFICE OF THE PRESIDENT
WASHINGTON, D C 20504

January 14 1974

DIRECTOR

The President
The White House
Washington D C

Dear Mr President

I am pleased to submit to you the report of the Cabinet Committee on Cable Communications As you requested the Committee has developed proposals for a new policy that will allow cable to be integrated into our nation s communications media in an orderly way that is consistent with the principle of the free flow of information so deeply imbedded in our national traditions

During the Committee s deliberations we heard the views of a wide range of industry groups and nonprofit and public interest organizations and we also examined the extensive research on cable communications On the basis of the views we heard the research we examined and our own study and deliberations the Committee has recommended a comprehensive new national policy for cable communications

Our goal was to insure that cable would develop as a communications medium open and available to all Americans free of private or governmental barriers to its use Under such a policy we believe that cable can be a communications medium that allows the great creativity of the American people to express itself

Sincerely

Clay T Whitehead

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INTRODUCTION

"The Committee did not attempt to assign a role for cable or choose a place for it in the future of communications in this country, nor have we treated it as a modern day Rosetta stone capable of unravelling the complex problems facing this society. We have simply concluded that cable has much to offer, and it should be given an opportunity to prove its worth to the American people in the marketplace of goods and services and in the marketplace of ideas."

On June 27, 1971, the President announced the formation of a Special Committee[1] to develop proposals for a comprehensive national policy on cable communications. In creating the Committee, the President noted that communications have a profound impact on the social fabric of our nation and that it was time to come to grips with cable communications in order to avoid the social, economic, and regulatory instability that this technological innovation could cause.

Early in the course of its work, the Committee established an interagency working group which held many formal meetings and was in regular contact on an informal basis. In addition to the departments and agencies represented on the Committee, the working group coordinated its activities with other interested governmental organizations, including the Department of Justice and the Federal Communications Commission (FCC).

The Committee also heard the views of industry groups as well as a wide variety of nonprofit and public interest organizations. We also examined the many studies, reports, and research analyses regarding cable that have been prepared by a wide range of organizations.

After reviewing the current range of views and research, as well as conducting its own studies, the Committee has set out its conclusions and recommendations on the major policy issues regarding cable. These recommendations do not represent a master plan to create a fully operable nationwide cable system, but rather a broad policy approach for integrating a new technology into our country's mass communications media.

In recommending the policies and types of regulation to govern cable during the foreseeable future, we attempted to forecast only about ten years into the future; we were concerned both literally and figuratively with "1984." Prediction is a perilous task in the rapidly changing communications field, and the chilling vision of "1984" can never be far from any group studying a new mass communications medium for an advanced technological society. We would rightly be held derelict in our duties if we took no steps to avoid the clear present and future dangers of government control of communications technology which have been foreshadowed in the literary imagination.

The Committee has examined the growth of cable communications and the governmental response to it, and we have concluded that a new policy is needed (Chapter I). At the heart of the Committee's recommendations is a proposed policy that would separate control of the cable medium from control of the messages on it. The goal of this policy is to assure the development of cable as a communications medium open to all, free of both excessive concentrations of private power and undue government control (Chapter II). Our specific recommendations (Chapter III) flow from this basic policy proposal; their thrust is that neither the local monopoly power of each cable system nor the government regulatory power necessary to prevent abuse of that private power should be extended to the programs or other content of cable's channels.

The Committee has concluded that programming, advertising, and other information and services on cable channels can be allowed to develop on a free and competitive basis, with no more regulatory power exercised over the content of this communications medium than is exercised over the print or film media. Of course, some safeguards are needed for cable, as for other media, to protect individual privacy and prevent the unwanted intrusion into the home of offensive material.

The Committee recognized that many of our policy recommendations should not be implemented immediately (Chapter IV). These policies are best applied to an industry that is more developed and mature than today's cable television industry. There is, however, a need for broad agreement now on a long range national policy for cable. Without such a consensus, it would be difficult to take the steps necessary to move from current cable policies to the future policies that we recommend. Consequently, the Committee has recommended a transition period in which a new cable policy would evolve, and we have specified transition policies and procedures to assure that there would be a reasonably advanced and mature cable industry in existence when the long term policies take effect.

Finally, we have proposed a Federally supported program to demonstrate innovative public service uses of cable technology and to identify more precisely the technical and legal safeguards necessary to protect personal privacy in the use of cable (Chapter V). Some of the Committee members, however, were not in favor of this proposal. They expressed misgivings regarding both the need for such a demonstration program and the desirability of the Federal Government supporting an endeavor that they felt should best be left to private industry and local governments. While their concerns were shared in varying degrees by the entire Committee, a majority of the members concluded that, on balance, such a program would be appropriate as long as it stressed the preeminent roles of private industry and local governments and minimized ongoing Federal involvement.

The report concludes with a summary of the Committee's major long range policy recommendations and outlines the principal rights, obligations, and prohibitions created by such policies as they affect cable operators, cable channel users, existing communications industries, and various levels of government.

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[1] The Committee was composed of Peter G. Peterson, Secretary of Commerce, who succeeded Maurice H. Stans; Elliot L. Richardson, Secretary of Health, Education and Welfare; George Romney, Secretary of Housing and Urban Development; the Presidential advisers Herbert G. Klein, Leonard Garment, and Robert H. Finch. Clay T. Whitehead, Director of the Office of Telecommunications Policy, served as Chairman of the Committee, and his Office conducted the Committee's staff work.

CHAPTER I

THE DEVELOPMENT OF CABLE COMMUNICATIONS AND THE NEED FOR A NEW POLICY

"Cable offers countless Americans a chance to speak for themselves and among themselves in their own way, and a chance to share with one another their experiences, their opinions, their frustrations, and their hopes "

There have been many names associated with the subject matter of this report — Cable TV CATV broadband distribution networks coaxial communications and others The names reflect the multi-channel distribution capacity of coaxial cable technology and the services such technology makes possible Recognizing that any name chosen will be awkward or incomplete until it finds its way into general usage we have chosen for our report the most simple and most encompassing if not the most descriptive name cable

Coaxial cable however is only one type of broadband communications technology Others such as multi-channel microwave may become available soon while still others such as fiber optics and laser communications are further down the road However the substance of this report is applicable to the electronic distribution functions of such technologies rather than to coaxial cable alone We believe that our policies are sufficiently broad and flexible to accommodate developments in the emerging communications technologies The policies are by design not overly sensitive to the technology employed since the potential for abusive monopoly control of multi channel distribution systems are inherent in the technologies that we foresee being used for mass communications purposes

In attempting to create a policy for cable and other multi-channel distribution systems the Committee found that several technical and economic facts provided an indication of the potential opportunities and risks presented by their future development

Cable has the technical potential to become a communications medium of abundant capacity with an almost limitless number of channels capable of carrying virtually any kind of communications [1] Cable can distribute information to all households schools and places of business in an area or it can route it to specific locations upon electronic request It can offer a two-way capability allowing users to signal their wishes back up the cable and thus select particular programming or other information or order goods and services from among those offered

Economically two factors are relevant First the cost of providing a cable channel is relatively low and is likely to decrease as improving technology expands the number of usable channels and lowers the cost of electronic equipment the customer may use in conjunction with cable Thus the cost of communications capacity is likely to be a small component of the overall cost of producing and distributing television programming or of many other information services that might be offered over cable Second the apparent economies of scale involved as the number of channels and customers increases on a cable system mean that in any particular neighborhood or community only one cable system is likely to be viable and efficient, thus cable will be a natural monopoly in each locality

The remainder of this Chapter is devoted to a review of cable development and regulation to the present and an examination of the need for a new public policy regarding cable communications

The Growth of Cable

The first cable systems were simply community antenna systems (CATV) built in the late 1940 s to bring better television reception to isolated communities in mountainous parts of Pennsylvania and Oregon In these early CATV systems for a monthly fee customers homes would be linked by coaxial cable to a tall antenna which could receive signals from television broadcast stations

The first cable operators were usually local businessmen who encountered little regulation The FCC chose to exercise no authority over cable and most state governments took little notice of it Local governments became the regulators during cable s first decade largely because CATV operators needed permission to use public property and rights of way to lay their cables The nascent television broadcast industry also paid little attention to cable systems aside from vaguely endorsing them as a means of extending and increasing the size of their viewing audience

Despite the limited number of channels CATV systems could transmit this service spread rapidly throughout many small towns in this country In 1952 there were some 70 cable systems with 14 000 customers while 10 years later there were an estimated 800 systems and 850 000 customers

The decade of the 1960 s was a period of even greater growth for cable New technology increased the potential channel capacity of cable systems to 20 or more channels by the end of the decade A number of cable systems were not only providing improved reception of nearby broadcast stations but were also importing additional broadcast signals via microwave links from television stations in distant cities Dozens of systems also began to offer some form of locally originated programming often by transmitting pictures of news service or stock market ticker tape machines time and weather information and local advertisements

Now cable is no longer simply CATV It is no longer simply a conduit for television distribution to the home And it is no longer a cottage industry From its origins as a predominately rural and small town industry cable is now beginning to come to some larger cities It has grown to an industry composed of over 3000 systems in 1973 connecting almost 8 million households and continuing to grow at a rate of more than ten per cent per year

The attitudes of the investment community toward cable have fluctuated widely in recent years Currently cable is facing a slow-down in the rate of investment flowing to construction of new systems in major cities in part due to tight money markets and in part to investor disenchantment in reaction to over-optimistic views of cable profitability and growth

The actual prospects for cable growth however have not fluctuated appreciably In fact research and development are

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[1] In this report a "channel" means the communications capacity for the equivalent of one standard television signal (6 MHz) This communications capacity may be used whole or sub-divided for distributing audio data single frame facsimile and other types of information, as well as a television signal Thus several "channels" of various kinds of communications might be distributed over one equivalent television channel

producing lower cost distribution methods and equipment for specialized home use of cable programming and other information services. It is reasonable to expect that cable's recent growth trends will continue or even accelerate.

Thus, cable is on the verge of becoming a new medium of communications in its own right, a vehicle for a wide variety of new services, and big business.

Cable Regulation and the Need for a New Policy

The change in cable technology and in the economic and social importance of cable should have been accompanied by changes in the public policy that govern its regulation. Yet the regulators' perception of the cable medium has lagged far behind its evolving reality.

Federal regulation of cable is presently based upon the Communications Act of 1934, which deals with technologies that can accommodate only a limited number of signals. Lacking Congressional guidance and uncertain of its authority, the FCC at first denied that it had jurisdiction over cable. Through the late 1950's and early 1960's the Commission maintained this position, but in 1959 and 1966 it sought legislation expressly conferring such jurisdiction. During this same period the Commission gradually moved to regulate cable indirectly by exercising its unquestioned authority over the other communications services that cable was using. The FCC began by placing restrictions on cable systems that were served by the microwave facilities of telephone companies and other communication common carriers. By 1966 the FCC had asserted broad regulatory authority over all cable systems, principally with respect to retransmission of television broadcast signals, and in effect froze cable growth in the nation's top 100 television markets. In 1968 the Supreme Court upheld the FCC's action as "reasonably ancillary" to the Commission's power to regulate television broadcasting.[2]

The FCC extended its jurisdiction over cable in March 1972 when it issued rules that dealt not only with the retransmission of television broadcast signals but also governed access to and use of nonbroadcast cable channels. At the same time the FCC established technical standards and divided regulatory jurisdiction between the Federal and local levels of government. Cable regulation under the FCC's current rules is discussed in the Appendix to this report.

The legal basis for the FCC's broadening of its authority over cable beyond retransmission of broadcast signals was narrowly upheld by the Supreme Court in June 1972 in a case challenging the FCC's authority to require cable operators to originate programs. The deciding vote in the 5-4 decision was cast by Chief Justice Burger who stated in his concurring opinion that:

> Candor requires acknowledgment ... that the Commission's position strains the outer limits of even the open-ended and pervasive jurisdiction that has evolved by decisions of the Commission and the courts.

The Chief Justice added:

> The almost explosive development of CATV suggests the need of a comprehensive reexamination of the statutory scheme as it relates to this new development, so that the basic policies are considered by Congress and not left entirely to the Commission and the courts.[3]

Presumably the FCC could continue this process of step-by-step rulemaking for cable under court interpretations of its existing authority but, as Chief Justice Burger noted, the jurisdiction of the FCC to regulate cable derives from a very limited foundation in the Communications Act of 1934, which created the national policy for broadcasting's use of the public airwaves. That policy was designed for a scarcity of outlets, but cable needs a policy designed for a communications medium of abundance and diversity.

If we do not create a new public policy for cable, it seems clear that cable will continue to develop and be regulated in the policy mold created for broadcasting. To some extent this choice already is being made by the FCC, almost by default, since neither the Congress nor the Executive Branch has devised an alternative policy. In the absence of an alternative policy view, cable is regarded simply as an extension of, and a supplement to, the broadcast television industry. It is treated as a secondary service, albeit one that could engulf the primary broadcast service if cable's many channels are used to their full capacity. The perception of cable's multi-channel capacity as a threat to broadcasting could retard cable growth and even limit full use of all its capacity in order to protect broadcasting's financial viability.

But cable is not merely an extension or improvement of broadcast television. It has the potential to become an important and entirely new communications medium, open and available to all. The Committee has concluded, however, that cable may never become what it can become if it continues to be constrained by the policy of the Communications Act.

The Need for Federal Action

The new public policy that is needed for cable communications must be created through a conscious and deliberate effort which will anticipate both the risks and opportunities of cable development.

We are approaching what has been characterized as a "post-industrial" society in which knowledge and information will be major factors in economic enterprise as well as in personal growth and satisfaction. In the past the expansion and application of any new technology was often encouraged without particular concern for its future impact. Many Americans have accepted technological change almost as a good in itself. While our enthusiasm for technological change has been almost without bounds, in earlier times there was more room to compensate for error. If somehow technology went awry in one place or at one time, correctives could be applied in a different place or time.

But the era of haphazard technological development is drawing to a close. We can no longer permit technological innovation to "just happen" and then attempt to "regulate away" the adverse effects. This is especially true of a communications technology such as cable, which involves the delivery and exchange of knowledge and information. Because we have a legal and social system that fosters, and is dependent upon, a free flow of information so that a well informed citizenry can guide its own destiny, the question of the relationship between the private communications media and the government is, in many ways, the ultimate issue in a free society. If the achievement of a new relationship between government and the private cable medium is not anticipated but left to chance, the free flow of diverse information and ideas that is protected by the Constitution could be endangered. This is the most important reason for a clear and far-sighted policy for cable technology on the Federal level: the overriding national interest in freedom of expression.

There is also another reason, less philosophical but very important. Cable is not only a medium of expression, it is an industry — an employer of labor and capital, a producer of goods and services, and a contributor to the overall productivity of our economy. Cable is an industry which is closely linked to several major national industries including electronic

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[2] United States v. Southwestern Cable Co., 392 U.S. 157 (1968).

[3] United States v. Midwest Video Corp., 406 U.S. 649, 675-76 (1972).

data processing telephone television and radio broadcasting the motion picture and music industries and communications satellites Although each cable system is a local enterprise it distributes television signals in interstate commerce Because of these characteristics cable requires a consistent and coherent national policy

Recognition of the need for a national policy however must not preclude an appreciation of the important and often diverse local interests in the development and performance of cable systems Localism plays as important a role in our system of mass communications as it does in our system of government Cable can fulfill its promise of providing a medium for a multitude of diverse voices serving both local and national purposes only as long as state and local governments are given a substantial role in determining the policies for cable communications services

The Nature of the Choice to be Made

Having concluded that a new policy is needed for cable communications we felt it important to clarify the issues that underlie the policy choice to be made

Many questions have been raised concerning the ultimate implications of cable for society Will people use all the services that full development of cable promises? Will they be able to absorb all the information cable can place at their fingertips or will it result in information overload and lead to increased confusion instead of increased knowledge? Will multiplying the choices available to us enhance the differences among us and result in social and political fragmentation? Will there be a fractionalization of audiences because of cable, and if so what will be its effects on social stability and on the economic viability of the broadcasting and cable industries? Will there be a loss of the sense of community and nationhood that has been enhanced by television broadcasting? Will there be an alienation of group from group region from region an unravelling of the social fabric and the development of a parochial outlook to replace a national and international outlook? Will a President be able to command all the major television channels to make an address to the nation? If not how will this affect the political and governmental processes?

Every new medium of communications has posed similar questions and we have no way of providing definitive answers to such questions in advance We are certain however that the response to the challenges posed by new communications technologies must not be to stifle their growth because of fears about their effect A democratic society must have faith in the good sense and resilience of its citizens and institutions in dealing with advancing technology The extent to which we as individuals and as a society are able to benefit from the development of cable communications depends upon the wisdom and ingenuity displayed by private citizens private industry and governmental agencies

We believe that cable development has the potential of creating an electronic medium of communications more diverse more pluralistic and more open more like the print and film media than our present broadcast system It could provide minority groups ethnic groups the aged the young or people living in the same neighborhood an opportunity to express and to see expressed their own views Yet it would also enable all of these groups to be exposed to the views of others free of the homogeneity which characterizes contemporary television programming

Cable offers countless Americans a chance to speak for themselves and among themselves in their own way and a chance to share with one another their experiences their opinions their frustrations and their hopes Rather than increase the alienation of individual from individual and group from group cable could combine the shared experience of national television with a type of active participation in the political and social process that was common in the days before urbanization eroded the opportunity for personal involvement in events that affected the community

It is hazardous to attempt to predict cable s place in the future of communications Even more than many other new technologies cable has a host of zealous proponents who wax enthusiastic about a future in which cable will serve as an electronic genie ready to provide a rich variety of services to mankind Others are doom sayers who see cable as the instrument that will lead us inevitably into 1984 serving as the final extension of the industrial revolution which will make us the slaves of technology leading lives devoid of freedom or privacy

Still others see cable as having almost no impact They predict it will struggle along as a minor supplement to broadcast television and will be shorn of all its glamour as soon as another new technology captures the imagination of a fickle constituency of academics technocrats newspaper feature writers and assorted futurists

The Committee did not attempt to assign a role for cable or choose a place for it in the future of communications in this country nor have we treated it as a modern day Rosetta stone capable of unravelling the complex problems facing this society We have simply concluded that cable has much to offer and it should be given an opportunity to prove its worth to the American people in the marketplace of goods and services and in the marketplace of ideas The proper role of government policy is to adopt consciously and deliberately a policy which insures that access to and use of cable s channel capacity are not constrained by any one force whether it be the cable system operator s power over his channels or government regulation to deal with that power

CHAPTER II

CABLE A MEDIUM OF COMMUNICATIONS AVAILABLE TO ALL

"At the heart of the Committee s recommendations is a proposed policy that would separate control of the cable medium from control messages on it The goal of this policy is to assure the development of cable as a communications medium open to all, free of both excessive concentrations of private power and undue government control"

If cable is to become a constructive force in our national life it must be open to all Americans There must be relatively easy access at one end of the cable for those who wish to promote their ideas state their views or sell their goods and services and at the other end the consumer must have a meaningful freedom of choice to select from among a diverse range of cable programming and services This unfettered flow of information is central to freedom of speech and freedom of the press which have been correctly described as the freedoms upon which all of our other rights depend These freedoms are no less essential in the days of cable than in the days of soapboxes and pamphlets

Our nation s theory of democratic government is based on the principle that the power to make decisions affecting the flow of information to and from the individual must be dispersed so that irresponsible inequitable or simply bad decisions will not have a pervasive irreversible effect In view of this principle both governmental power and excessive concentrations of private economic power over the flow of information have been viewed as inimical to the achievement of a free and open society The long standing and deeply felt opposition to concentrated private power over the media stems not simply from a belief that such power inevitably must be antithetical to this central principle of our Government Although this reason continues to be valid traditionally the excessive concentration of private power also has been opposed because it has often been used as the pretext for Government s own intrusive entry into the communications media Given the technological and economic imperatives of cable excessive concentrations of both private power and government power threaten the unfettered flow of diverse information and ideas in the cable medium

The private power of the cable system operator is potentially great because of the local monopoly characteristics of cable Unless restrained in some manner the system operator could control all of the channels on his cable system which could constitute the bulk of the channels of electronic communications in a particular locale There are two ways to restrain this power One is a detailed governmental prescription of the affirmative obligations of the cable operator requiring him to use his power in socially desirable ways The second alternative is to limit the number of channels over which the cable operator has control of program content and to require that the bulk of channels be leased to others By the first alternative the Government would seek to regulate the *use* of private power by the second it would seek to limit its *extent*

The first alternative was chosen for broadcasting — a policy prescribing the use of private power Under this approach the FCC enforces affirmative programming obligations upon the broadcaster to regulate exercise of his power over program content While it is difficult to take issue with many of the goals underlying such government imposed program requirements they result in a regulatory framework in which the Government has the power to oversee the content of a medium of communications and expression The existence of the power affects the relationship between the Government and the broadcast media and creates the constant danger of unwarranted governmental influence or control over what people see and hear on television broadcast programming

The Separations Policy

The Committee has chosen the second alternative — a policy limiting the extent of private power rather than asserting detailed regulatory control over the use of that power We recommend adoption of a policy that would separate the ownership and control of cable distribution facilities or the means of communications from the ownership and control of the programming or other information services carried on the cable channels By separating the distribution function in cable which is a natural monopoly from the programming functions which can be highly competitive the dangers of governmental intrusion and influence in programming can be avoided while the wide variety of competitors vying for the public s attention can be expected to produce a diversity of programming

This policy would create an essentially neutral distribution medium and require control of the medium to be separated from control of the messages on it The effects of private economic power on the means of distribution would cease to be a danger to the free flow of information and there would be little need for the continued application or threatened application of Government power The cable system operator would be obliged to deliver the messages of channel users with as little regard to content as the Postal Service has for the content of the print media Ideas would have to win their influence in the marketplace rather than requiring exposure through the regulatory process

To place the separations policy in perspective it is important to understand the functions of the mass media and the present extent of Government regulation of the various mass media

The Functions of the Mass Media

Three basic kinds of functions are involved in the mass media (1) the creation or compiling of information or entertainment (2) the selection or editing of this information and (3) the transmission or distribution of the information to the public [1]

The owners of the various mass media differ markedly in the nature and extent of their involvement in each of these three functions The information and entertainment that appears in newspapers for example is written primarily by reporters and writers who are employees of the newspaper and this

[1] The terms media and mass media are often used with great ambiguity Generally medium refers to the [illegible] technological means of producing or distributing information such as newspapers magazines radio broadcasting or motion pictures The term media usually refers to the industries or business that provide information or entertainment to the public A medium can be a mass medium technologically and economically but it may or may not collect a mass audience around a particular presentation For example television today is a mass medium in both senses but [illegible] may not collectively constitute a mass medium [illegible] in the sense of [illegible] to a large audience small [illegible] of copies of such magazines would be inexpensively printed and distributed but far fewer would be bought and read

material is selected and edited by other employees The newspaper is often printed on the paper s own presses and usually distributed throughout the metropolitan area in the newspaper s own trucks It ultimately reaches the reading public through independent newsstands and retail stores or through delivery services which may be owned by the newspaper In magazine and book publishing there is less of this vertical integration [2] of the media functions than in newspaper publishing A book publishing company is often no more than a suite of offices from which representatives of the publishing company purchase manuscripts from writers and then contract with printing companies to print them The books are shipped through the mails and various express companies to a wide range of independent retailers who sell the books to the reading public While many magazines employ their own writers they often contract out most of the functions involved in producing and distributing magazines In television broadcasting the essential functions of selection and transmission are by law performed by the same entity the television station and the station employees may create the programming as well

Government Regulation Common to All the Media

Despite the differences among the various mass media Government control or regulation of media power is in many respects reasonably uniform

To the extent that private power over a medium of mass communications takes the form of economic control Government regulation is very little different from its regulation of any other business For example the antitrust laws apply to the media to prevent excessive concentration of economic or market power just as they apply to the production and distribution of other goods and services Indeed to the extent that such laws and regulations prevent the assertion of significant private power over the dissemination of ideas information and entertainment Government imposed limits on the growth and exercise of private economic power also foster competition in the marketplace of ideas

The communications media however because they are the media of expression have another type of power that arises simply through the force or attractiveness of the ideas information or entertainment provided It is here that Government power is and must be strictly constrained lest it stifle the opportunities for the easy access and diversity of choice that the Government in a free society is supposed to foster Government attempts to limit or suppress the flow of information have been regarded as particularly pernicious and are explicitly prohibited under the First Amendment s injunction that Congress shall make no law abridging the freedom of speech or of the press

But even within the framework provided by the deeply rooted legal and philosophical principles embodied within the First Amendment the exercise of Government regulation of the media goes beyond the regulation of the media s economic power Government especially state and local governments in the exercise of their police powers protects the individual s right to be free of unwarranted and unwanted intrusions Therefore the application of certain laws regarding obscenity pornography privacy libel slander criminal incitement and the like are deemed by the Supreme Court to be consistent with the First Amendment Similarly Government properly may regulate to some extent which means of communication may be used to disseminate which types of information Because of the need to strike a reasonable balance among competing constitutional rights and considerations each means of communication presents its own problems in defining the nature and the permissible scope of this type of Government regulation For example certain materials cannot be sent through the mail though they can be sold on newsstands and a film that could be shown in a theater could result in criminal penalties if broadcast on television

Government Regulation Unique to the Broadcast Media

The broadcast industry in common with all the other mass media is subject to Government limits on its economic power and the exercise of Government police power -type regulation of its information content and its transmission function It is only in one significant respect that Government regulation of broadcasting is vastly different from the *laissez faire* approach that the First Amendment requires for the other media of expression

In broadcasting Government power is used to shape and direct the content of programming toward various social ends by requiring or indirectly coercing the presentation of various types of information and programming in the name of the public interest Such aspects of broadcast regulation as the encouragement of certain types of programs by means of the license renewal process the concept of broadcaster responsibility for all information disseminated over the airwaves the equal time requirement for political candidates and the Fairness Doctrine requiring balance in the discussion of public issues have no counterparts in the nonbroadcast media No Government agency directs a documentary film producer to present all sides of a controversial issue or a magazine publisher to devote equal space to all candidates for an elective office or a newspaper to devote some of its space to children s features or stories about minority group problems

It is only in the broadcast media that the First Amendment has been interpreted to permit governmental efforts to foster the expression of certain ideas or information by intruding upon the creation selection and editing functions of the private media owners Why this difference? The answer turns upon the unique power of the broadcaster in the marketplace of ideas

The dominant characteristic of the broadcast media especially television has been the scarcity of usable frequencies or channels This scarcity has facilitated an economic concentration in the broadcast industry that because of the governmental role in assigning frequencies for use by the industry is in effect a Government-conferred monopoly of broadcast outlets In conferring this benefit upon broadcasters the Congress has also decreed that broadcasters by law may control and must exercise responsibility for both the transmission and the programming functions of their stations This combination of vertical integration of the media functions and the scarcity of outlets gives television broadcasters great power over the flow of entertainment and ideas To offset such power there was an inevitable expansion of Government regulatory power over the broadcast media and it is not surprising that this regulation of the medium has carried over into regulation of the broadcaster s programming

As a practical matter to regulate the means of communication apart from the programming when the two are controlled by the same entity requires powers of discipline distinction and restraint by Government that are perhaps unattainable The regulation of programming tends to become an end in itself rather than a means of achieving constitutional goals for the free flow of information Government is driven to consider the practical effects of its regulation in terms of the effects on program content What information and which speakers should be given preferential access and in the final analysis what should the American public see and hear? These

[2] A firm is said to be vertically integrated if it performs a series of successive functions in the production and distribution of a product As an example a petroleum firm that produces crude oil transports it refines it and again distributes it to its own service stations would exhibit a high level of vertical integration An enterprise is horizontally integrated if it operates a number of facilities that produce the same products Examples are chain stores and in the cable industry the so-called multiple system owners who operate a number of geographically dispersed cable systems

questions inevitably arise not only when the Government chooses to control information through prior censorship but also when it seeks to require the presentation of certain types of information through affirmative programming requirements

The end result of the fundamental policy choices made for broadcasting is that it is not a medium of communications open and available to all The originators and producers of programming advertisers and individual citizens can gain access to the medium only through the broadcast industry or through a regulatory process that uses Government power to require the broadcasting of certain types of material There is a very real danger that access to cable will be similarly constrained unless an appropriate policy is chosen

The Print Media as a Model for Cable

Cable's multi channel technology together with the economic imperatives of a medium that is a natural monopoly could lead to an even greater concentration of power than exists in broadcast television When a single cable operator has the power to control the programming and information content of all the channels on his system his monopoly power over the cable medium of expression is nearly absolute Therefore detailed and prescriptive regulation by Government is well on its way Federal rules already require the dedication of certain channels on cable systems for such purposes as local government use other rules apply the Fairness Doctrine the equal time requirements and other aspects of public interest program regulation to programs originated by the cable operator If broadcast history is any guide this program regulation will expand until access to cable is circumscribed by Government regulations

The only way to avoid the broadcast regulatory model and allow cable to develop as a medium of communications open and available in a manner similar to the print or film media is to preclude the vertical integration of the programming and distribution functions in cable In this way the cable operator's distribution monopoly would not produce any concentration of power over free expression in the use of cable channels and would offer no pretext for Government control of programming or other information distributed by cable

Thus the separations policy would limit both private control over cable channels and the Government regulation intended to offset that control Under the separations policy cable may be able to offer Americans the opportunity diversity and richness that characterize the print and film media in this country Cable would offer unfettered access for those who wish to use its channels to promote their ideas state their views or sell their goods and services and the cable customer would have the freedom to pick and choose from among a diverse range of entertainment information and services

CHAPTER III

LONG-RANGE POLICY RECOMMENDATIONS

> *"We must guard against allowing regulation of the communications media to become an end in itself rather than a means of achieving the free flow of information and the free expression of ideas that are so vital to a democratic society"*

This Chapter sets forth the Committee s policy recommendations for a developed cable industry Discussion of the recommendations is in hree parts

- an industry structure for the 1980 s and beyond
- an institutional and jurisdictional framework for cable regulation and
- the relationship between the consumer and the cable

As stated in Chapter II the Committee attempted to anticipate and deal with the adverse effects of concentrated power in a vertically integrated cable industry We recognize however that full implementation of the policy is not appropriate for the developing cable industry of today and therefore in Chapter IV the Committee recommends a transition period during which the full policy gradually would be implemented

Industry Structure Distribution

Recommendation 1 Control of cable distribution facilities should be separated from control of programming and other services provided over the channels on those distribution facilities

Under this recommendation the principal business of the cable operators[1] would be to lease their channels or sell time on those channels to individuals or organizations that wish to offer programs or other services to the public [2] The cable operator would be precluded from having any financial interest in or relationship with those leasing channels or time on his cable system This would preclude common holdings in stock or other securities loan arrangements or any other interest in the channel user s enterprise [3] If the cable system operator were to have such an interest in a channel user he would have an economic incentive to favor the user in which he had a financial interest

Simply requiring the system operator to treat all channel users on a non-discriminatory basis without prohibiting him from having an economic interest in a user would not be adequate to prevent anti competitive behavior The cable operator could for example charge artificially high but still non discriminatory rates to users of his channels and use the excess profits from his system ownership activities to subsidize his programming affiliate This cross subsidization would place the other channel users at a severe competitive disadvantage Moreover requiring arms length transactions between companies in the same corporate structure and prohibiting cross subsidization present severe enforcement problems Such problems typically lead federal or state enforcement agencies to impose rate-of return public utility type regulation in an effort to control cross subsidization and other anti-competitive abuses

The Committee believes it is better to establish policies at the outset that deal with the causes of such adverse effects than to create the incentives for abuse and invite detailed Government regulation to deal with the effects

Recommendation 2 Common ownership or control of cable systems interconnection facilities and program supply services should be the only form of cable network operation that should be prohibited

It is likely that landline terrestrial microwave communications satellite systems or other means will be used to interconnect cable systems on an *ad hoc* or long term basis to create various national or regional networks for program distribution Therefore the Committee considered whether implementation of the separations principle must be extended beyond the local cable system itself to prevent the adverse effects of regional or national cable monopolies

There are four functional entities that must be taken into account when applying the separations policy to such network operations (1) the cable system operator (2) the program retailer who uses channels on local cable systems to offer programs to the subscribers (3) the program supplier or producer who provides programs to the retailer and (4) the interconnection facility operator who provides intersystem transmission capacity to connect one or more channels on several cable systems Naturally there may be overlaps among these entities The cable system operator may be a multiple system operator who offers channels for lease on his many systems to a single program retailer Moreover there will be instances in which the program retailer and the program supplier are one and the same

In one form of networking the program retailer would lease channels or buy time on a number of local cable systems and on interconnection facilities in order to reach a large number of geographically dispersed viewers This type of networking would pose no threat to the public interest unless a single program retailer controlled a major portion of the available local cable system or interconnection capacity or entered into anti-competitive agreements with the operators of these facilities Such instances of abuse can and should be dealt

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[1] The cable operator is the person or entity holding the cable franchise or effectively controlling through ownership or other arrangements the operation of the cable system in the geographical area covered by the cable franchise The cable system consists of the facilities used for head-end receive transmit switching storage and control functions facilities used for local distribution of signals subscriber taps and related equipment and functions We recommend however that the separation policy not apply to those limited capacity cable systems whose operators do no more than (1) retransmit the signals of television and radio broadcast stations that are defined by the FCC as local to the cable system franchise area and (2) provide weather scan or teleprinter type information service on no more than one or two standard television channels

[2] Even if the cable system owner does not control the content on all channels he will still have incentive to restrict access to his system by others if he controls and profits from significant proportion of the channels thereby defeating the purpose of the separations principle It would however be consistent with this principle to allow the system operator to continue to have control over the channels used for retransmission of the local and distant television broadcast signals authorized under the FCC cable television rules effective on March 31 1972 *i e* all local and significantly viewed stations plus the number of distant signals allowed on the basis of market size of the cable system community) as well as control over the channels used for retransmission of radio signals authorized by the FCC Program content of such channels is of course under control of the broadcast stations that originate the signals not assembled by the cable operator It also would not be inconsistent with the separations principle to allow the system operator to have program control over one or two additional channels Of course the policy would not preclude the presentation of programs produced by a firm in the same corporate structure as the cable system owner as long as the channel lessee is independent of both the cable system and the program producer

[3] This requirement would not preclude the system operator from having variable rates for channel leasing as long as there is no discrimination among comparable channel uses or users (see Recommendation 9)

with under the antitrust laws and there is no reason to prohibit networking of this type

A second form of networking would involve the common ownership or control of local cable systems and interconnection facilities by a single multiple system operator This too would pose no competitive threat to programming competition as long as there is non discriminatory access to cable channels and competitive availability of interconnection facilities

The only form of networking that necessarily raises concerns sufficient to warrant its prohibition is the common ownership or control of cable systems interconnection facilities *and* program supply services In these circumstances program retailers who are the pivotal point in the competitive supply of services to the viewers would be caught in such a cable network s vise making realistic competition impossible

The common ownership of any other combination of functions except cable ownership and program retailing requires no special prohibition Application of the antitrust laws should be sufficient to police possible abuses arising from other forms of joint ownership

> *Recommendation 3* There should be no restrictions on either cross media ownership or multiple ownership of cable systems

We recognize the potential dangers in allowing newspaper publishers or *broadcasters to own cable facilities Common* ownership of media that are nominally competitive in the same markets may limit the range of ideas discussed and reduce the competition for advertising revenues and in some cases for audiences

However in the long run cable development could significantly alter the competitive relationships among the broadcast and print media and the cable industry It would not constitute economic protectionism to give some consideration to those industries especially television broadcasting that would bear the brunt of technological innovation and competition from a successful cable industry Broadcasters and publishers should have an opportunity to own or invest in cable systems in the communities they serve without being required to divest themselves of their present media holdings in those markets Although broadcast stations would thus be allowed to a limited extent to engage in both program origination and cable operation in the same community they would still be bound by all the restrictions on program control placed on cable operators [4] There would of course be no prohibition against broadcasters or newspaper publishers owning cable systems outside the markets they already serve with these other media outlets

It is reasonable to expect that most broadcasters and publishers would prefer to offer programming on cable channels that they lease rather than to own cable systems and that should be allowed On balance the separations policy with its assurance of access by all channel users considerably lessens any potential harm which may arise from the cross media ownership of cable systems Therefore no special restrictions on such cross-ownership appear to be necessary Excessive concentrations of cross media ownership would however be prohibited by normal operation of the antitrust laws as would excessive concentration of control over broadcast newspaper cable channel content

The Committee also considered the question of limits on the number of cable systems any one firm may control or the number of customers it may serve The present trend towards increased concentration of ownership by multiple system owners would present serious problems if cable operators were allowed to control the use or content on all or most of their channels Although the separations policy would significantly lessen those dangers some anti-competitive dangers and the risk of technological stagnation presented by large scale *multiple system ownership would remain and should be dealt* with by rigorous enforcement of the antitrust laws However such enforcement should be tempered by the usual infant industry considerations that have generally been found to be in the public interest with respect to developing new industries

As a final matter affecting ownership of cable systems the Committee considered the appropriateness of municipal ownership We concluded that while there was no need to prohibit such ownership by law it would be unwise for municipalities to function as cable operators For the foreseeable future cable system ownership will be a capital intensive enterprise that may well be subject to rapid technological change and associated financial risks As long as private entrepreneurs are willing to do so it is almost certainly an unsound allocation of tax dollars for municipalities to underwrite such ventures Moreover with a financial interest in the entity being regulated it would be inappropriate for a local authority to function simultaneously as the regulator and operator of the cable system

> *Recommendation 4* Telephone common carriers should not control or operate cable systems in the same areas in which they provide common carrier services

Cable systems share some of the characteristics of existing common carrier telephone systems Both provide direct electronic connections between the subscriber and a central office thus both are capable of identifying and serving individual customer needs Although most existing cable systems provide only one way distribution of conventional television programming the systems could also provide subscribers with a capability for signaling back up the cable to order particular programming or other information services

Similarly telephone networks intended to carry two way switched voice communications have the potential to carry other one way and two way information services although they cannot provide television or certain data services with present voice communications technology

Unless limited in some way widespread expansion by telephone companies into the cable business could stifle the development of competitive cable communications service The local telephone companies franchise arrangements and rights of way their established marketing and operating organizations and the opportunities they have for cross subsidization *from existing monopoly services could work to obstruct cable* development as could the heavy capital needs of telephone companies to extend and improve telephone service Moreover the size vertical integration and long distance interconnection role of the nationwide Bell System if extended to cable communications could make it very difficult to maintain any realistic competition in communications

The Committee has concluded therefore that the present FCC rule which prohibits telephone companies from owning or controlling cable systems within their telephone service areas should be retained Telephone companies should however be allowed to continue to offer cable system operators transmission facilities for local distribution under the type of lease back arrangement that is currently in use [5] Moreover the carriers should provide cable operators with nondiscriminatory access to the carriers poles conduits and other rights of way

While telephone companies should be precluded from control of cable systems they should be allowed to compete with cable systems in offering communications capacity for such

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[4] Their position would be little different from the cable operator who was permitted to originate or control programming on one or two channels However the television broadcaster over the air channel would be counted as one of the one or two cable channels on which the system operator can originate or control programming

[5] This would not include operation of cable system head end switching or other functions not associated with actual signal transmission

services After the cable industry is fully developed there are likely to be a range of communications and information services that could use either cable or telephone systems It will therefore be important for cable franchising authorities and utility commissions to make certain that the cable system with its local monopoly of broadband distribution facilities and the telephone company with its monopoly over switched public telephone service can compete fairly with each other and with others without cross subsidization or other anticompetitive practices

Industry Structure Programming

Recommendation 5 The development of new programming and other information services that can be offered over cable should not be impeded by government established barriers to the consumers opportunity to purchase those services

At present the range of information and entertainment available in television is quite limited In many instances the viewer in prime time may choose from among only three network programs one educational television program and perhaps one more program which may well be a network rerun offered by a local station not affiliated with a network Because most of these programs are designed to attract as large an audience as possible they are often geared to the lowest common denominator of viewers interest [6] There are few opportunities for the viewer to see programs of special interest or emphasis even though that special interest may appeal to millions of people over the course of a week or a month Moreover the limited number of broadcast television outlets reduces television s utility to advertisers who wish to reach only a particular segment of the mass audience The high cost of the relatively scarce TV broadcast advertising time makes it uneconomic for such advertisers to purchase commercial time

With cable the quality and diversity of advertiser supported programming can be expected to be greater than it is now with television broadcasting Cable s larger number of channels means advertising time will not be as costly as it is in television broadcasting and this alone could attract more advertisers *Advertisers could also avoid the need to pay for exposure to* audiences they have no interest in reaching and could support on a regular basis new types of programs appealing to limited audiences

While increasing the overall magnitude of advertiser support of cable programming is important to both the viewers and the advertisers full opportunity for the viewer to express the intensity of his program preferences and to satisfy those preferences can be assured only if the consumer also is able to make direct payments for television programming as he does for magazines books and records

The Committee recognizes that there are some valid concerns regarding the growth of subscriber supported programming or pay TV It is argued that some people may not be able to afford to purchase information or entertainment in the quantity they may desire This is true just as it is true that some people cannot now afford to buy as many books magazines newspapers or records as they might like But the creators of programs and other information services should not be prohibited from selling to anyone but broadcasters and advertisers to do so would deny to the public many services and benefits obtainable in no other way Especially in the constitutionally protected media the problem of poverty should not be dealt with by governmental restrictions of the range of choices open to consumers Moreover from the standpoint of the poor pay cable may be regarded realistically not as a more expensive form of television but as a cheaper form of motion picture theater sports arena or concert stage entertainment They may be able to purchase more of this type of entertainment programming over cable than they could otherwise afford

Another frequently voiced concern is that some of the programs presently supported by advertisers may be withdrawn from free television to be sold instead directly to viewers The FCC now has rules forbidding direct sale to viewers of certain types of sports programs feature films and other entertainment programming to prevent this program siphoning Of course viewers already pay indirectly for advertiser supported television since the costs of advertising are reflected in the products they purchase Nevertheless if programs once financed by advertisers must in the future be paid for directly by viewers there will be a measure of discontent which makes the issue both emotionally and politically charged

Television broadcasters have already sounded the alarm in the press and in the Congress arguing that program siphoning by pay cable will exacerbate the audience fractionization that they expect cable s abundance of channels to produce even without such programming They maintain that cable s competition for the viewing audience will diminish the total advertising revenues now flowing to broadcast television and sharply reduce the profitability of their business They claim that their profits are used to underwrite news and public affairs programs and to produce costly high quality entertainment programs all of which would be sharply cut back in response to cable s competition for programs and audience

This line of argument assumes that news and public affairs programs as well as high quality entertainment programs cannot be self sustaining through advertiser support or a combination of advertiser and subscriber support This assumption is questionable *There is no doubt that the networks and individual* television stations perform a valuable public service in their information programs If it is true that no other entity is capable of matching the broadcast networks scale of national and international news coverage there will continue to be advertiser and subscriber dollars available to support the networks news and documentaries At the same time cable s abundance of channels and lower programming costs appear likely to lead to the emergence of additional news and public affairs programmers offering specialized or in depth analysis to supplement the general coverage

More generally there can be a mixed system of advertiser and subscriber support for television programs the two means of support can coexist in the electronic media as they do in newspapers magazines and other print media

We anticipate that the broadcast media will continue to find advertisers who wish to reach the largest possible audience and are willing to continue to support the present kinds of mass appeal programming At the same time some national and local advertisers also will be attracted to the relatively smaller audiences that could be reached by sponsoring programs that appeal directly to those audiences Cable would thus provide a wider choice of advertiser supported programs than now exists Moreover other advertisers who wish to reach audiences with special interests but cannot afford the high cost of broadcasting s limited advertising time can be expected to underwrite free programs on cable

By definition most of the time most of the viewers will be watching general appeal entertainment programs This type of programming will continue to attract sufficient advertiser support and people will pay only to see those programs that do not attract such support Therefore it is likely that most of the cable channels used for subscriber supported programming will be devoted to special interest programs not available

[6] This is not meant to be a criticism of the intellectual or artistic quality of television programming but simply a recognition of the effect upon programming of channel scarcity and the vertical integration of TV broadcasting It is unlikely that very many Americans are reading Shakespeare s work at any given hour either but our print media — unlike broadcast television — makes them economically available in such a fashion that we can read them when we choose to do so

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on advertiser supported broadcast or cable channels or to repeating mass appeal programs at off hours. This conclusion is important not only for its implications of expanded consumer choice but also for its promise of additional sources of revenue for the performing arts, public and private education, and for the television program production industry.

If the performing arts are to remain a vital part of our national life, they must be able to tap substantial new sources of funding. The expanded electronic box office provided by subscriber supported cable could be a major source of assistance. Public and private educational institutions could also derive additional revenues by offering vocational education, continuing and specialized education, and university extension courses over cable systems. Furthermore, the television program and motion picture production industries could be revitalized by subscriber supported cable.

However, there may be a need to preclude the possibility that one type of mass audience appeal programming might shift to pay television. If there were no restraints, some popular professional sports programs might be siphoned from advertiser supported television. In view of the congressional exemption of the professional sports leagues from the antitrust laws and the recent legislation barring the free television blackout of sold out home games, sports programming stands on a different footing from all other entertainment programming on advertiser supported television. Given the unique nexus between such programs and congressional policies, the Committee recommends that the FCC continue to apply some anti siphoning restrictions concerning professional sports programs until the Congress determines that they are no longer appropriate.

However, there is no need in the long run for such restrictions on other forms of entertainment programming. The anticipated competition and flexibility in cable programming will make unnecessary and inappropriate any sweeping Government restrictions on the public's right to purchase a wide variety of information and entertainment services and on the originator's right to sell such services.

Recommendation 6. The programming, information or other services provided over cable should not be subject to administrative regulation of content, nor should the prices of such services be regulated by any governmental authority.

Administrative regulation of broadcast programs has been sanctioned by the Supreme Court on the grounds that it assists in achievement of First Amendment goals under conditions of vertical integration and a scarcity of broadcast frequencies. But with no use of the public airwaves, with a large number of channels, and with implementation of the separations policy, there is no need to resort to governmentally imposed approximations in the cable medium. Under such conditions, use of the Fairness Doctrine, the equal time rule, and other forms of program content control to regulate what the audience can or must see and hear would simply be an end in itself — an unconscionable choice for a free society.

The absence of administrative regulation of the content of cable communications, however, need not and should not remove local, state, and Federal sanctions on pornography, libel, criminal incitement, and the like. Indeed, the Committee believes that additional safeguards may be necessary. The Government can and should vary its regulation of the communications media according to their particular characteristics. Cable systems are analogous to the mails and broadcasting in that they serve the consumer in his home where, without adequate safeguards, children may have easy access to the material distributed over cable channels. But the postal laws appear to provide a better example than the broadcast laws of the type of additional safeguards that may be needed.

We recommend that the law provide safeguards to allow for selective control over reception of programs and other communications that are not desired by the recipient, enabling the individual to enforce his own standards of obscenity or violence without the need for extensive prior restraint. Such safeguards could include sanctions against the distribution of certain material to cable customers who have indicated they do not wish to receive it and requirements that the nature of certain programs be clearly identified so that the subscriber can decide whether to accept them.

Cable technology permits individual choice in filtering out undesired communications through scrambling codes, locked channels, and other devices. Once such protective mechanisms are in place, more latitude could be allowed in programs presented over the cable medium than over the broadcast medium.

In addition to precluding administrative regulation of program content on cable channels, the Committee recommends that there be no regulation by any governmental authority of the prices charged to subscribers for information, programming and other services by channel users. As discussed above, provision of programming and information services should be a highly competitive activity. There should be no need for any governmental authority to regulate the prices of such services. Moreover, Government regulation of such prices inevitably would lead to regulation of program and information content, since rate regulation would ultimately have a bearing on the nature, quantity, and quality of the services being sold. For similar reasons there should be no requirements that certain programs or information services be provided free of charge by channel users or cable operators.

Recommendation 7. Incentives to create programming for cable should be fostered by full applicability of the copyright laws to cable channel users.

There will be a steady supply of programming for presentation on cable channels only if there is a full range of financial incentives for the creators of programs. Both equity and the incentives necessary for the free and competitive supply of programs require a system in which program retailers using cable channels negotiate and pay for the right to use programs and other copyrighted information. Individual or industry wide negotiations for a license or right to use copyrighted material are the rule in all the other media and should be the rule in the cable industry.

As a matter of communications policy, rather than copyright policy, the program retailer who distributes television broadcast signals in addition to those provided by the cable operator should be subject to full copyright liability for such retransmissions. However, given the reasonable expectations created by current regulatory policy, the cable operator should be entitled to a non negotiated blanket license conferred by statute to cover his own retransmission of broadcast signals (see note 2, page 10).

Institutional and Jurisdictional Framework for Cable Regulation

The preceding recommendations have dealt with the structure of the cable distribution and programming industries. This section sets forth the Committee's proposals for the requisite federal state local governmental relationships regarding cable regulation.

Since the general thrust of the Committee's recommendations involves far less detailed administrative regulation than has existed in broadcasting, we considered carefully the question of why cable systems have to be regulated at all. There are three reasons usually given: (1) a cable system is a natural monopoly in its service area and as such should be regulated to preclude abuses that competition would normally prevent (2) *virtually all cable systems are integral parts of the interstate* distribution of programming and other information services and some regulation of the transmission medium is necessary to assure system compatibility and interoperability and (3) since cable systems compete with broadcast stations and could compete for some services with telephone companies there should be parity of regulation among the competitors

The third reason relies on a distorted notion of equity which would justify pervasive and detailed regulation of cable simply for the benefit of cable s competitors The first two reasons are valid but they justify only a limited degree of regulation quite different from the type that is usually considered in the telecommunications field

Cable is an integral part of the interstate movement of electronic communications and this relationship to interstate commerce provides adequate legal authority for the Federal Government to establish uniform conditions or minimum standards to which non Federal action must conform

However the existence of Federal authority does not resolve the question of how to determine the most effective combination of national and local regulation Federal authority could conceivably occupy the entire field but this would be an unwise course even if the Federal Government were somehow able to cope with the administrative burden of regulating thousands of cable systems across the country State and local governments have an important interest in the construction and operation of cable systems and *they can best provide regulation responsive to local needs* Consequently the Committee has concluded — as has virtually every other body that has grappled with this issue — that there must be a carefully structured dualism of governmental oversight

> *Recommendation 8* The Federal Government s authority over cable should be exercised initially to implement a national policy thereafter detailed Federal administrative supervision should be limited to setting certain technical standards for cable and applying anti siphoning restrictions on professional sports programming

The policy we recommend calls for use of Federal authority over cable solely as a means of achieving the national policy goals that we have identified But Federal authority need not and should not intrude into all aspects of cable operations as has happened in other fields of Federal regulation

The Federal Government would exercise jurisdiction only over those aspects of cable operations that require uniform national treatment The most important policies in this regard are the separations policy the prohibitions on rate of return regulation of cable operators and on rate regulation of channel users the anti siphoning restrictions on pay cable presentations of professional sports programming certain privacy safeguards copyright liability and other policies concerning industry structure in the cable transmission and programming fields

Most of these policies do not require the day to day supervision of a Federal regulatory agency but rather the uniform and consistent treatment that generally can be derived from enforcement in the Federal courts For example the Department of Justice and private parties could seek enforcement of those aspects of the policy that depend on the antitrust laws for their implementation (such as prevention of abusive cross media and multiple system ownership anti-competitive joint use of interconnection facilities and cable systems etc) and those that involve constitutionally and legislatively protected rights (such as free speech nondiscriminatory access to channels and privacy)

The only aspects of cable regulation that appear to require continuing supervision by a Federal agency are enforcement of technical transmission or distribution standards and the sports anti siphoning restrictions The mandatory technical standards however should be limited strictly to those that are necessary to make cable systems interoperable and compatible with the equipment required to transmit and receive cable signals as well as those necessary to protect individual privacy in cable communications (see page 13 of this Chapter) The Committee recommends that the function of establishing and enforcing technical standards be performed by the FCC but this function should not be used as justification for cable licensing rate regulation or other control over industry operations or practices

> *Recommendation 9* Franchising authorities should have the principal responsibility for the regulation of cable systems

At present overlapping local state and Federal jurisdiction over cable has led to the consideration or imposition of inappropriate forms of regulation The FCC has dealt with some of these jurisdictional problems but the comprehensive resolution of all of them will best be achieved through early enactment of Federal legislation to assure that non Federal regulation is compatible with the overall national policy for cable Federal legislation should establish the jurisdictional framework but as a general rule the non Federal franchising authority should have the principal responsibility for regulation of cable systems Use of the franchising process to exercise reasonable oversight of cable will avoid the continuing burden and bottlenecks of day to-day supervision of system operations that could result from Federal or non Federal regulation of cable by an administrative agency

At present the cable franchising function is performed by municipalities and other local governments The Committee believes that the local levels of government should continue to exercise this vital function since they are the authorities most closely attuned to local conditions and needs affecting cable system construction and operation But it would not be appropriate for the Federal Government to assign responsibilities for governmental supervision of cable directly to municipalities The decision regarding whether states or localities will perform franchising functions must be left to the states although we strongly urge that the local governments retain such authority and functions

This is not to say however that there should be no role for the states The state governments are in the best position to assure that cable systems provide substantial public benefits and do not abuse their natural monopoly positions States could provide overall guidance and assistance to local authorities in their franchising activities and establish minimum requirements regarding safety of cable system construction and operation If ultimately required states could also oversee the reasonableness of customer connection charges and of channel leasing rates imposed by the cable operator and assure that cable systems and telephone companies compete fairly with each other and with other companies

Within the regulatory structure we recommend the franchising authorities would be subject to certain uniform conditions standards and guidelines intended to implement the national policy objectives for cable The most important prohibitions and requirements to which state and local action must conform in order to achieve these objectives are as follows

a Prohibition on public utility type rate of return regulation

Rate-of return regulation of the rates which cable operators charge channel users should not be imposed by any level of government unless there is a clearly defined need for it [8] The

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We also recognize the responsibility of the FCC to set standards for spurious radiation from electronic equipment However these standards are not unique to cable

All regulation of rates and charges set by channel users for the provision of programming and other information services to their subscribers will of course be precluded need for such regulation may never arise since the power of the operator to charge excessive rates for channel leasing would be held in check by the presence of competition from broadcast stations, telephone companies or new technologies. More importantly, under the policy we have proposed the cable operator would profit most in the long run by encouraging wider and more extensive use of his cable capacity. This should bring about an industry pattern of expanding cable capacity and facilities and lowering rates to stimulate increased usage. In any event, if cable operators were to evidence a pattern of limiting capacity and charging high rates, public utility regulation could then be imposed by the states. Such regulation would necessarily include both rate of return regulation and a requirement that the system add channel capacity upon reasonable demand. As with rate-of-return regulation, the expansion of capacity requirement should not be imposed until there is a clearly defined need for it.

b. Prohibition on grants of exclusive franchises

There should be a prohibition on the grant of exclusive franchises for cable systems. While cable systems will be local monopolies because of technical and economic factors, there is no reason to erect legal barriers to competitive communications systems that may develop in the future or to other cable companies that could provide better service to the public than the cable system franchised initially. Even the possibility that the franchising authority might issue another franchise for the same area could act as a check upon the cable operator who was initially franchised.

c. Prohibition on use of franchise fees as general revenue raising devices

Local authorities should not use the cable franchise as a means of raising general revenues, since revenue raising franchise fees could dilute or remove the cable operator's incentives to expand services. Franchise fees, however, could be used to compensate the franchising authority for the costs of issuing and administering the franchise and for costs associated with the use of public rights of way. Moreover, the prohibition on revenue raising franchise fees would not preclude local governments from imposing reasonable business taxes on the cable operator.

d. Prohibition on dedicated free channels

Franchising authorities should be prohibited from requiring the dedication of special channels for governmental, instructional and other special purposes. At present FCC rules require that cable operators reserve one channel for educational use and one channel for local government use and that these channels be made available without charge. Such specially designated and reserved channels served a purpose in the limited channel, vertically integrated environment of broadcast television. Such requirements are unnecessary in a cable industry operating under the separations principle, since educational and local government entities, along with everyone else, will have unfettered access to the cable system's channels. Moreover, such requirements inevitably invite franchising authorities to make value judgments and set priorities regarding the terms and conditions of using free channels. The interest of governmental, non commercial and nonprofit entities in low cost access to cable channels will be served adequately through the operation of the variable charge leased channel rate schedule discussed below.*

e. Requirement of adequate channel capacity

To assure ample channel capacity for a variety of programming and other information service, the franchise should specify the number of channels that is considered to be adequate as a basic level of cable system capacity. The FCC presently requires that systems in the top 100 television markets be constructed with a minimum of 20 channels. Franchising authorities would be authorized to require channel capacity in excess of this minimum by negotiations with the prospective cable operator when the franchise is to be issued initially or reissued.

f. Requirement of non discriminatory channel lease rates

The franchise should require that the rates charged channel users by the system operator do not unreasonably discriminate among comparable channel uses and users. Disputes regarding the schedule of rates would be resolved by the courts rather than the franchising authority.

There may be different rates charged for various times of the day, discounts for long term or volume leasing of channel time or capacity, as well as different rates for various uses of the cable channels. For example, the highest unit rate for commercial use might be a percentage of the channel user's gross revenues received from subscriber supported presentations of feature films, with flat rates charged for advertiser supported programs; different rates could be used for utility company meter reading services or banking services.

The cable operator could also establish various pricing mechanisms for particular channel users. Channel users could be charged on the basis of each home subscribing to the particular program rather than charged a flat rate based upon the total number of homes connected to the cable system. In this way special interest, public service or instructional programmers could benefit from the economic base provided to the cable operator from channel users offering mass appeal programming.

In short, there are many ways that the cable operator could participate in the profitability of the programs offered by certain types of channel users without undercutting the objectives of the separations policy. Furthermore, this would make possible lower rates for local governmental, educational, charitable and other nonprofit organizations and civic groups.

g. Miscellaneous franchise provisions

The jurisdictional framework for cable recommended by the Committee would allow franchising authorities to establish conditions dealing with the cable system operator's qualifications, construction timetables, extension of service to all portions of the franchise area, setting maximum limits on the rates charged by the system operator for cable installation and monthly service, handling of service complaints, and establishing other conditions not expressly prohibited by Federal policy.

The Consumer and the Cable

In one sense a separate discussion of relationships between consumers and cable systems should not be necessary. The policy direction we have chosen is intended to remove technological, economic and legal barriers to the flow of information between the public and those who wish to provide programs or other information services. Theoretically, once the absence of those barriers is assured there should be no further need for Government to intrude upon relationships between the cable operators and channel users or between channel users and subscribers. In practice there are bound to be problems which will require some affirmative governmental effort to deal with them.

The Committee therefore recommends that steps be taken to prevent the invasion of individual privacy that could otherwise arise in some uses of cable. Additional action may also be needed to assure that basic cable or other broadband communications facilities are available to residents of outlying rural areas or to the poor. However, some of these actions will not be necessary for many years until problems arise, or may not be needed at all if no problems arise.

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* We note, however, the growing interest in public access in which a cable channel is used as a "soap-box" to allow members of the general public to participate in [illegible] dialogue. We believe that such a cable channel can serve important goals of free expression. It would not be inconsistent with the policy stated above to retain the present FCC requirement that the cable operator provide the use of one channel without charge for such public access purposes, as long as this requirement is imposed and administered by the franchising authority. However, we recommend against earmarking a portion of the cable franchise fee to subsidize the use of the public access channel, since other public and private funds can be used for this purpose.

Recommendation 10 There should be strong legal and technical safeguards to protect individual privacy in cable communications

There has been justifiable concern over the possible invasions of privacy posed by the development of cable For example remote monitoring services such as automatic meter reading may be used by unauthorized persons for clandestine surveillance Unauthorized persons could also misuse confidential personal information conveyed by cable to data storage or processing centers Furthermore commercial enterprises and perhaps local governments would be able to keep track of every program a person watches or any information service he or she uses This could cause a substantial chilling effect on the flow of information as well as a serious erosion of privacy New technology could also make it possible to address selectively each cable subscriber and provide the means to inundate him with unwanted information

The Committee considers the individual s ability to safeguard his personal privacy to be one of the most important goals of a free society The law and the traditions of a society based on the initiative responsibility and privacy of the individual require that technology serve not erode this goal

Therefore we recommend the adoption of legal safeguards to allow individual control over undesired communications and intrusions into the home These safeguards could include sanctions against the distribution of material which the subscriber indicated he does not wish to receive or which he has not specifically requested In addition to these safeguards the constitutional and common law of privacy would also apply to cable and should be adapted and enforced by the courts Finally cable lends itself to use of technical safeguards such as scrambling codes and locked channels The FCC in conjunction with other government agencies should develop and implement technical standards and requirements necessary to afford added protection of privacy in cable communications

Recommendation 11 Governmental authorities should assure that basic cable or other broadband communications are available to residents of rural areas and to the poor

Even though a majority of the homes in the United States may be wired for cable and cable may be providing programming and other information services in addition to retransmission of broadcast signals many residents of outlying rural areas may not have the option of subscribing to cable While it may eventually become economical for cable operators to *extend facilities to these areas this may be an instance in* which sole reliance on the free market incentives of cable operators may not be adequate to meet certain national policy objectives such as the widespread availability of information

If this becomes a significant problem in the future the Government should take affirmative action to assure a basic level of broadband communications service for residents of outlying rural areas We recommend that the Secretary of Housing and Urban Development and the Secretary of Agriculture be directed to follow the development of cable in rural areas and make recommendations for such Government action as they deem appropriate

There has also been concern expressed regarding the availability of cable to the poor in urban and rural areas Cable operators may attempt to delay or refuse to offer their service to areas where there is high proportion of poor households To meet this difficulty franchising authorities should require extension of service to all portions of the franchise areas While this may be viewed by some as a subsidy of the poor by the rich it is not a subsidy that is unusual or very burdensome and it could avoid the emergence of a class of citizens cut off from what could well become the information mainstream of the future Furthermore many governmental services directed to the poor may be provided inexpensively and most effectively by cable Vocational training adult education preschool instruction and public health information are examples of services that might be provided over cable with state or in some instances Federal funding We recommend that the Secretary of Health Education and Welfare be directed to examine the feasibility and cost of using cable to assist in the delivery of such services to make such information available to the state and local governments and to include use of cable channel capacity in Federally funded programs when appropriate (see Chapter V)

Recommendation 12 Participation by minority groups in cable system ownership operation and programming should be facilitated

The development of cable represents a unique opportunity for minority racial and ethnic groups to become actively involved in a new communications medium Minority groups should have not only employment opportunities but also full opportunity to participate in all aspects of cable ownership operation and programming

The general policy for the structure and regulation of the cable industry that we recommend would facilitate participation by all segments of society in cable ownership or control of channel use Moreover the local franchising authority should ensure opportunities for minority ownership and control in cable systems and programming

At the Federal level the Equal Employment Opportunity Commission should devote special attention to the development of the cable industry to assure ample employment opportunities for minority group members *We also recommend that the* Office of Minority Business Enterprise and the Small Business Administration of the Department of Commerce be directed to give high priority to cable and to propose any necessary special provisions such as loan guarantees to foster significant minority ownership or control of cable operations

CHAPTER IV

A TRANSITION PERIOD

"The almost explosive development of CATV suggests the need of a comprehensive reexamination of the statutory scheme as it relates to this new development so that the basic policies are considered by Congress and not left entirely to the Commission and the courts "

– Chief Justice Warren E Burger

The policy recommendations in Chapter III are designed to deal with a developed cable industry Such a nationwide cable medium used for a wide variety of information and entertainment services will be far different from the cable industry today which is oriented primarily to the retransmission of broadcast television signals and is a relatively small part of the nation s communications media

The next decade of cable s growth will require large quantities of long term capital to finance construction of transmission facilities and more speculative risk capital to finance programming and other service ventures Without the opportunity for adequate financial rewards entrepreneurs will lack the necessary incentives either to construct systems in major cities or to develop a wide range of services that use cable channels

The Committee is aware that there are those in the cable industry and the financial community who fear that cable will not grow at all unless the cable operator is allowed to program his own channels in order to attract subscribers and maintain an adequate short run cash flow This concern rests on the questionable assumption that no one but the cable operator has sufficient incentives to develop the new programming that will be needed to attract subscribers in major cities However unwarranted these fears may be the immediate adoption of the separations policy could prompt many potential investors to avoid the cable industry causing cable to fall prey to a self fulfilling prophecy of failure

Nonetheless the Committee believes this is the proper time to agree upon a broad long range public policy for cable communications which reflects agreement upon the core principle of separating the control of the cable distribution medium from control of the programs or other information distributed by cable Such consensus is needed in order to indicate the framework in which the cable industry is to operate and to diminish the uncertainty that has troubled cable entrepreneurs investors regulators and customers during the past decade

However in order to facilitate the orderly development of the cable industry the Committee recommends a transition period during which there would be a phased evolutionary implementation and application of the new cable policy by the Federal state and local levels of government Taking such an approach cable development in accord with the new policy need not await congressional action Although some of the Committee s policy recommendations would best be implemented by enactment of legislation in the immediate future there is much that the Executive Branch the FCC states municipalities and private groups can do to implement the Committee s policy recommendations during the transition period

Duration of the Transition Period

Specifying in advance the duration of the transition period on the basis of some measurement of the cable industry s maturity is a somewhat arbitrary but still necessary task The Committee considered many possibilities of which the two most likely were to

(1) end the transition period at some predetermined future date such as ten years after the initial aspects of the long run policy are adopted or

(2) end the transition period upon attainment of some objective criterion of maturity such as the connection of some specific percentage of households to cable either nationwide or in each franchise area

There are several variations and combinations of these possibilities and each has its strengths and weaknesses Almost any approach that would end the transition at the same time nationwide could rather arbitrarily work hardships for particular cable operators or communities Conversely if the end of the transition period were based on homes connected to cable on a system by system basis some cable operators might have an incentive to delay reaching the critical percentage and to forestall the separations policy through such tactics as charging excessive rates This would be less of a problem if the overall nationwide rate of homes connected were used to measure the maturity of the cable industry

On balance the Committee believes that the most appropriate criterion to mark the end of the transition period is the point when the nationwide percentage of households connected to cable systems reaches about 50 per cent As discussed below however the various franchising authorities should establish procedures for gradually loosening the operator s channel control in a manner most appropriate for each community prior to achievement of the 50 per cent level nationwide In this way there would be ample local control over the rate at which each cable system became subject to the separations policy Moreover a viable national cable program supply industry could evolve in an orderly manner over the course of the transition period rather than having to spring into existence full blown at its end

Transition Period Provisions

In cable s early years the potentially adverse effects of its natural monopoly characteristics will be minimal Therefore the primary purpose of the transition period is to postpone the full application of the separations policy and the other long range policy recommendations that flow from it until the cable industry approaches maturity when such policies will be both necessary and appropriate

Accordingly during the transition period cable operators should be permitted to offer programming directly or to have financial or other interests in the programming and other services offered over their systems *At the end of the transition* for the particular system the cable operator would be required to certify to the franchising authority that the sales trades and other divestiture arrangements have been made to assure full compliance with the separations policy

Before the full separations principle is in effect cable operators may have economic incentives to limit channel capacity in order to enhance the value of the channels under their control Therefore to assure from the outset a reasonable number of channels available for lease to others franchising authorities should be required by Federal policy to specify that cable systems make available for lease one equivalent channel for each channel used by the cable operator for program originations and for retransmission of broadcast signals Moreover the franchising authority should establish a pattern of gradual lessening of the cable operator s control of channels by increasing the proportion of channels to be leased to others over the course of the transition period

Without the protection of the separations policy the dangers inherent in allowing cross media ownership (newspaper magazines broadcast stations) of cable systems will have to be dealt with in some other fashion Therefore certain types of cross media ownership of cable systems should be prohibited until the end of the transition The FCC s present cable rules prohibit the television broadcast networks from owning cable systems and preclude television broadcasters from owning such systems within their stations service areas These rules should remain in effect during the transition period but there should *be no divestiture required for existing cross media ownership* combinations No other cross ownership rules should be adopted

The Committee also recommends against imposing multiple system ownership restrictions by the FCC during the transition The dangers of excessive multiple ownership can be adequately controlled through application of the antitrust laws tempered by the usual infant industry antitrust enforcement practices that have been found to be in the public interest

Finally during the transition period there should be some limitations on the type of programming now available on advertiser supported television that could be offered for a fee on cable systems The FCC s present anti siphoning rules are intended to preserve a basic level of advertiser supported sports and entertainment programs on over the air television While a mixed system of subscriber support and advertiser support for programs will provide the greatest choice and diversity for consumers and should not be restricted by government in the long run (see Chapter III Recommendation 5) we recognize that some aspects of this policy are not appropriate for the transition period For example if some popular programs were siphoned from advertiser supported TV while relatively few households were connected to cable some viewers might be deprived of a program on broadcast television before they had access to it on a cable channel

As discussed above many provisions of the transition period will end for some cable systems prior to the time when the number of homes connected to cable reaches 50 per cent nation wide if the franchising authorities so determine However siphoning is a national concern and removal of restrictions should not be left to the discretion of franchising authorities Therefore we recommend that some restrictions on siphoning be administered by the FCC for the full transition period and be made applicable against whomever is providing subscriber supported programming during that period whether it is the cable operator or a channel programmer not affiliated with the cable operator However the FCC s current anti siphoning rules are quite complex We do not endorse these particular rules but we recommend that the FCC have the authority to adapt reasonable anti siphoning provisions to the changing conditions in the broadcast cable and programming industries selectively lessening the restrictiveness of the rules

At the end of the transition period there should be no siphoning restrictions except those applying to the pay presentation of professional sports events As noted in Chapter III the Committee feels that the Congress should determine the most appropriate time to lift such restrictions on professional sports programs given the close relationship between such programs and congressional policies regarding the antitrust exemption for sports leagues and the blacking-out of sold out home games

There should be no additional administrative controls on program content on cable channels Thus the equal time provisions of the Communications Act the Fairness Doctrine and public service program requirements should not apply to programming originated on cable during the transition period or in the long run It is essential from the outset that the use of the cable medium for distributing programs be free from administrative regulation of content

Evolutionary Implementation

The Committee believes that the long range and transitional steps we recommend should evolve in a number of steps along two broad fronts division of regulatory authority and adoption of long range policy While we strongly believe that the Congress should establish the principles of the new cable policy virtually all of the steps described below could be taken by the FCC either independently or in conjunction with franchising authorities if the Congress fails to act

a Division of regulatory authority

The first step in the evolutionary plan which should be taken immediately is to divide regulatory authority over cable between the Federal and non Federal levels as discussed in Chapter III Recommendations 8 and 9

The FCC would keep in effect its present cable rules except for removal of the requirements regarding (1) mandatory program originations (2) application of the Fairness Doctrine equal time provisions and similar kinds of program content requirements to cable program originations (3) reservation of a public access channel which would be left to franchise requirements (4) specification of a basic level of channel capacity to be leased to others which would also be left to franchise requirements (5) designation of educational and local government channels (6) expansion of channel capacity and (7) specification of two-way channel capacity Existing cross media ownership of cable would be allowed to continue but the FCC would maintain its present rules forbidding cable system ownership by television broadcast stations in their own markets and by television networks nationwide

The FCC would also be prohibited from adopting multiple system ownership rules for cable and from imposing rate of return regulation on cable operators or any form of rate regulation on channel users The common ownership or control of cable systems interconnection facilities and program supply services would be prohibited (Recommendation 2) as would the ownership of cable systems by telephone common carriers in their service areas (Recommendation 4) The FCC would adapt its present anti siphoning restrictions on cable programming to reflect changing conditions in the broadcast cable and programming industries

With respect to the franchising authorities Recommendation 9 would be fully implemented Thus there would be prohibitions on rate of return regulation of cable operators on rate or program regulation of channel users on granting exclusive franchises on use of franchise fees to raise general revenues and on requirements for special use dedicated channels or free service There would also be franchise requirements that lease *rate schedules do not unreasonably discriminate* among comparable channel uses or users that system operators have adequate channel capacity that system operators make available for lease to others at least one equivalent channel for every channel used by the operator for retransmission of broadcast signals or for program originations and that one channel be made available for public access purposes Furthermore franchising authorities would have specific authority to control the rate of progress to full application of the separations policy by increasing the proportion of channels to be leased to others

The Committee believes that prompt action by the Congress to divide regulatory authority over cable is especially desirable The necessary consensus on a national cable policy could be reflected in a preamble to such legislation While the preamble would not have the force of law it would establish the separations principle as the goal for subsequent regulatory and legislative action by all levels of government This would give the industry the public and governmental authorities a clear indication of where cable is headed and what the industry structure and government regulation is likely to be This would facilitate planning by the cable industry and the investment community and greatly ease the subsequent evolution to a full separations policy

b Adoption of long range policy

Implementation of the balance of the Committee s long range policy recommendations and termination of the special transition provisions require the following actions effective at the end of the transition period

1 Limitation of FCC authority to enforcement of technical standards and of restrictions on charging viewers for professional sports programs

2 Removal of restrictions on joint ownership of television stations and cable systems in the same market and on television broadcast network ownership of cable systems

3 Adoption of appropriate privacy safeguards

4 Implementation of special provisions regarding availability of cable services to residents of rural areas and to the poor

5 Requiring cable operators to divest themselves of activities not in compliance with the separations policy

Ideally these provisions would be enacted by the Congress to become effective at the end of the transition period However certain provisions such as those regarding privacy and residents of rural areas and the poor might become effective before the end of the transition period If the Congress failed to act before the end of the transition period the FCC other government agencies and the franchising authorities could still implement most of the long range policy provisions

CHAPTER V

A DEMONSTRATION PROGRAM

'We have proposed a Federally supported program to demonstrate innovative public service uses of cable technology and to identify more precisely the technical and legal safeguards necessary to protect personal privacy in the use of cable

The Committee s basic concerns about the free flow of information led us to recommend a regulatory framework in which Government is neutral with respect to the nature and content of the messages distributed over the cable Thus the Government would not have regulatory mechanisms to require public interest uses of cable as it does in broadcasting At the same time the Committee recognized the potential of using cable for public services that traditionally are promoted or provided by Government agencies We feel there is a need for the Government to make sure that this potential is fully explored and realized We are concerned that relying solely on the commercial marketplace for the development of cable services may cause commercial applications to outstrip the development of public services Unless cable s use for public services is thoroughly explored and developed early in cable s growth the introduction of such services may be greatly delayed or thwarted

Moreover the Committee is convinced that legal and technical safeguards needed to protect individual privacy must be developed and evaluated before cable growth is so extensive and cable facilities and practices are so firmly entrenched that the appropriate safeguards cannot be adopted without major opposition disruption and expense

Finally there is a chicken and egg problem hampering the development of many valuable services that might be commercially viable The demand for these services depends heavily on their availability yet few potential suppliers are willing to accept the risk of developing new services without significant evidence of a market demand for them Similarly while each new cable service would require relatively expensive special facilities if offered alone these services can be aggregated and the requisite facilities can be combined so that these costs can be shared but no one has emerged to lead and coordinate such a joint effort

The Committee believes the Federal Government has a responsibility to help identify the public services that can best be provided via cable communications and to evaluate appropriate privacy safeguards The committee has concluded that the most effective way to achieve these objectives would be through a Federally supported effort Consequently we recommend consideration of a systematic demonstration program involving Federal state and local government agencies appropriate public and professional groups and the cable and electronics manufacturing industries The experience gained from this program would reduce the lead time needed to develop many desirable public service uses of cable and facilitate their widespread implementation with greater effectiveness and efficiency The demonstration program would also make it possible for private users to test the feasibility of various new services at their own expense offsetting some of the cost of testing public service applications

Description of the Proposed Demonstration Program

Although the Committee did not attempt to establish the precise characteristics of the demonstration program it did consider the program s basic structure and overall objectives

It is important that the demonstration program be carefully delimited in both geographic scope and duration in order to assure that the program does not constitute a widespread or continuing subsidy for the cable industry or a vehicle for government propagandizing over cable

Governmental funds should be used only to support the purchase of advanced terminal equipment and to underwrite certain of the costs of the public service aspects of the demonstration We expect that much of the system equipment and facilities including the cable transmission system needed for the demonstration program would be financed by the private sector or would consist of existing systems in a number of representative communities

Participants in the program should include the Department of Health Education and Welfare the Department of Housing and Urban Development the Environmental Protection Agency and other Federal agencies which provide direct service to the public State and local governments should be involved in the selection of demonstration services and sites as well as in operational aspects of the program And both private and public institutions should share in designing and providing services and in conducting related experiments

Federal support for the program should run for no more than five years with actual on site demonstrations beginning as early as the second year Systematic evaluation plans should be incorporated into each of the experimental efforts so that information will be available to guide the development of other experiments All public and private institutions that participate in the demonstration program including those who do so at their own expense by paying projected commercial rates for channel leasing and facilities should be obliged to agree that all evaluation and experimental data will be made available to the public

Some examples of types of service that have been suggested to the Committee as appropriate for the demonstration program are

- Adult education courses and university extension instruction could be provided to individuals in their homes at times most convenient to them and in a manner tailored to their particular needs These could include cable transmission of high school equivalency programs vocational training and college course work offered in conjunction with particular colleges and universities
- A broad range of medical and public health information and services could be delivered to people in their homes and channels could be used to enhance the professional training of doctors and para medical personnel
- State and local agencies could use the demonstration program to develop improved services for the collection storage and retrieval of a wide variety of local government information including office hours where to go for various services and municipal code enforcement
- Similarly environmental agencies could experiment with cable in improving the effectiveness of their activities including the monitoring control and enforcement of air pollution standards pollution health warnings for people with special sensitivities and similar activities
- Various businesses may wish to use facilities to test the feasibility of offering such services as use of the cable subscriber s home terminal to select and order goods from department store catalogues to order tickets for transportation entertainment and cultural events for home use of computer processing networks for banking transactions for files and record maintenance and for electronic mail delivery

CHAPTER VI

SUMMARY OUTLINE OF RECOMMENDATIONS

"The Committee has concluded that programming, advertising, and other information and services on cable channels can be allowed to develop on a free and competitive basis, with no more regulatory power exercised over the content of this communications medium than is exercised over the print or film media"

The following sections A E constitute a summary outline of the Committee s long range recommendations (Chapter III) as they affect cable operators channel users telephone common carriers the FCC and the franchising authorities The exceptions to those recommendations which would apply during the transition period (Chapter IV) are summarized in section F

A Policies Affecting Cable System Operators

1 Operators should be REQUIRED to

a Offer their channels or time on their channels for lease to others for any lawful purpose and without discrimination among comparable uses and users (pp 10-13 15) [1] with the exception of the channels used for retransmission of the broadcast signals authorized for carriage by the FCC s cable rules plus one or two additional channels The FCC s rules regarding broadcast signal carriage will apply to channels used for retransmission of the broadcast signals (note 2 p 10)

b Comply with Federal and franchising authority requirements to construct cable systems with adequate channel capacity (p 15)

c Comply with the minimum technical standards established for cable distribution by the FCC (p 14)

d Offer customers a selective means to control or prevent reception of programming or information services which the customer does not wish to receive and to prevent interception of personal or confidential information distributed over cable (pp 13 14)

2 Operators should be ALLOWED to

a Own and operate other media outlets such as newspapers magazines or broadcast stations or networks including those within the same market area as the cable system (p 11)

3 Operators should be PROHIBITED from

a Having any financial or ownership interest in or any control of the production selection financing or marketing of the program or information services supplied by channel users leasing the operators distribution facilities (p 10) with the exception noted in section A 1 a

b Participating in the joint ownership or control of cable systems interconnection facilities and program supply services (pp 10-11)

B Policies Affecting Program Retailers and Other Channel Users

1 Channel users should be REQUIRED to

a Adhere to all applicable provisions of copyright laws and accept full liability for any program materials or information services they may supply (p 13)

2 Channel users should be ALLOWED to

a Lease channels or obtain other distribution services from any cable system with which they have no financial relationship or other form of common interest or control — with the exception noted in section A 1 a — and offer to the public any lawful program materials or information services via such system (pp 10 13)

b Establish such charges as they consider appropriate for the programming or information services they supply without regulation by Federal state or local authorities (p 13)

c Have legal recourse against any cable system operator (1) who denies access or discriminates against the channel user by reason of the content of the user s message or the user s race religion nationality or beliefs or (2) who otherwise engages in practices that violate the requirement of non-discriminatory channel lease rates (p 15)

3 Channel users should be PROHIBITED from

a Providing any information or taking any action in violation of relevant laws and statutes protecting privacy and governing dissemination of obscene libelous or otherwise illegal material as well as material the cable customer has indicated he does not wish to receive (p 13)

b Requiring viewers to pay a fee for professional sports programming unless consistent with the FCC s anti siphoning restrictions (p 13)

C Policies Affecting Telephone Common Carriers

1 Common carriers should be REQUIRED to

a Provide pole conduit or other right-of way access to any franchised cable system operator at reasonable rates and without discrimination among users or uses (p 11)

2 Common carriers should be ALLOWED to

a Offer local cable distribution service on a lease back basis to any franchised cable system operator (p 11)

b Obtain franchises to operate as cable system operators outside of any area in which they have exclusive authority to provide telephone service (p 11)

3 Common carriers should be PROHIBITED from

a Owning controlling or operating any cable system within their telephone service areas i e performing any function not associated with actual signal distribution such as the operation of cable system head-ends used for information origination reception conversion switching or other processing functions (p 11)

D Policies Affecting the Federal Communications Commission (FCC)

1 FCC should be PERMITTED only to

a Establish minimum technical standards for cable distribution systems only as needed to ensure compatibility interoperability privacy and security of cable systems (p 14)

b Require that cable systems be constructed with adequate channel capacity (p 15)

c Apply restrictions to the presentation for a fee of professional sports programs (pp 13 14)

2 FCC should NOT BE PERMITTED to

a Regulate in any way the information content of any services carried by cable system including any regulations as to the balance or fairness of such information (p 13)

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[1] All page references are to Chapter III, except where otherwise indicated

b Require minimum channel capacity to be leased to others designate special purpose channels require expansion of channel capacity or construction of two way capacity (Chapter IV p 18)

c Regulate the rates or earnings of cable operators or channel users or require any free service (p 13)

d Limit by regulation or policy the ownership of cable systems by broadcast stations or networks or by news papers magazines or other media outlets or limit the number of cable systems to be owned by one firm or the number of customers to be served by one firm (p 11)

E Policies Affecting Franchising Authorities

1 Franchising authorities should be REQUIRED to

a Award non exclusive franchises for the use of public rights of way by cable systems and collect franchise fees for such use to the extent the fees merely compensate for the costs of regulation or costs incurred in the use of the public rights of way (p 15)

b Require that the rates terms and conditions for channel leasing not unreasonably discriminate among comparable channel uses and users (p 15)

c Require that the cable operator make available one channel to be used for public access purposes (note 9 p 15)

d Require through negotiations with prospective cable operators that cable systems be constructed with adequate channel capacity (p 15)

2 Franchising authorities should be PERMITTED to

a Set maximum limits on the rates or charges imposed on customers for cable installation (p 15)

b Establish franchising conditions dealing with the cable system operator s qualifications construction timetables extension of service to all portions of the franchise area handling of service complaints and other conditions not expressly forbidden to franchising authorities (p 15)

3 Franchising authorities should NOT BE PERMITTED to

a Regulate the information content of any service carried by a cable operator including any regulation as to the balance or fairness of such information (p 13)

b Award exclusive franchises for cable systems or require dedicated free channels for special purposes (p 15)

c Impose franchise fees on cable systems when the primary purpose is to raise revenues (p 15)

d Regulate the rate of return or earnings of cable operators or the rates charged by program or information suppliers to their subscribers (pp 14 15)

F Transition Policies

The following exceptions to the long range policy recommendations would apply during the transition period which would end when 50 per cent of the nation s households were connected to cable systems (Chapter IV p 17)

1 Cable operators would be exempt from the prohibition on offering programming directly or having financial or other interests in the programming and other services offered over their systems (Chapter IV p 17)

2 Franchising authorities would have to require cable operators to

a Make available for lease to others at least one equivalent channel for every channel used by the cable operator for retransmission of broadcast signals or for program originations (Chapter IV p 18)

b Establish a pattern of gradual lessening of the cable operator s control of channels by increasing the proportion of channels to be leased to others (Chapter IV p 18)

3 The Federal Communications Commission would continue to

a Prohibit future ownership of cable systems by television broadcast networks and by television broadcast stations in their station service areas (Chapter IV p 18)

b Apply restrictions on the type of entertainment programming that can be offered to cable system customers for a fee and adapt such restrictions to changing conditions in the broadcast cable and programming industries (Chapter IV p 18)

APPENDIX

Current Regulatory Framework[1]

At first the cable television industry was regulated only by local authorities whose requirements were designed primarily to assure that cables were installed in a manner consistent with construction and safety codes. These requirements were similar to those applied to other users of city streets and rights-of-way.

In 1965 the FCC issued its *First Report and Order* on cable television in which it asserted jurisdiction over microwave linked cable systems. The following year the *Second Report and Order* broadened FCC jurisdiction to include all cable systems whether or not microwave links were used. This jurisdiction was tested in the courts and affirmed by the Supreme Court in 1968.[2]

The *Second Report and Order* also imposed restrictions on bringing distant television signals[3] into the top 100 markets. This constraint resulted in a virtual freeze on cable development in the nation's major urban and suburban centers since cable operators believed that they would be unable to attract customers without offering distant signals in areas that already had good local broadcast TV reception.

In 1972 the Commission issued its *Third Report and Order* together with comprehensive rules and regulations which are reprinted below,[4] lifting some of the distant signal restrictions and imposing a number of other requirements for major market cable systems. Although the rules permit expansion of cable into major markets they also contain restraints which are designed in the view of the FCC to limit the competitive threat to the existing broadcast industry and to stimulate the use of cable for non broadcast services.

The rules require that each newly franchised cable system obtain a Certificate of Compliance from the FCC before it may begin to carry broadcast television signals. This permits the Commission to determine whether the local franchising process, the franchise agreement and the design of the cable system are in compliance with FCC requirements. The certification process also permits the applicant as well as the franchising authority to request waivers of the FCC's requirements when sufficient justification can be demonstrated. This provides a degree of flexibility in structuring a franchise to meet each community's individual objectives.

A two-tier regulatory system exists today with the FCC regulating the areas of

- Broadcast television and radio signal carriage
- Program exclusivity
- Channel capacity
- Cablecasting
- Operational procedures and requirements
- Minimum franchise requirements

At the same time local authorities may regulate such items as

- Selection of franchisee
- Subscriber rates
- Monitoring system's performance and compliance
- Operation of municipal channels

In addition there appears to be a third tier of regulation developing at the state level. Although only a few states have enacted cable regulations so far it seems likely that eventually almost all will exert some degree of authority.

In terms of the specific uses to which a cable system may be put the current FCC rules establish minimum requirements and require capacity for development of new services. For new major market systems the rules require the following designated services:

1. *Retransmission service* Mandatory carriage of local broadcast television stations and permissible carriage of distant broadcast stations up to defined limits (usually one or two)
2. *Local origination service* At least one channel under the control of the cable operator devoted to local non automated programming
3. *Public access service* One free channel for the use of the general public on a non-discriminatory first come first served basis
4. *Educational access service* One channel free for at least five years reserved for use by local educational authorities
5. *Government access service* One channel free for at least five years reserved for government uses
6. *Leased access service* A number of channels available for lease to others who wish to provide new undesignated services via the cable

In addition the FCC's rules require a 20 channel minimum capacity. At least one channel must be available for non broadcast use for each channel used to carry broadcast signals. Thus if 12 broadcast signals are carried the system must provide at least 24 channels.

With regard to two way communication the Commission has required only that the cable system be capable of eventually providing return nonvoice signals from the subscriber to the cable control center. No time schedule for implementing this capability or for providing a wider range of two-way communication is imposed.

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[1] Portions of this summary of cable regulation are reprinted from *The U[illegible] of Cable Comm[illegible]* [illegible] with the permission of the Cable Television Information Center, The Urban Institute.

[2] United States v. Southwestern Cable Co. 392 U.S. 157 (1968)

[3] Distant television signals are those that originate too far away to be received by ordinary home antennas.

[4] Editor's Note: Full text of Third Report & Order and Rules & Regulations were reprinted by Television Digest Inc. Feb. 3, 197[illegible]. Therefore they are not repeated below.

Attachment No. 5

Article from The Village Voice describing private antitrust action brought by consumers against Time, Inc.

THE monitor

The Village Voice · **Bob Brewin** P45 1/13/86

People 1, Time and Cravath 0

Cable subscribers seeking redress against Manhattan Cable Television no longer live in legal limbo, thanks to a recent ruling in Manhattan federal court. In a precedent-setting decision, U S District Court judge Robert Sweet ruled that cable subscribers—not just the city—have the right to sue the company His ruling laid the ground for what could become a long antitrust suit brought by New York Citizens on Cable TV, an ad hoc public interest group, against Manhattan Cable, its parent company, Time Inc, and Home Box Office, another Time subsidiary

Bob Perry, an attorney for the tiny Media Law Clinic at New York Law School, which is handling the suit on a pro bono basis against a Time team from the giant Cravath, Swaine & Moore, said the ruling is the first he knows of in the country that gives third party beneficiaries—the cable subscribers—the right to sue a cable company for failure to adhere to the terms of its contract This decision could pave the way for future suits by disgruntled New York cable subscribers who feel the city has done little to enforce its contracts with Manhattan Cable (or the companies selected to wire the outer boroughs, which are behind in their promised construction schedules)

The December 18 decision was made in response to a motion by Time and MCTV to dismiss the suit, in which the citizens group, headed by Gary Kaskel, an Upper East Side videographer, alleged that the defendants engaged in monopolistic practices by offering subscribers services owned by Time (Home Box Office and Cinemax) but not unaffiliated services such as Showtime, owned by Viacom Time sought to have the suit thrown out, claiming the citizens group lacked status as a third party to the cable contract Judge Sweet, however, ruled that "the Franchise Agreement [between the city and MCTV] clearly manifests an intent to benefit the Committee's members in their status as cable subscribers . "

THE VIEWERS FIRST

Time also sought to have the suit dismissed on the grounds that any ruling requiring it to carry particular programming would be an abrogation of its First Amendment rights as a cable TV operator Judge Sweet didn't buy this argument either, ruling that viewers and cable TV programmers have First Amendment rights that should be considered too "Despite the intrusion on an operator's discretion a nondiscrimina tory injunction to open up the wires of MCTV to [non-affiliated programmers] would 'neither favor one group of speakers over another' nor regulate the content of speech More importantly, an injunction would enable programmers to reach their intended audience, a result consistent with the preference of plaintiff cable subscribers The Supreme Court has repeatedly admonished that the 'interest of viewers should be considered paramount in the First Amendment calculus' "

A Manhattan Cable spokeswoman said the company intended to continue to defend its position, but what route that defense will take is not yet clear According to Perry, Time and MCTV can either appeal Judge Sweet's ruling against summary dismissal to the second circuit court of Appeals ("and I think we'll win that too") or go to trial in district court. If the suit goes to trial it will kick off a discovery proceeding in the most controversial area of cable TV—the growing vertically integrated nature of the business, in which companies that own the wire also own the programming. This suit could prove once and for all what cable's critics have contended all along that big companies in the industry have a monopolistic hold on an entertainment medium that now goes into nearly 60 per cent of all American TV-owning homes.

On the local level, the suit will also shed needed light on Time Inc., the company that now controls the entire Manhattan cable TV market after a buyout of Group W last year (still not approved by the Board of Estimate) and a good portion of Queens through its American Cablevision subsidiary

MORE $$$ FOR TIME

The 400,000-plus Manhattan subscribers will also be sending Time Inc more money now, because, as of December 29, cable TV became a federally deregulated industry—meaning operators can raise prices at will As of January 1, MCTV's price for basic cable jumped from $12 95 to $13 95, and basic services in Group W went from $12 95 to $13 95 Prices for services such as HBO remain the same

MCTV has dropped the Christian Broadcast Network from its lineup, replacing its pastiche of exhortations and westerns with the 24-hour CNN Headline News And just in case two shopping channels (HSN1 and 2) aren't enough for people who want to but a lot of gold chains, MCTV will add yet another shopping channel, the Cable Value Network, on a partial basis sometime late this month

And MCTV *still* can't find room for Showtime?

WORLD TV FEST

Want to catch the U S premiere of an Ingmar Bergman film? Wondering what kind of stuff Radio Telefis Eirann is pumping out over the heather? Curious how Czech TV looks at WW II? How does Norwegian TV portray punk rockers?

All this will be spotlighted at the World Television Festival, which will be held at the Museum of Broadcasting (1 East 53rd Street, 752-4690), January 27 through February 28

The festival will include a Bergman retrospective that features the first U S showing of *The Blessed Ones* (a/k/a *The Sign*), which Bergman directed for television from a play by Ulla Isaksson

SCAN LINES

. . . **Even Birds Do It** Video, that is, now that the National Audubon Society has entered the field with its *Videoguide to the Birds of North America* The three-volume series includes 450 different birds in both still and motion video and animated range maps as well as bird calls and sounds from the Cornell Laboratory of Ornithology The series is available on video cassette and videodisc . . . **Cheap 'Clowns'** CBS/Fox has included one of the funniest New York movies ever made, *A Thousand Clowns*, in its budget priced ($29 95) Five Star Collection III, which went on sale January 5 Other titles in the 60 film package are *Star Wars*, *Exodus*, *The Verdict* and a number of *Pink Panther* and James Bond films .. **Turner Hits 42nd Street** Yep He's done it again Ted Turner has "colorized" the original Busby Berkley musical, 42nd Street, which will be released by CBS/Fox for Turner Entertainment in February . ■

Attachment No. 6

Anticompetitive Cable Channel Shifts

[From the Cincinnati Enquirer, November 29, 1986]

WCET to ask subscribers to write, call Miami Valley

Public station works to remain in cable's lineup

BY IRENE WRIGHT
The Cincinnati Enquirer

WCET-TV in Cincinnati will seek the support of subscribers to prevent Miami Valley Cable Television from dropping the public television station

Postcards will be mailed Monday asking members and contributors to write to Miami Valley if they want to continue viewing Channel 48, said John Dominic, WCET vice president of marketing

Cards will go to the station's 1,650 members in the Hamilton-Fairfield area and slightly fewer in the Middletown-Franklin area, Dominic said

The impact of cancellation by Miami Valley "could be significant," Dominic said

"Our entire membership is between 28,000 and 29 000, but that's just members, not all the folks who watch us," he said

Miami Valley plans to drop eight channels in its north area and seven in its south area in December, and will add a comparable number of new channels, said Taylor G Banks, Miami Valley's western Ohio manager for the parent company, Tele-Communications Inc. (TCI) of Denver Rates will increase Jan 1, he said.

Banks said subscribers will be asked to judge new programming for about 30 days

"If we've misjudged the importance of channels taken off, we may have to look at that," he said

Monthly rates will increase about 35%, from $9 92 to $13 40

The Viacom cable television company in south Dayton had planned to drop WCET from its service, but decided not to after viewers wrote and called the company, Dominic said

Each WCET member contributes an average $30 a year toward the station's estimated annual budget of $3 4 million, but being dropped by Miami Valley would mean more than just a loss of funds, Dominic said

'There are a lot of intangibles," he said "People who don't necessarily belong contribute to the annual spring auction If they don't see us how can they purchase things on the auction?"

Merchants in areas where viewers no longer have access to the channel might stop contributing to the auction, and that could halt educational programs provided to schools by the station, Dominic said

Miami Valley officials say they are adding new channels to do away with duplicate channels But Dominic said Channel 48 does not offer only duplicate programming

"We purposely program differently than Dayton (Channel 14-16) We purchase a lot of movies and series that Dayton doesn't," he said

It isn't as easy as cable officials say to pick up UHF channels, such as WCET, with rabbit-ear or regular antennae Dominic added

More than 2,000 TCI subscribers in other parts of the country were surveyed to come up with the new programming, Banks said Representatives for area cities have said they want local surveys taken before programs are changed

Jeff Heinrich, manager of the Miami Valley north service area, said the public protest "was not totally unexpected But we didn't expect quite this big an outcry "

The 22,000 Miami Valley subscribers in the north area — which includes Middletown, Franklin and Carlisle — will lose Dayton Channels 2, 22 and 45, Cincinnati Channels 19, 48 and 64, and Indiana Channels 4 and 43 The 28,000 subscribers in the south area — which includes Hamilton and Fairfield — will lose Dayton Channels 2, 7 and 22, Cincinnati Channels 48 and 64, and Indiana Channels 4 and 43

Channels to be added to both areas are Discovery, WGN of Chicago Arts and Entertainment Network, EWTN and PTL religious channels, the weather channel (new for the south), Nickelodeon and American Movie Classics An expansion of the Cable Value Network shopping channel also is planned

Viacom to raise cable TV rates in Dayton

By David E. Kepple
and Dave Daley
STAFF WRITERS

While Dayton-area subscribers to Viacom Cablevision prepare for a rate increase, some cable television viewers in Warren and Butler counties face a rate increase and the loss of three Dayton television stations from the program menu.

And, in Franklin, at least, people are not happy about it.

"It s a public outcry," Franklin Mayor Bill Thomas said Wednesday "I've talked to no one who really likes it "

In Dayton word of a Viacom rate increase came Wednesday

While the exact amount has not been set, Stan Smith Viacom general manager, said subscribers can expect basic cable rates to increase to about $12 50 or $12.75 a month from the current $10 95.

That would represent more than a 14 percent increase and it will come shortly after the cable industry becomes completely deregulated Jan 1 The Dayton City Commission has had some say over Viacom s rates, but that will end under a federal law approved two years ago

"We re anticipating an increase sometime in the first quarter of 1987 probably February or March," Smith said. "The concern I've had in the past is that, since the basic rates have been regulated, they've been artificially low

"The pay customer, the premium customer, the person who orders the extra service like HBO or Showtime which were not regulated were paying an inordinately high price

"We re going to try to bring those two in order so we may see a little bit more of an increase on the basic rates and possibly a reduction in the pay rates he said

At the least, Smith said pay TV rates would not go up HBO subscribers now pay $12 45 a month in addition to the $10 95 for basic service Showtime customers pay an additional $10 95 a month

"We brought two or three new services on in the past year," Smith said "Like everybody else labor is increasing a small percentage and our operating costs are going up So it s going to have to cover those kinds of costs "

Last month, Continental Cablevision in Dayton's southern suburbs also announced rate increases effective Jan. 1, saying the rates reflect the company's increased costs for fees it pays for satellite programming

Meanwhile in Franklin, Mayor Thomas said the controversy over the loss of Dayton stations will be discussed when the city council meets Monday night

He also said city officials will seriously consider switching to another cable company in January when the city s contract with the Middletown based Miami Valley Cable Television Co expires

' If there s another cable company that s willing to come in, I d certainly look at it " Thomas said. "I don't care if it's Johnny's TV' out of New Carlisle I feel we ve been wronged.'

Lowell Lindon, general manager of Miami Valley Cable was unavailable for comment Wednesday evening

The company last week announced its plans to drop Dayton stations WDTN (Channel 2), WKEF (Channel 22) and WRGT (Channel 45), along with two independent channels and an educational channel from Cincinnati and an independent station from Indianapolis. The channels would be replaced by The Discovery Channel, WGN of Chicago, the Arts and Entertainment Network, EWTN (Catholic Cable Network), PTL Network, The Weather Channel, Nickelodeon and American Movie Classics.

Dayton s other commercial television station, WHIO (Channel 7), survived the purge and will remain available to subscribers.

The changes could come Monday Miami Valley Cable serves Franklin, Middletown, Trenton, Monroe and Carlisle among other communities.

The company also has announced its basic cable service rate is scheduled to climb from $9.92 to $13 40 per month beginning in January

Thomas said city hall has been flooded with complaints from local subscribers.

"It s less of what we like to watch and at more cost said Thomas, who said he will cancel his cable subscription

'I'm going back to my rabbit ears," he said.

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Cable firm to raise rates, change channels

BY IRENE WRIGHT
The Cincinnati Enquirer

Miami Valley cable television subscribers from Carlisle to Fairfield will be seeing some different channels and about a 35% rate increase in about a month

Six channels including three Dayton stations will be dropped and replaced by seven other channels among them Nickelodeon and American Movie Classics

Monthly rates will jump from $9 92 a month to $13 40 a month starting Jan 1 said Jeff Heinrich manager of Miami Valley s south operation which covers Hamilton Fairfield New Miami Seven Mile Trenton and Millville and St Clair Fairfield and Hanover townships

Costs of cable television was going up regardless of channel changes he said The new channels are to improve the service we provide and add more variety

In the south area customers will gain the following channels

■ American Movie Classics with movies devoted to 50 years of Hollywood s greatest films

■ Discovery Channel focusing on nature technology history and exploration

■ Arts & Entertainment Network cultural programming

■ Nickelodeon children and family programming

■ WGN superstation out of Chicago

■ PTL and EWTN religious stations

■ Cable Value Network home shopping that will be expanded to 24 hours a day

Stations to be discontinued in the south area are

■ Channels 2 7 22 out of Dayton

■ Channel 64 Cincinnati

■ Public television Channel 48 in Cincinnati

■ Channel 4 from Indianapolis

Slightly different channel changes will be made in the north operation which includes Middletown Monroe Franklin and Carlisle Heinrich said

[From the Cincinnati Enquirer, November 27, 1986]

Cable viewers see red

Give satellite change a chance, firm says

BY IRENE WRIGHT
The Cincinnati Enquirer

Miami Valley Cable is getting static over its decision to replace some Dayton and Cincinnati stations with national satellite channels

With the replacement and a rate increase, the cable system's 50,000 subscribers in Butler County and parts of Warren County are getting "less of what we want to see, and we're paying more for it" That's how Franklin Mayor William Thomas summarized the sentiment of subscribers he has heard from

But a company spokesman thinks the dissident cable viewers will be won back once they view the new programs, due Dec 1 or as soon as new equipment can be hooked up

"We believe selection of satellite channels, compared to duplicated local network channels and some independent channels, is better programming for our subscribers," said Taylor G

Miami Valley cable picture

What they lose

Here's what 22,000 Miami Valley Cable subscribers in the north area will lose

- Dayton Channels 2, 22, 45
- Cincinnati Channels 19, 48, 64
- Indiana Channels 4, 43

Here's what 28,000 subscribers in the south area will lose

- Dayton Channels 2, 7, 22
- Cincinnati Channels 48, 64
- Indiana Channels 4, 43

What they gain

- Discovery Channel
- WGN, Chicago superstation
- Arts and Entertainment Network
- EWTN and PLT religious channels
- Weather Channel (new for south)
- Nickelodeon
- American Movie Classics
- Cable Value Network shopping channel expanded

Banks, Miami Valley's western Ohio manager for the parent company Telecommunications Inc (TCI) of Denver

Banks asks subscribers for time, about 30 days while new programming goes into effect

"Then we'll know where we stand," he said "If we've misjudged the importance of channels taken off, we may have to look at that

Hamilton City Council, after hearing from half a dozen angry subscribers, voted Wednesday night to send a letter protesting the program changes The board also resolved to start looking for another cable service though the franchise won t expire until 1991

Only about 13 subscribers have canceled service because of the lost channels, and a few others canceled because of higher fees, Banks said

Monthly rates will increase about 35%, from $9 92 to $13 40 starting Jan. 1

Subscribers in the north service area — Middletown Franklin and Carlisle — are most vocal about losing nearby Dayton channels 2, 22 and 45 Those in the south area — which includes Fairfield and Hamilton — object to losing channels 48 and 64 out of Cincinnati, Banks said

Michael Best, Fairfield first ward councilman, contributes to public television WCET (Channel 48), which he will no longer be able to view He has heard the cries from viewers too

'People are concerned, not about the rate increase but about the changes Best said "Other companies can go double or better on the number of channels I think therein lies the problem

Residents who want to see the local channels they are losing can pick them up by using small rabbit-ear antennas or with an A-B switch available at electronics stores for $5 to $7 Banks said

Subscribers concerned about losing children's programming, sports and films will get extra benefits from the Nickelodeon, American Movie Classics and WGN channels Banks said

Starting Jan 1, communities will have no voice in program or rate changes by cable television companies Cable companies also will no longer have to carry every channel within a 50-mile radius, Banks said

TCI surveyed 2,000 of its 6 million nationwide subscribers to come up with the new programming, but Hamilton, Fairfield and Franklin officials say they would like to have seen separate surveys in their cities

"I don t think they're taking into consideration local programming and priorities people have," said Hal Shepherd, Hamilton assistant city manager "Each community is unique '

Middletown City Manager William Burns is asking residents to write to him about what channels they want and he will inform Miami Valley and city commissioners But, he cautions We can t promise that we can meet everybody's demands '

C-2/Metro THE CINCINNATI ENQUIRER Friday, November 28, 1986

Cable changes anger Hamilton customers

BY JOHN R CLARK
The Cincinnati Enquirer

HAMILTON, Ohio — Butler County cable television subscribers are keeping their fingers crossed that they may have — just may have — convinced Miami Valley Cable Co officials that they are unhappy with coming programming changes

And a 35% rate increase proposed by the company isn t helping matters any

Jeff Heinrich Miami Valley Cable assistant manager, conceded Wednesday night after listening to complaints from Hamilton City Council and cable subscribers that the proposed changes "are not all set in stone '

"Changes can be made," he said

Heinrich said Tele-Communications Inc , parent company of Miami Valley, wants to give cable subscribers the best programming possible After a 30-day viewing period comments will be sought from subscribers on the changes

The programming changes — dropping Dayton channels 2, 22 and 45 and Cincinnati channels 48 and 64 and adding several others — are scheduled to take effect the first week in December Heinrich said The 35% rate increase from a basic rate of $9 92 to $13 40 a month, with no charge for additional outlets is to follow in January

Heinrich s explanation, however, failed to appease members of Hamilton City Council several of whom sharply criticized the company for proposing the changes without local input

Councilman Adolf Olivas said that "it doesn't make sense to judge this market with 600 other markets across the nation" in deciding programming Local opinions should have been sought before any changes were proposed, he said

"Unfortunately this council has no authority to dictate to the cable company what they can do ' Olivas, an attorney, said. "That ability has been legislated away from us '

Councilwoman Joan Witt said discontinuing WCET public television Channel 48 "would be a great loss to us" and asked that the addresses of the local cable company and its parent company be announced so subscribers can contact the companies

Mayor Gregory Jolivette noted that many Hamilton area residents are subscribers to Channel 48 He suggested that Cable Value Network, which offers items that can be bought by telephone, be taken off instead

"We are trying to get people to buy locally," he said

According to a Channel 48 spokesman, that station is aware of the proposed change and is preparing a protest

One unhappy subscriber referred to the proposed changes as "cablegate" and told council, "You can put all the exclamation points you want behind the name Hamilton but as long as you allow these things to happen — Chem-Dyne, Vancegate (the city's ongoing power purchase dispute with Vanceburg, Ky) and now this — the exclamation point means nothing "

Heinrich said the changes were proposed first because the company "could not ask subscribers what they they think of channels they haven't seen " He said the company received 261 telephone calls at its office at 4117 Hamilton-Middletown Road regarding the changes

Council unanimously approved a motion that an official letter of protest be sent to the cable company and its parent company advising company officials of the city's objections to both the proposed rate increase and programming changes

A second motion also was approved unanimously directing the city administration to begin solicitation of new franchise proposals Although the franchise with Miami Valley Cable does not expire until 1991, Olivas said, "it is not too early to be looking for new proposals "

A-2—MIDDLETOWN (Ohio) JOURNAL Sunday, November 23, 1986

Cable subscribers offer thoughts on upcoming changes

Miami Valley Cable subscribers may not be pleased with the company's decision to hike rates, drop several channels and add others according to an informal telephone survey conducted Saturday by The Journal

Of 15 subscribers contacted, one voiced support for the change and seven said they did not approve Seven more did not know about the change or chose not to comment

Customers expressed only mild discontent with the rate changes, but the main area of concern seemed to be the dropping of seven local channels

'We're kind of unhappy with the changes because the reason we have the cable is for the channels they have that they are going to be taking off," said Terry Whitt, 3505 Vannest St

The minuses are all things that I look at and listen to," said Keith Rainey, 451 Doverdale Drive, Monroe "I can't see much of anything on the plusses I want to look at "

Rainey said he is considering canceling his service and putting back up his motor-driven antenna

Here we are sitting half way between Cincinnati and Dayton (and that) should be a big plus for this company," said Rainey, adding Dayton has been virtually deleted from the company's programming

We will drop (the service) and get a satellite dish," said Debbie Altick, 8195 Meadowlark Drive, Franklin She agreed that she and her husband primarily view the stations being dropped

Sue Alberts, 2212 Superior Ave , said the changes wouldn't upset her and her husband enough to drop the company's service, but they were not happy especially with the dropping of channels 64 and 45

R D Smallwood, 223 Park Ave , Franklin, cited, in particular the dropping of Channel 4 from Indianapolis He said it provided good farm news

' I believe we get a better selection of viewing on the channels that we're carrying now, ' he said

Subscribers will lose Channel 2, WDTN-TV, Dayton, Channel 22, WKEF-TV, Dayton, Channel 45, WRGT-TV, Dayton, Channel 48, WCET-TV, Dayton, Channel 19, WXIX-TV, Cincinnati, Channel 64, WIII-TV, Cincinnati, and Channel 4, WTTV-TV, Indianapolis

Cable will add the Discovery Channel, WGN of Chicago, Arts and Entertainment Network, EWTN — Catholic Cable Network, PTL Network — religious, the weather channel, Nickelodian and American Movie Classics

The changes will also include the raising the basic cable rate from $9 92 to $13 40 at the first of the year

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Channel Realignments

United Cable Eyes Plan To Bump Network Affils to Upper Channels; TCI Unit Will Cluster Independents

United Calls Plan A Trial Balloon

By Peggy Ziegler

LOS ANGELES—In a bid to program cable channels in much the same way television stations program their broadcast hours United Cable Television Corp the nation s ninth largest cable operator said last week it is developing plans for a company-wide channel realignment program that could move network affiliates and independent stations out of low bandwidth positions and into spots on the upper reaches of system lineups

United chairman and chief executive officer Gene Schneider said the plan to move broadcasters is still just a tentative part of an overall plan to realign basic cable services on United systems. "We haven't come to a complete conclusion on this, but we think it's interesting to move some of these network stations around the dial," he said

United marketing and programming vice president Nimrod Kovacs likened the new programming theory to shopping mall designs that encourage traffic past small stores by anchoring large-volume department stores at opposite ends of the mall. He said United hopes to increase viewership of basic cable services by putting them between repositioned network affiliates and independents The realignment plan will roll out in United systems over the next year United systems in Denver, CO, Abilene, TX, and Bellevue NB, will be among the first to undergo channel lineup changes he said

If broadcasters occupy channel positions beyond the popular VHF 2-13 bandwidth, there will be no more Siberia," Mr Kovacs said referring to the upper reaches of a cable system s channel lineup Cable services get less viewership there than in the VHF band, where viewers are drawn by broadcast network fare and independents.

United didn't want to follow the lead of the Southern California Cable Marketing Council, which is planning a universal tier for Los Angeles area cable systems, with selected basic services joining broadcasters on the lower tier, because the plan is would move just four basic cable services to slots near the broadcast

See United, page 39

> "Broadcasters will be moved and in some cases dropped I m sorry if they're pissed off But we're not singling them out TBS is out there, too Goddamn it, it's my cable system, and I paid millions to build the plant I get mad when they tell me how I can run my store "
>
> — Barry Marshall, TCI West

TCI West Move Angers Indies

By Linda Haugsted

SEATTLE—A top official of TCI West said last week that the regional cable operator is finalizing plans for a universal channel lineup for systems in five western states which will retain network broadcast affiliates on the lowest channels along with American Movie Classics, The Discovery Channel and The Disney Channel but will probably displace local independent broadcast stations in many systems

Officials at other systems in Washington state said they will likely follow the TCI model.

Barry Marshall, divisional vice president and operating officer of TCI West, a unit of Tele-Communications Inc., said broadcast network affiliates will remain in the VHF band because they are traditionally the most watched channels. Local broadcasters will remain in the lower band if their

See TCI, page 39

United

Continued from page one

stations, Mr. Kovacs said United has eight to 10 services it wants to place in better channel positions, including what Mr Kovacs termed United "must-carries"—services in which United has an equity position including The Discovery Channel, the Preview Network and Cable Value Network.

"It's the way (NBC Entertainment president) Brandon Tartikoff and other people at the networks look at programming Mr Kovacs said Just as broadcasters program to provide strong lead-ins to certain shows, under the United plan, basic cable services would be positioned to take advantage of nearby strong broadcast signals to boost viewership, he said

To reduce viewer confusion about the changes, United would put repositioned network affiliates in a channel position that included their original channel number, with channel 2 for example becoming channel 12 or channel 22

The changes will start in United's Denver system but will be modest there since Mile Hi Cablevision with which United shares an interconnect has franchise provisions protecting broadcasters channel positions All network affiliates will retain their off-air channel numbers, but United will place USA Network, Cable Value Network, and ESPN in new positions in the lower tier, Mr Kovacs said

Plans in other systems could be more ambitious. "Our view of it is as long as you carefully communicate to consumers what you are doing and why are doing it, they don't really care if channel 4 is on channel 4," Mr. Kovacs said

In Abilene, TX, a system that will be programmed under United's proposal, all three network affiliates are already in off channel positions, and one station manager said he expected additional changes would make little difference to the station. "I'd have to see what their plan is before I react to it," said Ken Knox, station and sales manager for NBC affiliate KRBC-TV "Chances are the effect would be minimal." KRBC, which broadcasts over channel 9, has been on channel 5 in United's Abilene system for many years, Mr. Knox said. With 16 cable systems in the area, KRBC has resorted to promoting only its call letters in its advertising. "Channel identification is virtually impossible," he said.

In Bellevue, NB, Omaha broadcast stations will remain on-channel, said system general manager Steve Shippers. "We want them to retain their channel identity," Mr. Shippers said of the broadcast stations. "When they say, "Watch KMTV-3 we want our subscribers to know where they are"

Mr Kovacs said the roll-out of the plan will be gradual and done in co-operation with the wishes of the local United operators. "We will not dictate to the local systems," Mr Kovacs said

United was concerned enough about broadcasters reaction to the plan to label it a trial balloon" but Mr Kovacs said (Broadcasters reaction) depends on how it's being done The stations might bitch about it, but conceptually our job is to promote cable television not broadcast television"

United has already faced fire for channel changes. Its recent move to bundle three UHF stations, including an NBC and ABC affilite into one channel on the United cable system in Hartford CT drew fire from the Connecticut Consumer Council office and from the franchise's local advisory council

But Mr Kovacs said subscribers in Hartford didn't complain about the hundling of the three signals "The broadcasters were the ones who complained," he said

Other services that will be shifted at United Systems include MTV, USA Network, ESPN CNN, and Headline News

Mr. Schneider said realignment of broadcast signals would also help eliminate ingress, the signal disturbance caused by a strong broadcast signal interfering with its own cable signal ☐

TCI

Continued from page one

ratings justify it, otherwise they will be clustered in channels 20-30 with distant signals such as WTBS and WGN Music and other topical services will also be clustered together. Ratings dictate that popular services such as ESPN and CNN should be in the VHF band, he said. Pay services will remain relatively unchanged.

"I view the future of the cable business, in 1987 and thereafter, as a retailer no different from J C. Penney or a grocery store, with merchandise to sell, including premium services, remotes, et cetera. In the past there were too many fingers in the pie regarding how much we could charge and must-carry Now we can make a business decision based on national research, and you can't always make everyone happy. Just like when a man with a 48-inch waist goes into a store, he's not going to be happy if you don't carry a 48-inch waist in pants," Mr. Marshall said.

"Broadcasters will be moved and in some cases dropped. I'm sorry if they're pissed off but we're not singling them out. TBS is out there, too. Goddamn it, it's my cable system and I paid millions to build the plant. I get mad when they tell me how I can run my store," he said

Mr Marshall said broadcasters are presently being formally notified of the cable company's plans Some Washington state independents, however are already aware of the impending shift from their traditional off-air placements and they are fuming

"They never told us what they were planning, and as we got more information, the more shocked we became They have no regard for their subscribers They're just basing a decision on the bottom line what's especially distressing is there is no logical manner to the move We've heard we're to be on channel 25 in one system and channel 29 in the next," said Kevin Hale general manager and vice president of KSTW 11 in Seattle. (Mr Marshall said KSTW will be on 23 in all markets except those where the placement creates a technical problem In those markets it will continue to be carried on Channel 11)

Mr Hale said the move of the cable operator will disrupt the viewing habits of 200 000 households in 14 cable systems.

"Ultimately, the viewers will suffer I think they'll be very upset. We do one hour of local news. We'll be carrying Cheers. 'Family Ties, Night Court, possibly 'Cosby (in syndication) and I think they'll be very upset if they can't find us," he added

"We've spent a lot of money identifying ourselves with a number," added Roger Ottenbach general manager of KCPQ-13 of Tacoma. "If they put us out at the end of the dial, (consumers) will have to tune through a lot to get through to us. The question is, will they? Maybe that's part of the reasoning behind putting us out there"

Mr Ottenbach said a shift in the channel assignment could affect ratings because the families "out there filling out those diaries won't be able to find us, and ratings will determine what will be the bottom line" he said

Broadcasters in Washington state said they will be meeting together with attorneys and representatives of the Association of Independent Television Stations Inc. to determine what options the broadcasters have to prevent or rescind a change of channel.

"This is a direct attack on independents. If we don't fight it, the affiliates could be next," Mr. Hale said.

Mr. Marshall said the channel lineup will be instituted in TCI West systems Jan. 1, hardware permitting

Officals at TCI West's parent company could not be reached for comment last week on whether the TCI West lineup will be the pattern for other regional divisions of the nation's largest cable systems operator. ☐

[From the Multichannel News, September 8, 1986]

Cable Operators Begin To Shuffle Channel Lineups

By Debbie Narrod

NEW YORK CITY—Cable operators around the country, now planning budgets for 1987, the first year cable rates will be wholly deregulated, are more and more looking to restructuring channel lineups so that satellite-delivered cable services take the low-numbered channel slots near or adjacent to local broadcast network affiliates.

Likely to lose those low-numbered slots and be pushed to upper channel spaces, according to a number of system operators, are UHF broadcast stations, duplicative network affiliates, alphanumeric services and access channels.

One of the first companies to begin this channel-shifting process was Heritage Communications, which months ago reconfigured lineups in Dallas and Des Moines and is now dedicated to making such changes "wherever the opportunity presents itself," said Jim Braun, program manager. Such changes are now being effected in other major Heritage systems, including south Texas and South Bend, IN, he added.

Heritage had identified what it called a "core four package" of cable services it would like to put on the V-band (channels 2-13) of systems: CNN, ESPN, MTV: Music Television and USA Network. Moving these services to lower-numbered channels and near broadcast affiliates, Mr. Braun said, will increase spot viewing of the services, leading to increased cable viewing overall and to an increased perception of value in cable by the subscriber.

The fact lower-numbered cable channels are more significantly viewed was proven in Dallas shortly after a lineup change was effected. The system, formerly owned by Warner Amex Cable Communications Co. and equipped with Warner's two-way interactive Qube equipment, was monitored by MTV to see how its viewership changed with the lineup switch.

Until mid-November last year, MTV was on channel 58 in Dallas; after the switch, MTV moved to channel 10, near the local ABC affiliate; no change in program package was made.

According to Steve Seidman, MTV vice president, research, MTV's viewership increased by one-third in December and by the same amount in January in the Dallas system. (The Qube equipment has since been replaced.)

"I think it's clearly a function of having moved closely to a highly used channel, the broadcast channels," said Mr. Seidman, who called the phenomenon a "rub-off effect." Cable subscribers, he continued, "spend a disproportionate amount of time around clustered channels . . . and it comes down to where a lot of usage comes down from the broadcast networks."

Another reason the operator sees for bringing basic cable services to lower-numbered channels is to encourage local ad sales, Mr. Braun noted· "It's a much easier sell when you can tell the advertiser it'll be adjacent to a broadcast station." Heritage Des Moines manager Ted Stewart agreed he'd gotten positive feedback from local advertisers, but he couldn't quantify how much of an increase his system achieved from the switch.

Mr Braun, like other operators reached last week, downplayed how much of an effect programmers' incentives to be on lower channel numbers were playing in Heritage's efforts in the area, although he called the incentives "a worthwhile discount." He added, "We were doing this prior to the incentives."

ESPN and MTV have been most aggressive in pursuing low-band channel slots, operators said, with ESPN offering discounts for single-digit placement and with MTV viewing such placement as one in a number of factors leading to more favorable contract extensions. Other services, notably USA, said they had no intention of offering monetary incentives for placement although they advocate such switches to improve the customer's perception of cable's value and to boost local ad sales.

"This is a matter of choice between short-term dollars from services who buy positions versus the long-term benefits of customer satisfaction and retention," said USA senior vice president, affiliate relations Gil Faccio.

ESPN began studying channel placement more than a year ago, following a "gut feeling that it must have some impact" on viewing, according to Roger Williams, vice president, affiliate marketing. The sports network began doing its own analyses and then had A.C. Nielsen Co. run some statistics, as have other basic networks. Today, Mr. Williams said, several hundred systems have committed to moving ESPN to single-digit channels, with most of the changes coming from system rather than multiple systems operator level.

MTV Networks senior vice president and general manager, affiliate sales and marketing, John Reardon said while MTV had always pushed for advantageous channel placement, operators have lately been "taking a brand-new look at how lineups are arranged," a look he called e pecially important in view of price increases operators are expected to effect next year.

Mr. Reardon said he noticed this interest "came to a head at the Cable Television Administration & Marketing Society meeting in July.

"Viewers are habitually driven to watching shows around (the broadcast networks)," Mr. Reardon continued. "If the cable industry can increase viewership of cable product, then it could get better advertising revenues and enhance its perceived value as it changes price structures."

"We fundamentally believe the business we'll be in, in the next five years, is selling cable product," concurred Brian Roberts, Comcast Cable vice president of operations. By 1990 or 1992, he said, "We could be charging $20 for basic, and subscribers will want product worth that much."

That product, he said, should be cable product, "MTV and VH-1" more than independents, which he said had been proliferating since cable offered them distribution. "Shouldn't we give more, and good, shelf space to cable? Why have people trained to view UHF?" Mr. Roberts asked.

Comcast, according to president and chief executive officer Robert Clasen, has seven to eight basic services it would like to see on lower bandwidths, nearer broadcast affiliates. "You probably only need four broadcast stations below (channel) 13," Mr. Clasen said, adding, "We'd rather viewers migrate to cable "

To get such lineups, Comcast expects to drop former must-carries, depending on how the rules are finally structured, according to Mr. Clasen, who noted his systems had already axed 10-12 stations. Comcast is now reviewing channel lineups on all its systems as part of its budget process; Mr. Clasen said half to 70 percent of the operator's systems would have "significant" channel realignments in the coming year. "We view this as an opportunity to come back and resell the product," he stressed.

United Cable Television Corp. is also looking at system-by-system lineups, with an eye toward putting cable services "with the greatest potential" on the lower bandwidths and near broadcast affiliates, said Nimrod Kovacs, vice president of marketing. Services with potential, he said, are those with consumer appeal or those with possibilities for strong local ad sales. He said he believes a cable service moved to a lower-numbered channel could gain 50 percent in local ad sales, "if not double."

Mr. Kovacs said to make room for cable services on the lower bandwidth, UHF stations will likely be displaced and duplicative TV stations would be removed "where capacity is tight." United began considering such changes a year ago, he said, using studies from ESPN, United systems and local coincidentals.

In the early stages of research into V-band and broadcast channel adjacency for cable networks is American Cablesystems Corp., which assistant vice president, marketing, David Thaler said was also doing research system by system. American has also begun talking to other operators in its markets about configuring channel lineups the same throughout a market—the "fixed-channel" concept.

Boston is one of the markets where the talks have gone farthest, where 600,000-700,000 cable subscribers may be affected, said Mr. Thaler. Charles Townsend, Colony Communications president, said the game plan there would be to select four or five top cable channels and put them next to the broadcast channels. Mr. Townsend said the research he's seen on such restructuring "is tremendous," noting the proximity to broadcast stations rather than specific low-numbered channels seems to be most important.

Robert Williams, president of National Cable Advertising, was charged by the Boston-area operators to explore the fixed-channel ideal further and report back to the group.

He said last week his study of the channel lineups of the 23 systems and 40-some headends in the area had shown that getting fixed numbers for four or five basic services might be unreasonable in Boston, but added there may be a way to choose one such service. Smaller markets, he added, probably could go to fixed channel lineups. Still, he said he now believes "if a particular system can create a cluster of highly viewed channels, it may be more important than fixed channels."

Mr. Williams said area broadcasters have been showing interest in the fixed-channel idea, with some offering to fund new converter cards for operators and others looking at other innovative ways to get involved.

The Boston operators are expected to meet to discuss the issue further next month.

Cox Cable is another of the big operators examining the V-band channel issue, according to director of programming services Terry Freedman, who noted the decentralized company doesn't dictate to its operators what their lineups should be "One dilemma we have, is while we understand the benefits viewership-wise in being on a low V channel, we wonder what type of service should be there," he said.

Putting an ad-supported channel on the lower numbers, he said, may increase viewership, but the benefit in local ad sales is questionable as operators aren't yet selling on costs per thousand. On the other hand, perhaps operators should put services with lower viewer awareness (Mr. Freedman cited Lifetime and Arts & Entertainment Network) on the lower bandwidth to better convince subscribers of cable's value. Most subscribers, he pointed out, know what ESPN and MTV are.

"We don't know which way we'll go," Mr. Freedman said, adding, "We don't think the decision should be based on who gives what" for placement.

Cox Cable Spokane reconfigured its channel lineup early this summer, resulting in a channel 2-13 roster of four broadcast stations, a governmental access channel and the rest basic cable services: Headline News, USA, ESPN, CNN, MTV, WTBS and Nickelodeon. Higher-numbered channels were grouped in genres, such as information, family or religious; * * *

[From the Seattle PI, December 4, 1986]

Cable TV company's plans could leave viewers' heads S P I N N I N G

By Susan Paynter
P-I Television Critic

The Davids of local independent television felt they won a round yesterday in Seattle City Council Chambers in their battle with the Goliath of the cable TV industry

But the postponement of a takeover of Group W Cable by Tele-Communications Inc. (TCI), the nation's largest cable company, may be just a stay of execution for Channels 11, 12 and 13, which, under TCI's proposal, would soon go spinning off their designated VHF spots on the dials of Group W cable customers and into the upper reaches of the less accessible and less profitable UHF range. Channels 2-13 VHF (very high frequency) have the strongest signals, are the most easily accessible on standard TV sets and are the stations most often watched. Naturally, advertisers favor those stations.

Under TCI's plan, KSTW (Channel 11) would be shifted to Channel 28, KCPQ (Channel 13) would appear on Channel 34, and Bellingham's KVOS (Channel 12) would be on Channel 32. KTPS (Channel 28), Tacoma's public-TV station, would be dropped entirely and stands to lose the 34 percent of its subscribers who live in the Seattle area.

Several of the most desirable lower-numbered spots would be given to programming favored by the cable conglomerate. The Cable News Network would be on Channel 3, American Movie Classics (a new movie service) would be on Channel 6, Lifetime cable would be on Channel 8, ESPN sports would be on Channel 10, Disney would be on Channel 12, Nickelodeon would be on Channel 13, The Weather Channel would be on Channel 14 and a cable shopping program would be on Channel 15

TCI spokesman Curtis Speck, general manager of Seattle's Group W, admitted that TCI owns stock in CNN, American Movie Classics, The Weather Channel, the shopping service, Discovery Channel (which would be on Channel 33) and the Black Entertainment Network (which would share space with other shows on Channel 34)

Group W customers would also see their bills jump 17.5 percent by January under the TCI plan, and there seems to be no hope for stopping that increase since, under the Supreme Court-ordered deregulation of the cable industry effective Dec. 29, cable companies no longer need the approval of city and county councils to raise their rates, even if those rate hikes exceed the 5 percent ceiling formerly in effect.

In fact, it was unclear yesterday just how many teeth are still left in local ordinances governing cable TV operations. Technically, councils still grant cable franchises and the transfers of those franchises from one firm to another (in this instance, from Group W to TCI), but City Councilman Paul Kraable said a council can't deny such a transfer unless the applicant lacks the finances, technical capability or industry experience to deliver cable services to customers.

New "must carry" rules were issued by the Federal Communications Commission last Friday governing which local stations cable outfits must make room for, and the council moved to postpone its ruling on the TCI takeover until its members have read those new rules. Chairman Norm Rice delayed the TCI vote until a special Dec. 17 session, saying he also wants more time to study just how much authority city councils still have over cable TV when it comes to the public interest. He also wants time to study other issues that were raised by angry independents at yesterday's meeting.

But time is the one resource TCI does not have. Speck pushed hard for an early decision, pointing out that the company will lose valuable tax advantages if the franchise transfer isn't accomplished by Dec. 29

Concerns over the transfer fall into three categories.

■ **Rate hikes:** Deborah Lewis of the Seattle City Office of Cable Communications called the 17.5 percent increase "very high," but Rice said it is difficult if not impossible for a city council to stop such price leaps under the free-enterprise atmosphere of deregulation.

But, in an interview, TCI-Group W spokesman Bill Covington said some customers may actually save money, since the new TCI schedule offers several programs for free that customers formerly had to pay for

■ **Channel number switching:** The changing of FCC-assigned channel numbers was the biggest bone of contention at yesterday's hearing. KSTW general manager Kevin Hale said his station has spent the last 23 years, not to mention millions in advertising and promotion, fixing Channel 11 in the minds of viewers. Stations such as KING and KOMO have the advantage of call letters that spell out a pronounceable name. When your letters are KSTW or KCPQ, community identification with your number is crucial, Hale said.

Calling himself an angry Irishman, KCPQ owner Robert Kelly vowed that local broadcasters will mobilize to fight what he called "the autocratic, public-be-damned behavior" reflected in the proposed changes, which he claimed will confuse the public and cripple the ability of independent stations to compete.

And, while not directly affected, managers of KING, KOMO and KIRO also voiced concern. "Who's next?" asked KIRO program director Nick Freeman.

TCI's Speck claimed that the changes are in response to a survey that included 2,000 Seattle cable customers. Those surveyed were asked what types of programs they preferred and if they would like a system that would get rid of the cable switch-box, allowing them to use their remote controls.

But those questioned were not asked about the changing of channel numbers, and only new, "cable-friendly" TV sets allow full access to cable stations via remote control. Councilwoman Jeanette Williams voiced doubt that the survey, and not economic gain, really lay behind TCI's proposal.

Speck said the company is doing what it can to diminish confusion by clustering the independent stations together at the upper end of the dial. And TCI divisional vice president Barry Marshall asked, "Why should a Channel 11 or 12 have preferential position over a Channel 22? I believe in the free enterprise system. This (channel-changing) may cause a few problems for a short time, but broadcasters are alleging that the consumers aren't bright enough to adjust."

When similar station switching was proposed in the Los Angeles area, broadcasters and cable companies agreed to leave stations where they were. Rice said he will urge that kind of compromise here, but Marshall said that kind of agreement "smacks of antitrust to me."

■ **Cable monopolies:** The takeover itself raises broader questions about the emergence of huge cable monopolies under cable deregulation, an emergence Councilwoman Williams described as "dangerous."

"We now have a situation where a monopoly comes in and tells people what they will get and how much they will pay for it," KCPQ's Kelly claimed.

Decisions made in Seattle may affect the handling of cable takeovers pending across the country.

"What TCI is doing certainly isn't illegal," said KOMO manager Ed Lackner. "I don't know what recourse there is except to persuade cable systems it is not in the public's best interest or in their own" to change the numbers of existing stations.

But Marshall of TCI said local broadcasters are only worried about their own business interests, not public welfare. "These are the same guys who fought us (cable) for years and would just as soon have seen cable go away," he said.

Other issues raised at yesterday's hearing included concerns that:

■ In hilly Seattle, many people subscribe to cable simply to get better reception, not to have access to cable extras, and that these people might not be served by the changes.

■ Low- and fixed-income people who tend to have older TV sets will be charged more but might not get the advantages offered under the new system.

■ Acceptance of this plan might open the door to further chaos in the future.

Williams worried that no private citizens spoke at yesterday's session, and she hopes customers will come forward at the decisive meeting set for the morning of Dec. 17. No time has yet been set.

But letters protesting the dropping of Channel 28, Tacoma's public-TV station, have already been received by the Post-Intelligencer.

Viacom, the Northwest's next-largest cable system, also plans changes, including a rate hike, after the first of the year. But Viacom spokeswoman Carol Summers said the company will not move independent stations from their designated dial slots.

TCI's Speck left yesterday's hearing disappointed, saying his company is being unfairly blamed as "the bad guy." But TCI has earned its tough reputation in other cities, including the Denver area, where the company is based.

In Vail, Colo., when TCI couldn't get the rate increase it sought from the city council, the company turned off the cable system entirely and, instead of programming, ran the phone numbers of the mayor and the city manager for an entire weekend.

C 4 The Seattle Times Friday, November 7, 1986

Group W Cable changes likely to generate grumbles

JOHN VOORHEES
Times television columnist

One of the things about TV that seems to appeal to viewers is familiarity — tradition, comfortable patterns of programs seen at the same time on the expected channel

It's why people continue to watch repeats of old shows, or stick with Johnny Carson, switch to the news at 6 p m , or reach for 60 Minutes" at 7 p m on Sundays. Because TV is like a member of the family, viewers get annoyed at "surprises."

That, however, seems to be something the cable industry has never fully appreciated. They no more than get their viewers comfortable with one schedule than they change everything, usually resulting in a flurry of grumbles and complaints. It's about to happen again

Come Jan. 5, Group W Cable is planning a major reorganization that includes the introduction of some new channels, a restructuring of where you'll find some of the old channels — and a slight rate increase Gone will be the tier" system, which charged a small fee for several specialized channels like Arts & Entertainment and The Learning Channel

At that time everything that Group W carries with the exception of four pay services — HBO, Showtime, Disney and Cinemax — will be available for the basic fee of $15.50 per month (The basic fee is now $13 18, and that does not include the tier" programs)

One of the new channels to premiere in January is "American Movie Classics ' (on Channel 6), a free, commercial-free channel that shows old movies from 4 p m to 4 30 a m weeknights and from 10 a m to 4 30 a m on weekends. It s a movie service put together by T C I , the cable system that purchased the local Group W system last year (but which has not yet affixed its name to the service)

Some of the movies airing in November on American Movie Classics Channel (which is sold as a pay service in some areas) are from the 1970s, but the bulk of them are from the 1930s, '40s and 50s — movies like Orchestra Wives" with Glenn Miller, "Meet John Doe ' with Gary Cooper and a Betty Grable festival

Another new channel will be the Discovery Channel (33), which emphasizes nature, science and technology, history and exploration — programming similar to "Discover," "National Geographic" and "Smithsonian " It is, however, advertiser-supported, which means there will be commercial interruptions.

On the other hand, Group W also will be introducing Cable Value Network (15), which will be one long commercial — it's a so-called "shopping channel " Also new is The Weather Channel (14) and the Black Entertainment Channel, which will share Channel 34 with The Learning Channel, just as Spanish International Network, which is on in the afternoons and evenings, will share Channel 35 with the Financial News Network, which is on in the mornings and afternoons.

The biggest gripe may well be that Group W is moving Channels 11 and 13 from their accustomed places. Come January, in attempt to group all of the independent stations together, KSTW TV (Channel 11) will be found on Channel 23, KCPQ-TV (Channel 13) on Channel 24, KTZZ-TV (Channel 22) on Channel 25 and KTBW TV (Channel 20) on Channel 26. Moving Channels 11 and 13 is likely to annoy not only viewers, but the managements of those stations as well

Disappearing from Group W's schedule will be BCTV TV (Channel 8) from Canada, the Home Theater Network and — sob! sob! — KTPS-TV, Channel 28, in Tacoma, the area's second public-TV station

One of the great things about cable is that both Viacom and Group W have been carrying KTPS-TV in addition to KCTS-TV (Channel 9) This means that viewers usually have extra chances to catch "Masterpiece Theater" and a lot of other PBS programming, since Channels 9 and 28 generally carry most PBS programming at different times.

In fact, viewers often turn to Channel 28 first because it is more likely to carry the PBS schedule at the time PBS planned than is Channel 9 The Seattle station has a penchant for animal programs in prime time and shunting documentaries or anything even slightly controversial to times such as midnight or Sunday afternoon, where they will have the smallest audience possible

Viacom subscribers aren't going to fare any better since Viacom plans to drop KTPS-TV late in December in order to add The Nickelodeon Channel Viacom also plans a few changes after the first of the year, as well as a small rate increase, but is not yet ready to announce those changes.

TACOMA NEWS TRIBUNE - Wednesday, Nov 12th, 1986

Group W to shuffle local channels

In April, Tacoma subscribers may need a scorecard

Cable viewers of Tacoma I've got good news and bad news for you

The good news is you don t live in Seattle Group W Cable subscribers there will find them selves in January paying more for basic cable and needing a score card to find their favorite stations While network affiliates will stay where they are on the dial KSTW Channel 11 moves to cable chan nel 23 KCPQ (13) to cable channel 24 and KTZZ (22) to 25

The bad news is if you re one of Group W s 30 000 Tacoma area viewers chances are those changes will come your way in April

Tele Communications Inc (TCI) the industry giant that swal lowed Group W last June is send ing letters this week to Seattle subscribers announcing the addition of some program services the deletion of KTPS (because it s duplicative of Seattle public station KCTS) and a realignment of the channel lineup And while it s upping the monthly fee charges for additional outlets are being dropped

TCI does not plan to do the same to Tacoma s system — for now But come April, Gary Hokenson Washington state general manager for TCI Cablevision says subscribers will see some changes Hokenson maintains the plans for cutting some stations or switching

Andee Beck

the channels are vague, although we can expect KTPS to stay and KSTW (11) to stay in place

Viacom Cablevision is also avoiding comment on specifics because management is still discuss ing a variety of proposals But Seth Morrison Viacom s marketing manager in Tacoma says he s '99 9 percent sure we won t move the broadcast channels around There may be some increase for services, and a decrease for oth ers and yes some of the other channels will probably be moved around

And why all these changes after the first of the year? Because recent federal decisions effective Jan 1 give cablers more freedom than they ve ever known They can change the rates without the city's approval they can change the channels without subscribers approval. Shoot if they ve got mil lions to burn, mavericks can come into town and starting competing with each other for your subscribership

You don t want to pay more for basic cable? And you re not crazy about the stations being moved hither and yon?

Tough, say the big boys

TCI s Hokenson maintains It s just a matter of re-educating people about where those 36 program services are And even if we complain they re not changing back.

The local independent stations are furious KSTW KCPQ and KTZZ worry with good reason that viewers won t know where to find them up in the stratosphere of the TV dial

What does TCI have to say to those concerns? As Barry Mar shall a top TCI official rumbled to a cable trade journal last week Goddamn it, it s my cable system and I paid millions to build the plant I get mad when they tell me how I can run my store

Some day real soon before VCRs strangle cable completely companies such as TCI may learn the hard way to treat the customer with a little respect.

[From the Daily Oklahoman, November 3, 1986]

Cable Channel Switching Causing Stir

By Chuck Davis

Cox Cable of Oklahoma City's decision to move local television stations off-channel in January may be causing more problems than it is solving.

Cox denies that its move is anything but an attempt to provide better service to its subscribers.

The company has announced that Jan. 5, it will move local television stations and other cable channels to new locations on the dial.

According to a press release issued by the company last week, "The channel realignment will mean improved reception for Cox Cable customers... The move will eliminate direct pickup (DPU) effects which often result when local VHF stations are carried on their broadcast channel numbers

"When direct pickup occurs," the release says, "it is most often seen by cable television customers as a double image (ghost) frequently accompanied by a vertical bar on the viewer's TV screen ..."

As it stands now, KTVY-TV Channel 4 will be moving to Cox channel 7, KOCO-TV Channel 5 will be moving to Cox channel 8 and KWTV-TV Channel 9 will be moving to Cox channel 10

Local independent stations located on channels 13, 25, 34 and 43 also will be moved, although their locations on the dial have not been decided.

One source told *The Oklahoman* that Cox at first had planned to relocate KAUT-TV Channel 43, on Cox channel 34 KGMC-TV Channel 34 is a direct competitor with KAUT and KOKH-TV Channel 25.

The moves, and similar moves by other cable companies across the nation, have incensed some local and national independent station managers and top executives.

One general manager of an independent TV station in Oklahoma City, aware of Cox's plan to move him "off-channel," said the situation runs "far deeper than (fixing) poor signals."

He requested anonymity but referred *The Oklahoman* to Preston Padden, president of the Association of Independent Television Stations, in Washington, D.C.

"What Cox Cable is saying in its (press) release is a patent falsehood," Padden said

"The cable TV industry has succeeded in becoming an unregulated monopoly. Federal statutes state that their most likely competitor, the phone company, cannot carry TV cable signals," Padden said.

"Federal laws also say that the cable operators can take (or leave) any signal they want. The FCC rule — not a law — used to be that cable operators had to carry the local stations, including the independents.

"The FCC ruling (often referred to as the "must-carry" ruling) was knocked out in court, however."

Now, Padden said, "The cable operators can pick and choose anybody's signal they want — and not pay the station a nickel.

"This whole operation, at Cox Cable and elsewhere across the United States, is not being done to eliminate the ghosts. It's, one, to have an excuse to gouge more money out of the subscribers, and, two, to gin up the viewership of cable ad-supported services, like ESPN, MTV and the like."

Jill Trione, director of communications and programming for Cox Cable, said, "We didn't do this for any reason other than to eliminate the ghosting problems and the DPU problems, and to provide better service for our subscribers."

Attachment No. 7

West Virginia "Tie-in" Lawsuit

Multichannel News — March 9 1987

West Virginia Sues ATC Unit Over Service Change, Rate Hike

CHARLESTON, WV—The state of West Virginia has sued Capital Cablevision, a unit of American Television & Communications Corp., charging that the cable company violated state consumer protection and antitrust laws when it restructured its service and announced rate increases

Assistant Attorney General Doren Burrell said the suit was filed Feb 19 in the West Virginia Circuit Court for Kanawha County

Mr Burrell said Capital changed its service Jan 26 by abolishing its existing basic service, which offered 11 channels, and instead offering an additional seven channels and increasing the rate for the expanded service by $4 79 a month - He said only about 40 percent of the company's customers were subscribing to the basic-plus tier services before the change, which in effect changed their service to expanded basic.

The basic service had included three network affiliates, two Public Broadcasting Service stations, one local independent, a local programming channel, WTBS, USA Network, Nickelodeon and C-SPAN The expanded basic now also includes ESPN, The Nashville Network, CNN, MTV Music Television, CBN Cable Network, Lifetime, Arts & Entertainment and a home shopping channel

The main focus of the complaint was that the company took away the consumers' choice when it consolidated services and made them subscribe to services they didn't want "It was a deceptive way of raising the price," said Mr Burrell

He said ATC had had the case removed to federal court, where some action is expected in the next few weeks

Jon Scott, general manager at Capital, said last week "I personally feel that the case is totally without merit But we have turned the matter over to our attorneys" He said he understood that the case was based on West Virginia law and not on the federal Cable Act of 1984 ☐

IN THE CIRCUIT COURT OF KANAWHA COUNTY, WEST VIRGINIA

STATE OF WEST VIRGINIA ex rel.
CHARLES G. BROWN, Attorney
General,

Plaintiff,

v

Civil Action No 87-C-659

AMERICAN TELEVISION & COMMUNI-
CATIONS, INCORPORATED, doing
business as Capitol Cablevision,

Defendant.

COMPLAINT

PARTIES

1. Plaintiff State of West Virginia is a sovereign state, in whose name this action is brought by, and upon the relation of, Charles G. Brown in his official capacity as the Attorney General of the State of West Virginia.

2. Relator Charles G. Brown is the duly elected, qualified, and acting Attorney General of the State of West Virginia and is entitled to bring this action in the name of the State by virtue of the provisions of W Va. Code §§ 46A-7-108, 46A-7-110, and 47-18-8.

3. Defendant American Television & Communications, Incorporated, is a corporation organized under the laws of the State of Delaware, authorized to do business in the

State of West Virginia, and which does business in the State of West Virginia under the name of Capitol Cablevision

JURISDICTION AND VENUE

4 This complaint is filed and the jurisdiction of this Court invoked by plaintiff pursuant to the provisions of W Va. Code §§ 46A-7-108, 46A-7-110, and 47-18-8

5 Venue in this Court is proper pursuant to the provisions of W Va. Code §§ 46A-7-114 and 47-18-15

BACKGROUND

6. All the allegations in this complaint concerning the defendant are intended to refer to the defendant's operations conducted under the name Capitol Cablevision, and to activities of the defendant, its subsidiaries, agents, employees, and executives necessary to carry out such operations.

7. The defendant provides services, referred to hereinafter as "cable TV services," consisting of the reception of video signals and the re-transmission of those signals through high-quality, closed-path transmission lines to consumers, termed "subscribers," in return for a monthly service fee.

8. The defendant provides cable TV services to residents of the cities of Dunbar, West Virginia, South Charleston, West Virginia, and Charleston, West Virginia, under franchises granted by the respective municipal governments of those cities

9 Defendant is the only business entity currently holding a franchise to provide cable TV services in the city of Dunbar, West Virginia.

10. Defendant is the only business entity currently holding a franchise to provide cable TV services in the city of South Charleston, West Virginia.

11. Defendant is the only business entity currently holding a franchise to provide cable TV services in the city of Charleston, West Virginia.

12. Prior to January 26, 1987, and beginning at a time unknown to the plaintiff, the defendant offered three categories or tiers of cable TV service described as follows·

a. "Basic service" consisting of the reception and re-transmission of signals primarily from local television stations, broadcasting at very high frequency (VHF) and ultrahigh frequency (UHF) wavelengths, and from some additional, nonlocal stations or networks,

b. "Tier service" consisting of the reception and re-transmission of signals, originating outside the State of West Virginia, from specialized networks or stations which derive a portion of their revenue from commercial advertising and whose signals are broadcast at microwave frequencies through a network of relay stations and communications satellites; and

c. "Premium services" consisting of the reception and re-transmission of signals, originating outside the State of West Virginia, from premium networks, i.e., Home Box Office, Cinemax, and the Disney Channel, which do not carry commercial advertising and which are broadcast at microwave frequencies through a network of relay stations and communications satellites

13 The majority of signals or channels included in the Basic service may also be received by consumers with conventional television antennas.

14. Consumers can not receive any of the signals or channels included in the Tier service with conventional television antennas, although some of those signals may be received with parabolic reflector, microwave antennas, commonly known as satellite dish antennas

15. None of the signals or channels offered by the defendant as Premium services may be received with conventional television antennas, nor can such signals be received for viewing with parabolic reflector, microwave antennas unless the viewer uses special decoding equipment under license from the originators of those signals.

16. Use of unlicensed decoding equipment to view premium, "pay cable" signals is a violation of federal law

17. Prior to January 26, 1987, subscribers to the Basic service could view all signals provided in that service on a conventional television set.

18. Prior to January 26, 1987, subscribers to the Tier service could only view signals provided in that service with the aid of a cable "converter box."

19 Prior to January 26, 1987, the defendant charged a deposit fee to all subscribers using converter boxes

20. The defendant currently charges, and has charged throughout the preceding year, a fee of $7.16 per month for subscription to its Basic service and an additional fee of $4.95 for subscription to its Tier service.

21. Prior to January 26, 1987, the defendant provided cable TV services to approximately 30,000 subscribers in its franchise areas, reaching more than seventy-six percent (76%) of the households in the combined areas.

22. Of the defendant's 30,000 subscribers, more than fifty percent (50%), or 15,000 subscribers, chose not to subscribe to the Tier service.

23. On January 26, 1987, the defendant rearranged the assignment of individual signals to various television channels in order to promote and carry out a change in its services, combining the previous Basic service with Tier service to create one category of service termed "Expanded Basic service," eliminating the consumers' option of subscribing to Basic service only.

24. Beginning January 26, 1987, and continuing thereafter, subscribers to the previous Basic service have been unable to receive all of the signals provided in that service on conventional television sets.

25. On various dates, including January 26, 1987, and thereafter, the defendant has advertised, through newspapers of general circulation and through direct mailings to consumers, that the combined service is a "better" version of the previous Basic service and that the fee for the combined service would be $11.95 per month

26 The defendant has advertised that it will bill subscribers to its previous Basic service at the new, combined rate beginning March 1, 1987.

27 The defendant is taking and has taken steps, such as the distribution of converter boxes and the rearrangement of its signals corresponding to various television channels, to effect the change to the "Expanded Basic service" for all of its subscribers regardless of the subscribers' preferences for the various categories of services.

COUNT I

28 Plaintiff State of West Virginia, by its Attorney General, Charles G Brown, repeats and re-alleges the facts set forth in paragraphs 1 through 27 above.

29 By its actions, the defendant has unfairly and deceptively consolidated its services to limit and reduce consumer product options and by incorporating its Basic service and Tier service into one combined service, the defendant has unfairly and deceptively forced a substantial number of consumers to purchase a product which they do not wish to buy.

30 By incorporating its Basic and Tier service into one combined service, the defendant has unfairly and deceptively raised the price of its Basic service to approximately 15,000 consumers

31 The defendant's actions, set forth in paragraphs 6 through 30 above, are unfair and deceptive acts and practices detrimental and injurious to the public interest and in violation of W Va Code § 46A-6-104

COUNT II

32. Plaintiff State of West Virginia, by its Attorney General, Charles G. Brown, repeats and re-alleges the facts set forth in paragraphs 1 through 27 above.

33. On various dates on and about January 26, 1987, the defendant has advertised, published, and distributed, and caused to be advertised, printed, displayed, published, distributed, and broadcast, statements and representations with regard to the sale of cable TV services, stating that its new "Expanded Basic service" will cost "only $11 95" per month, that this is an "adjusted" rate for the Basic service, that the change to "Expanded Basic service" expands viewer choices while maintaining the same cost per channel and that this charge will mean a lower bill for those who had subscribed to both the Basic and Tier services.

34. The statements referred to in paragraph 33 above are misleading and deceptive in that they fail to state that the $11.95 monthly charge represents a price increase for subscribers to the previous Basic service, that the amount of the increase is $4.79, which is 66.7% more per month than the previous rate and that the corresponding decrease for subscribers to the Basic and Tier services is only a nominal sixteen cents ($0.16) per month.

35. The actions of the defendant described in paragraphs 6 through 27 and paragraphs 33 and 34 above are unfair and deceptive acts or practices as defined in subsections (12), (13), and (14) of W. Va. Code § 46A-6-102(f), detrimental and injurious to the public interest and in violation of Code 46A-6-104.

COUNT III

36. Plaintiff State of West Virginia, by its Attorney General, Charles G Brown, repeats and re-alleges the facts set forth in paragraphs 1 through 27 above

37. On various dates on and about January 26, 1987, the defendant has advertised, published, and distributed, and caused to be advertised, printed, displayed, published, distributed, and broadcast, statements with regard to the sale of its cable TV services, stating that converter boxes would now be provided to subscribers "free "

38. The statements referred to in paragraph 37 above are false, misleading, and deceptive because they fail to state that subscribers who wish to use a remote control with their television sets must pay four dollars ($4.00) per month for a special converter box and because the defendant has expressed an intention to increase its rates in the future to recoup its costs in providing the thousands of converter boxes necessary to effect the change to the "Expanded Basic service."

39. The actions of the defendant described in paragraphs 6 through 27 and paragraphs 37 and 38, above, are unfair and deceptive acts or practices as defined in subsections (5), (11), (12), (13), and (14) of W. Va. Code § 46A-6-102(f), detrimental and injurious to the public interest and in violation of Code 46A-6-104.

COUNT IV

40 Plaintiff State of West Virginia, by its Attorney General, Charles G Brown, repeats and re-alleges the facts set forth in paragraphs 1 through 27 above

41. The defendant is the sole business entity providing video reception services of premium channel signals within the cities of Charleston, South Charleston, and Dunbar, West Virginia.

42. Premium channel signals are encoded, "scrambled," so that they may only be received by consumers who subscribe to defendant's Premium services

43. Beginning at a date unknown to the plaintiff and continuing to the present, the defendant has provided its Premium services only upon the condition that the consumer also subscribe to the Basic service

44. By virtue of the defendant's exclusive position in the market for premium channel reception, the defendant has substantial market power to force consumers of the Premium service to subscribe to the Basic service as well.

45. Defendant's Basic service and Premium service are distinct products for which the defendant charges separate fees and for which there are distinct differences in consumer demand.

46. Tying the purchase of Premium services to the purchase of the Basic service distorts competition in the market for reception of local broadcast signals and restrains trade in consumer alternatives to Basic service such as conventional television antennas and related equipment

47. Tying the purchase of Premium services to the purchase of Basic service adversely affects more than 5,000 consumers and involves more than $100,000.00 per month in subscription fees.

48 By conditioning the sale of its Premium services upon the additional purchase of the Basic service, the defendant has created and maintained unlawful "tie-in" contracts in restraint of trade and competition in violation of W Va Code § 47-18-3(a)

COUNT V

49. Plaintiff State of West Virginia, by its Attorney General, Charles G Brown, repeats and re-alleges the facts set forth in paragraphs 1 through 27 above.

50. Prior to January 26, 1987, defendant's Tier service consisted of the following special-programming format, microwave networks Cable News Network, The Nashville Network, Eastern Sports Network (ESPN), Home Shopping Network, Arts and Entertainment Network, Music Television, Christian Broadcasting Network, and Lifetime Health Network

51 With the exception of the Cable News Network, which uses an electronically scrambled signal, the signals from the networks included in defendant's Tier service may also be received through the use of satellite dish antennas.

52 Under ordinances of the City of Charleston, the City of South Charleston, and the City of Dunbar, West Virginia, businesses and residents in those communities are severely restricted as to where they may have satellite dish antennas.

53. Signals from special-programming format, microwave networks are products distinct from signals from locally broadcast, conventional television frequency stations providing general programming

54. Defendant's Tier service consists entirely of the reception and re-transmission of signals from special-programming format, microwave networks.

55. Defendant's Basic service consists primarily of the reception and re-transmission of signals from local, conventional television frequency stations providing general programming.

56 Defendant's Tier service and Basic service are distinct products for which the defendant has charged separate fees and for which there are distinct differences in consumer demand.

57. Beginning at a date unknown to the plaintiff and continuing to the present, the defendant has provided its Tier service only upon the condition that the consumer also subscribe to the Basic service.

58. By virtue of the defendant's position as the sole commercial reception service for special-programming format, microwave network signals the defendant has substantial market power in the cities of Dunbar, South Charleston, and Charleston, West Virginia, to force consumers of the Tier service to subscribe to the Basic service as well.

59. Tying the purchase of Tier service to the purchase of Basic service distorts competition in the market for reception of local broadcast signals and restrains trade in consumer alternatives to Basic service such as conventional television antennas and related equipment.

60. Tying the purchase of satellite Tier service to the purchase of Basic service adversely affects more than 12,000 consumers and involves more than $14,340.00 per month in subscription fees

61. By conditioning the sale of its Tier service upon the additional purchase of Basic service, the defendant has created and maintained unlawful "tie-in" contracts in restraint of trade and competition in violation of Code 47-18-3(a).

COUNT VI

62 Plaintiff State of West Virginia, by its Attorney General, Charles G. Brown, repeats and re-alleges the facts set forth in paragraphs 1 through 27 above.

63 Plaintiff State of West Virginia, by its Attorney General, Charles G. Brown, repeats and realleges the facts set forth in paragraphs 41 through 47 above

64. Plaintiff State of West Virginia, by its Attorney General, Charles G. Brown, repeats and realleges the facts set forth in paragraphs 50 through 60 above.

65. By conditioning the sale of its Premium services and the sale of its Tier service upon the additional purchase of the Basic service, the defendant has engaged in unfair methods of competition in the market for the reception of local broadcast television signals in violation of W. Va Code § 46A-6-104.

COUNT VII

66. Plaintiff State of West Virginia, by its Attorney General, Charles G Brown, repeats and re-alleges the facts set forth in paragraphs 1 through 27 above.

67. The defendant provides discrete services, referred to herein as cable TV services, as its primary business

68 The defendant is the only provider of commercial cable TV services in the cities of Charleston, South Charleston, and Dunbar, West Virginia

69 The defendant has announced that it will raise the price of its Basic service by 66 7% and that, after expenses resulting from a change of services, the defendant expects to maintain a reasonable margin of profit.

70. The defendant has substantial power over the price of its services because consumers do not consider other reception products or services to be acceptable substitutes

71. The defendant maintains a monopoly over the supply of cable TV services within the cities of Charleston, South Charleston, and Dunbar, West Virginia.

72. The imminent restructuring of prices for defendant's Premium services and the imminent increase in the price of its Basic service constitutes use of a monopoly for the purpose of controlling prices in violation of W. Va. Code § 47-18-4.

PRAYER

WHEREFORE, plaintiff State of West Virginia prays that this Honorable Court will grant the following relief:

1. A preliminary order enjoining the defendant from violating the provisions of W. Va. Code §§ 46A-6-104, 47-18-3(a), and 47-18-4 as described in Counts I through III and Count VI of this complaint, including completing the combination of Basic service and Satellite Tier service into "Expanded Basic service," charging subscribers to the Basic service for the combined service, and all acts, including

advertising, in furtherance thereof during the pendency of this action;

2 Permanent injunctive relief enjoining the defendant from violating the provisions of W. Va. Code §§ 46A-6-104, 47-18-3(a) and 47-18-4 by unlawfully combining its services or conditioning the purchase of one service upon the additional purchase of another service and thereby preventing consumers from making independent purchase choices and forcing consumers to purchase services which they do not desire;

3. Full restitution to each consumer adversely affected by defendant's violations of W. Va. Code § 46A-6-104 described in Counts I-III of this complaint,

4 Appointment of a receiver for the sequestration of liquid assets and to preserve restitution for consumers found to have been damaged by defendant's actions;

5. Civil penalties in the amount of $5,000.00 for each violation of W. Va. Code § 46A-6-104 as set forth in Counts I, II, III, and VI of this complaint,

6. Civil penalties in the amount of $100,000 00 for all violations of W Va. Code §§ 47-18-3 and 47-18-4 as set forth in Counts IV, V, and VII of this complaint,

7. An award of plaintiff's costs in this action, including, but not limited to, filing fees, witness fees and expenses, and costs related to the production of non-testimonial evidence,

8. An award of reasonable attorney fees and investigative costs for time involved in the investigation and pursuit of this action, and

9. All other orders and judgments the Court shall deem just and proper to effectuate the purposes of the West Virginia Antitrust Act, W Va Code § 47-18-1 et seq., the West Virginia Consumer Credit and Protection Act, W. Va. Code § 46A-1-1 et seq., and other general laws of the State of West Virginia

STATE OF WEST VIRGINIA ex rel
CHARLES G. BROWN, Attorney
General,
Plaintiff,

By Counsel

Charles G Brown
CHARLES G. BROWN
ATTORNEY GENERAL

MARK KINDT
DEPUTY ATTORNEY GENERAL
State Capitol, Room 26-E
Charleston, West Virginia 25305

Counsel for Plaintiff

STATE OF WEST VIRGINIA,

COUNTY OF KANAWHA, to-wit

VERIFICATION AFFIDAVIT

The undersigned, Charles G Brown, after being duly sworn, deposes and says

I hereby verify that the allegations set forth in the foregoing complaint are true, except insofar as they are therein stated to be upon information and belief, and insofar as they are stated to be upon information and belief, I believe them to be true.

Charles G Brown

CHARLES G BROWN

Taken, subscribed and sworn to before me this 19th day of February, 1987

My commission expires July 19, 1994.

OFFICIAL SEAL
NOTARY PUBLIC
... MARTIN
... 25305

Notary Public

Attachment No. 8

"Siphoning" of NFL Games
From Free TV to Pay Cable

BETWEEN THE LINES

ESPN had the games and nobody complained

ESPN has completed its first year of National Football League regular season games, and the big news is, there wasn't any big news

Now hold on a minute, you might say Didn't the NFL on ESPN produce a combined average rating of 12 4 (a 10 6 cable-only rating), about three rating points higher than the network guaranteed advertisers? And didn't 98 percent of ESPN's universe carry the games, well above the 90 percent circulation figure guaranteed? And wasn't ESPN's production of the games of high quality, so good in fact that most critics said they were indistinguishable from those on the Big 3 networks? And didn't hundreds of cable systems reap an advertising windfall? Yes, yes, yes and yes

But here's what didn't happen Nobody—neither Congress, nor football fanatics, nor broadcasters nor the NFL owners—raised a hue and cry that ESPN was undermining the Republic It seems difficult now to recall the alarums sounded when the deal was announced, mainly to the effect that if *cable* (enunciated with definite distaste) were allowed to stick its nose into the pro sports tent, then what would be next, the Super Bowl?

Well, it remains doubtful that the Super Bowl soon will be carried by a cable network, but after this maiden NFL season on ESPN, that at least has become a real possibility and not rhetoric

In any event, ESPN specifically and the cable industry generally now is entitled to a small, private smile for successfully achieving a significant milestone, an immense accomplishment done modestly

—Steve Tuttle
Editor and Associate Publisher

Attachment No 9

Turner Network Television Plans
to "Siphon Major Events
From Free TV to Pay Cable

RADIO TELEVISION CABLE SATELLITE
Broadcasting Oct 12
Vol 113 No 15

Turner's TNT adds spark to Atlantic Cable Show

New basic cable network, planned for March launch, still needs board approval on the wish list major sports events including the Olympics Academy Awards Grammys, pageants

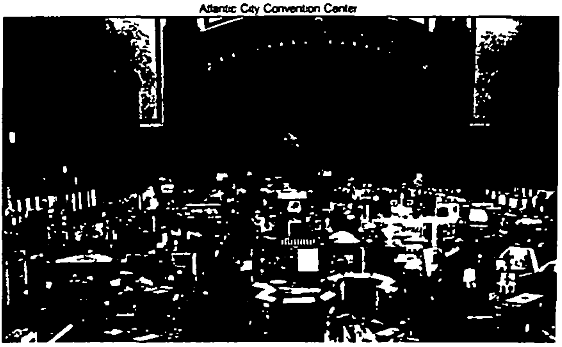
Ted Turner in a keynote address opening the Atlantic Cable Show revealed details about his planned basic cable network Turner Network Television which he said would be a cable-exclusive program service built around major television events The service which needs the approval of the Turner board which is scheduled to take up the matter at a meeting on Friday Oct 16 would be supported by both advertisers and cable operators

Turner s superstation WTBS(TV) Atlanta "has gone about as far as it can go " Turner said "I need to get subscriber fees so we can go to the next level " The fees he envisions would begin at 10 cents per month per subscriber in March 1988 and would increase to 20 cents in March 1989 He also said the network would carry 10 minutes of advertising an hour with three to four minutes turned back to the cable operator

The events Turner wants to go after include Major League Baseball the National Basketball Association NCAA basketball all the college football bowl games and associated parades the Olympics the Kentucky Derby the Daytona 500 the Indianapolis 500 the PGA U S Open golf the Masters the British Open Wimbledon U S Open tennis Miss USA Miss Teen USA Miss Universe the People s Choice Awards the American Music Awards the Kennedy Center Honors the Academy Awards the Tony Awards and the Grammys Turner s Good will Games would also appear on the new network

Turner made it a point to claim that making the new service cable-exclusive was his idea And he said his legal counsel has advised him that because TNT would be a start up service it would not run afoul of antitrust laws * * *

Atlantic City Convention Center



Media
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Turner sets TNT start in October

By JANET STILSON
Staff reporter

NEW YORK—Turner Broadcasting System hopes to launch Turner Network Television on Oct 3 with a 10 million to 15 million subscriber base

Gerald Hogan, president of TBS's entertainment network unit, is trying to nail down subscriber commitments in a series of teleconferences with the multiple cable system operator executives who attended TBS's meeting on TNT last week

Mr Hogan and Ted Turner, TBS's chairman and chief executive, are also talking to board members in an effort to get their approval of the proposal, including the Oct 3 kickoff

Representatives of about 10 of the country's largest MSOs attended the Turner meeting last week At least one, Tele-Communications Inc President John Malone, has given the network his full support

Others, such as Robert Miron, president of Newhouse Broadcasting, expressed some reservations

"It was an interesting presentation," Mr Miron said "Ted had some innovative program ideas"

He said some aspects of the plan, plus channel capacity considerations, will lead him to review the proposal "very carefully"

Turner's plans for a 10 million to 15 million subscriber base would be "by far the largest subscriber launch of a (cable) network," Mr Hogan says It would immediately make TNT eligible for A.C Nielsen Co ratings

That milestone, which some cable networks have taken years to reach, is vital in attracting significant advertiser interest.

TBS sources close to the plan say systems will not be charged a per-subscriber rate during the first year, but would pay 15 cents per subscriber in 1989, 20 cents in 1990 and 25 cents in 1991

Concerning the debut date, Mr Hogan says, "There are probably 20 different reasons why we chose Oct 3, but most importantly, the Olympics will be over"

A three-step programing strategy has been planned, he said, which will ultimately see the inclusion of high-profile programing "that drives new subscribers and enhances current customer satisfaction"

That has been the goal of Mr Turner, who told the Atlantic Cable Show in October that TNT would attempt to grab rights to such TV heavyweights as the Grammy Awards, the Olympic Games, "all of baseball" and "anything else we can think of"

Says Mr Hogan "Initially we'll rely on our library of acquired product But at this first stage we'll also be engaged in the development and hopefully the production of new programing"

That period, expected to last 18 months to 30 months, will be followed with a schedule integrating new, original programing

"But whether it will be breakthrough programing or not, I don't know," Mr Hogan says

The final step, about five years away, will see a prime-time schedule dominated with original fare—"250 nights a year would be original, including live sports," Mr Hogan says

In the battle for channel space on cable systems, TNT is expected to try to replace superstations in some markets #

Senator METZENBAUM Thank you very much, Mr Maltz
Our next witness is Wendell Triplett I will hold my questions until I have heard from this entire panel because we are running out of time Mr Wendell Triplett, Chillicothe, OH

STATEMENT OF WENDELL TRIPLETT

Mr TRIPLETT Thanks for the chance to testify, Senator It is greatly appreciated

Senator METZENBAUM Happy to have you with us, sir

Mr TRIPLETT I am here on my own behalf as a little guy trying to make a new UHF station in Chillicothe/Columbus go And also to plead for all new stations across the country that are either trying to exist in their very early phases or trying to build new construction permits who have recently been given to them by the FCC

We were a home shopper when we went on the air August 31 However, since January 4, we are a full, standard, independent television station We had to sell a radio station in order to get our programming, and that did not occur until December

My wife and I have undergone a living hell since the strikedown of must-carry on December 11, 1987 We are on three of the four cable systems in Columbus, having been taken off by Coaxial Communications Cable on approximately January 20 We are being carried by All American ATC out of Denver, Warner and Telemedia We are very appreciative to be carried by these three systems and would rather not comment on them due to the extreme sensitivity of the problems, sir

I will comment on Coaxial, since they have no intention of putting us back on, although we have offered consideration in the way of time for them to sell, assumption of any copyright liability They have additional promotional time for their programming, if they would like it They, the president and majority owner will not even meet with us to work out our differences They only want to exchange letters with much doubletalk and confusion to obscure any real truth on the issues between us

I would now like to comment on the damage being done to new stations and new construction permits all across the country

Senator METZENBAUM Who owns Coaxial, Mr Triplett?

Mr TRIPLETT The major owner is—it is a fairly closely held corporation The major owner is a gentleman who lives in Jay, NY, Mr Silverstein

Senator METZENBAUM Where?

Mr TRIPLETT Jay, NY That is upstate eastern New York

Senator METZENBAUM Is that the major cable company in New York?

Mr TRIPLETT It is one of the big ones Warner is the largest, having 77,000 current subscribers They have approximately 62,500 They are the second largest

Senator METZENBAUM Thank you

Mr TRIPLETT The Cable Act, as has been said here many times, they must be revisited The Government gave away the store

New stations cannot get any financing today, Senator None whatsoever You cannot get any existing working capital, nor can people build new stations that they have been construction permits from the FCC because of this must-carry problem

Many stations that are on are terrorized by the possibility of being taken off I have talked to them all the way from Riverside to Lowell, MA, to Florida New stations are held in bondage by cable today Cable's goal is to sell $5 billion in advertising by early 1990's It is pretty obvious why they do not want us new boys on the street

Stations on cable are locked out of the home As the NBC study showed, there is only 1 percent that have an A/B switch and only 10 percent ever look at over-the-air signals

Not being on cable completely undermines an independent station's morale If a station had a 2,000-foot tower in the middle of a market and it is not on cable, they will not get a decent market share to make it If we are on cable, we will make it fine, Senator If we are not kept on cable, we are simply going to die

Managers and owners of new stations are fighting for their survival which undermines their ability to manage their operations This hearing gives us hope, but it is only real if true action is taken quickly The time profile is a great problem for new stations If help is not received, some tremendous damage will be inflicted on these fledgling new businesses

I have approximated that 100 stations are affected, and I will complete my studies—being an old operational analyst from RCA And I think that there are $70 million in jobs a year are going to be lost I think there is $500 million in revenue if this problem is not fixed

Free local television will be dramatically affected along with diversity of views For example, Coelho mentioned 182 PBS stations were thrown off A couple more points, sir

Senator METZENBAUM Thank you very much, Mr Triplett

Our last witness today is Mr John Siegel, president of KBHK-TV, San Francisco

STATEMENT OF JOHN SIEGEL

Mr SIEGEL Thank you, Mr Chairman, for the opportunity to testify here today

Over the past few years the cable industry has radically changed from being a benign retransmitter of local stations to becoming a powerful producer of programming that competes with the local stations

For example, Mr Chairman, you have listed the financial interest in cable programming channels that TCI owns or controls Cable companies compete with local broadcasters for viewers while they control the access to the viewing choices in the home

Virtually, 100 percent of the cable systems in this country are local monopolies And when you combine the lack of competition and the power to control the viewing choices with a financial interest in the success of competing programming, you are left with a distorted marketplace that is far from consumer-preference driven

Even when must-carry rules were in effect, cable companies abused their gatekeeper power contrary to overwhelming evidence of consumer preference for the local stations' programming Only in an abusive monopoly climate can an entity reap higher and higher profits by not responding to consumer preference

Absent must-carry, the congressionally guaranteed compulsory license along with the lack of strict syndicated exclusivity provisions operate to enable cable companies to further distort the competitive process

Under the compulsory license, for virtually no cost cable companies regularly import distant television signals Often these stations air the same shows as the local station and often in the same time period

It can hardly be suggested that viewers desire the same programming to appear on two, three, or four channels But because cable companies compete for viewers and advertising revenue against local stations, it is to the cable's benefit to dilute the value of its competitor's programming

One cable system in San Francisco, United Cable, a TCI subsidiary, takes this unfair practice one step further They refuse to list KBHK in their cable guides with most of the other Bay Area stations, but they do list a distant UHF station from Sacramento which airs much of the same programming KBHK airs

Let me tell you a little about what my station has gone through in the last couple of years Years and years ago my station was San Francisco Cable Company's best friend We worked with them to help promote cable subscribership In exchange, we successfully unified our channel location to channel 12 on virtually all of the Bay Area cable systems

But as our historically good relationship based on interdependence became one of competition, things began to change In late 1986, we began to hear rumors of a marketwide cable channel repositioning plan to unify all cable and broadcasting channels in the Bay Area The plan had us slated to be moved to what we call "Siberia " This despite consumer preference for our programming over any other cable programming, and despite the fact that we were already unified

We first went to the various Bay Area municipalities to persuade them that they could protect local consumer preference But the cable companies stormed in wrapping themselves in the Cable Act, the first amendment, and threatened suit Obviously, the local municipalities were intimidated

Thereafter, we brought suit in State court alleging anticompetitive behavior and unfair competition We now have resolved our differences with the named defendant Viacom in that suit, but our cable position is fragile at best In fact, by testifying here today I fear retribution by cable companies in the Bay Area, especially TCI TCI and KBHK are at great odds, ever since they moved us in 1986 and inserted their owned and ad-supported channel in our place contrary to consumer preference

In conclusion, cable is an unfair competitor They reap higher and higher profits contrary to clear consumer preference Congress should launch an investigation of its own into cable's concentration of power It should look into amending the Cable Act to protect consumers and local broadcasters from cable's anticompetitive behavior It should tie the compulsory copyright license to must-carry and syndicated exclusivity And it should prevent channel shifting without a clear-cut showing of consumer preference

Thank you, Mr Chairman

[The prepared statement of Mr Siegel follows]

TESTIMONY OF JOHN SIEGEL,
PRESIDENT OF KBHK, SAN FRANCISCO,
BEFORE THE SENATE COMMITTEE ON THE JUDICIARY,
SUBCOMMITTEE ON ANTITRUST, MONOPOLIES AND BUSINESS RIGHTS
MARCH 17, 1988

Thank you, Mr Chairman, for inviting me to appear before this distinguished Subcommittee My name is John Siegel I am President of San Francisco independent T V station KBHK I also serve on the Board of Directors of KBHK's parent company, United Television, Inc , a publicly traded company Chris-Craft Industries, another public company, controls 51 percent of United Television's stock and I am a Vice President of Chris-Craft

KBHK is the number 2 independent T V station in the competitive San Francisco television market In terms of audience appeal (i e , consumer acceptance) KBHK is the fastest growing television station in the market

KBHK is a member of the Chris-Craft/United Television group of television stations This group is the eighth largest broadcasting group in the U S and the largest group west of the Mississippi

I <u>OVERVIEW</u>

The cable industry has changed dramatically in recent years It can no longer be dismissed as a friendly group of "mom and pop" entrepreneurs trying to improve television reception in a few isolated communities for the benefit of consumers Today, more than half the households in America receive their television programming through a cable The cable industry expects to be a $15 billion industry by 1991 And for this year, cable's largest company, TCI, is projecting a $1 billion cash flow

As the C-SPAN cameras make us all aware, cable television programming is no longer limited to broadcast transmissions, but instead a multitude of competing program services The alphabet soup of TDC, CNN, TNT, MTV, and CVN pervades the industry Indeed, the expansion in the scope of the cable industry is matched only by the consolidation in its ownership A few media behemoths now dominate the industry This week's Multichannel News headline uses "Godfather" to describe TCI

The sad truth is that the modern cable industry represents the emergence of the largest unregulated monopoly in this country Most cable operators have a de facto monopoly within each of their franchise communities Notwithstanding claims to the contrary, there really is no effective competition to these cable operators If you want clear broadcasting reception along with the variety of programming cable television has to offer, there is, for all practical purposes, just one player in virtually every town

Today, the cable industry is taking advantage of an unparalleled, favorable, legal environment endangering the continued viability of free, over-the-air television in this country and blatantly riding roughshod over the wishes of consumers Ironically, deregulation with its usual pro-consumer motivation, when applied to the cable industry has resulted in just the opposite effect Cable operators who now have financial interests in the cable programming they carry have strong economic incentives to conduct their business irrespective of demonstrated consumer preference and to the detriment of the broadcast industry Congress needs to take immediate steps to restore a "level playing field" on which local broadcast stations and cable can fairly compete

II ANTITRUST/COMPETITIVE FRAMEWORK

A Cable Companies are Competitors of Local Broadcasters

Today, cable companies not only own the cable delivery system, but also own numerous programming channels For example, TCI, the largest cable company, owns or has a significant interest in Turner Broadcasting (CNN) (WTBS), Cable Value Network (Homeshopping), The Discovery Channel, Black Entertainment, American Movie Classics, Tempo, Netlink U S A, X Press, QVC and Fashion Channel

Cable companies compete with local stations to capture the local audience's viewing attention (consumers) Based on that viewing level, what we call "ratings , cable companies compete with local broadcasters for national and local advertising revenue Because many cable companies may operate in a single geographic television market, they often enhance their competitive efforts in that market by banding together to sell, in concert, advertising on the cable channels they jointly carry on their respective systems in that market These combinations are called "interconnects '[1] In short, cable companies control the access to the viewer while having financial interest in the delivery of competitive programming

B The Cable Companies Possess Enormous Market Power Over Television Viewers and Broadcasters

Virtual 100 percent of the cable systems in the cities and towns of this country are local monopolies Less than one percent of the communities in the United States have overbuilds (that is, more than one cable system), and even then, almost none of those communities has cable systems which actually compete with one another in the same neighborhoods of that community As a result of its gatekeeper" position, each local cable system has the power to decide what the viewers in that community can and cannot receive on their T V set without regard to consumer preference And, through their channel placement practices, cable companies, regardless of consumer preference, decide

1 Interconnects are important because they function as an economic deterrent to overbuilding in a cable company's neighboring area currently being served by a partner in the interconnect

how convenient or inconvenient it will be for those viewers to find the programming of a competing local broadcaster on their cable system

To the extent that there is no competition to the cable company and given its gatekeeper status, the marketplace is distorted Viewers use the cable as a convenient means to gain reasonably clear access to local over-the-air programming as well as viewing the other cable offerings Nevertheless, while 50 percent of the television households in America now rely on cable, at any given time the vast majority of those cable viewers are watching the over-the-air broadcast channels As time has shown, cable companies prefer to eliminate or disadvantage their competitors by exercising their gatekeeper power, rather than having to compete against them in the marketplace

C Even With Must-Carry, the Cable Companies Have an Established Record of Misusing Their Power to the Detriment of Consumers

Even while the must-carry rules were in effect, cable companies began to reshuffle channels of local broadcasters This continues despite clear consumer preference for the local broadcaster's fare over the cable channel which replaced it I know of no channel repositioning that resulted in anything other than a local station being moved out by a lesser-viewed cable program The local station was either dropped or moved to a higher channel Consumers who were accustomed to viewing that local station on its prior channel were disadvantaged or even displaced if their T V set could not receive the higher channel on which their preferred programming now appears

Now that TCI has given its go-ahead to the new TNT Channel, local broadcasters fear for their very existence Will they be moved or replaced to make room for this new TCI program venture? An overwhelming economic incentive exists for the cable operator to replace the local station from which it derives no direct revenue, with either a cable channel in which it owns an equity interest, a cable channel on which it sells advertising, or a cable channel from which it derives money or other forms of direct compensation In short, the cable companies as local monopolists, can afford to place consumer wishes regarding programming and dial positions second to those companies' own direct economic interests

Often the cable companies publicly rationalize their channel positioning decision based on consumer surveys" -- surveys which are of highly dubious reliability and often are contrary to readily available consumer preference evidence such as existing rating service data provided by Nielsen and Arbitron

Cable's cavalier channel repositioning efforts reached their height when some cable companies in effect auctioned channel position to the highest bidder among cable networks It worked like this A cable network would say, 'our programming normally costs X If you move us to channel 2, we will charge you X - Y or less The distorted marketplace gives cable companies not only the incentive but the economic power to do this But there is clear injury to competition when a cable system uses its monopoly power and control over the delivery system to disadvantage its competitor in the face of clearly demonstrable consumer preference for the local broadcast station Regardless of consumer preference, cable companies prefer to position the cable programming in which they have a financial interest on the lower tier (2-13) Typically, they end up relegating many local broadcasters to "Siberia" on the television dial

On occasion, cable companies 'offer" to move local broadcasters to cable channel positions which match the broadcasters' over-the-air designations For some stations this may be acceptable, but for others a move of this nature is tantamount to being dropped from the system entirely For example, some cable companies like TCI do not automatically give subscribers with second sets a converter box when they hook up that second T V set If the second set is not cable-ready, and virtually all are not, and if the station was moved out of the 2-13 channel range, it is very unlikely that that station can be received on that second set

Companies such as TCI turn the argument on its head when they attack the local station for demanding better positioning than its over-the-air dial position We see it differently We are not demanding an upgrade, just don't downgrade us if consumers prefer what we do over what you own That is, unless TCI can show reliable consumer preference data for the programming it seeks to use to unseat a local broadcaster from its long-held channel position, TCI does not have the legal right to act contrary to consumer preferences in the environment of a distorted, monopolistic marketplace wherein it derives a financial benefit from uprooting the local stations

By definition, such a move is not in the consumer interest if consumers preferred the uprooted local station to the newly installed cable channel Such behavior is in the interest of the cable company monopolist, not in the interest of consumers

D With the Elimination of Must-Carry and Pursuant to Their Anticompetitive Agenda, Cable Companies Will Now Use "Editorial Judgment" as a Subterfuge to Unfairly Compete Against Local Broadcasters

Misconduct occurred during the must-carry years With the elimination of must-carry, anticompetitive behavior on the part of the cable companies will accelerate to the detriment of clear consumer preferences and to the detriment of the local broadcasters The delivery system will be used by cable companies as an anticompetitive device which need not be responsive to consumer wishes while it anomalously reaps ever higher and higher profits Only in an abusive monopoly climate can an entity earn more and more money not being responsive to consumers

A broadcaster is largely powerless to fight the cable operator's decision to favor cable channel programming over broadcast programming The broadcaster cannot realistically expect viewers to forego cable service to protest the deletion of a single broadcast station First the cable companies went after the public stations Now they are taking on the local stations one by one And even when viewers do object, cable companies do not respond They say, "Too bad, it's our system " Absent government regulation, the cable operator's monopoly position allows it to maximize profits while offering a less than optimal service to the viewers

Significantly, one means that local stations might use competitively to maintain or entice carriage by a cable system on an attractive channel is for the local broadcasters to offer exclusive programming which consumers/subscribers would want to see But the compulsory copyright law which Congress enacted, especially without strict syndicated exclusivity, has deprived local broadcasters of this most important competitive tool

III COMPULSORY COPYRIGHT -- ELIMINATION OF SYNDICATED EXCLUSIVITY -- OVERTURNING OF MUST CARRY AND THE 1984 CABLE ACT HAVE CREATED AN IMBALANCE ENABLING CABLE TO PROFIT CONTRARY TO CONSUMER WISHES AND TO THE DETRIMENT OF COMPETITIVE FORCES AND THE BROADCASTING INDUSTRY

The 1976 Copyright Act and the 1984 Cable Act (together with the elimination of the FCC's syndicated exclusivity and must-carry rules) have left a dramatic imbalance in the respective rights of broadcasters and cable operators Congress created cable's compulsory copyright license in 1976 to assist the fledgling industry's access to programming at a time when the cable industry argued it could not afford to negotiate for or acquire programming on its own Instead of having to negotiate for this valuable programming, cable was given the statutory right unilaterally to appropriate broadcast programming in exchange for relatively trivial payments With one company projecting a 1988 cash flow of $1 billion, this special copyright treatment makes no sense today -- the cable industry surely has the resources to bargain for its programming like any other copyright user

The operation of cable's compulsory copyright license is particularly harmful to broadcasters because, under current conditions, it facilitates cable's importation of duplicate programming without regard to licensing agreements negotiated between program suppliers and local broadcasters Television stations today routinely find that they have spent millions of dollars securing the exclusive right to show a syndicated program in their respective communities, only to discover that the local cable operator is importing several distant signals showing the exact same programming, often in the same or adjacent time periods Certainly it cannot be said that viewers prefer to see the same programming on different channels Yet, cable has an incentive to import this duplicative programming By doing so it fractionalizes the local station's audience and thereby causes the local station to receive less revenue That leaves more revenue for cable to go after Furthermore, the fractionalizing of local station's audience will result in lower ratings for that station As a result, traditionally low cable ratings will by comparison look slightly more competitive Again, the delivery system is being manipulated and used as an anticompetitive device

Cable's ability to duplicate the programming of local stations is not something cable bargained for Rather, it is a Congressional gift

Cable is able to secure local exclusivity for the programming it places on cable channels, local broadcasters should have that same right So long as that right is denied, local broadcasters are denied the ability to effectively compete with cable The compulsory copyright and lack of a strict syndicated exclusivity provision enables cable to circumvent privately negotiated program contract exclusivity provisions and undermine the efforts of local broadcasters to make themselves more attractive and competitive There no longer exists a satisfactory rationale for this disparate treatment of competitors operating within the same marketplace, especially in light of the damage it does to local broadcasters who continue to search for creative ways to remain competitive while bringing diversity to the viewing public

The operation of the compulsory license is especially damaging to local broadcasters because, absent the FCC's old must-carry rules, cable systems can completely bypass local broadcast stations and rely instead on imported signals There are no rules in effect today requiring the carriage of local broadcast signals, even as a condition to compulsory copyright licenses Thus, when a cable operator finds it in its own financial interest to drop a local station, there are no readily available legal means to prevent it from doing so

This problem is exacerbated by the cable industry's insistence that congress intended in adopting the Cable Act, to preclude interference, by either the FCC or local franchise authorities, regarding <u>any</u> cable-related decision

In court case after court case, cable continues to attempt to escape whatever regulatory burdens it still faces on the grounds of the First Amendment

When faced not only with proof of outrageously predatory conduct by a would-be competitor in its market, but also with objections from the franchising authority and the viewing public that it was supposed to serve, TCI Cablevision, in a celebrated court case, had the audacity to argue that its predatory conduct in trying to exclude competitors and ignoring consumer wishes was immunized by the First Amendment because TCI was engaging in "speech" activity Both the jury and the trial court rejected that claim and TCI ended up paying more than $40 million in damages

Cable companies also rely on two appellate court decisions involving must-carry to argue for First Amendment immunity for any and all of their activities related to program carriage, yet neither of those decisions even addresses -- much less decides -- issues of anticompetitive behavior by cable companies

Cable companies around the country have attempted to convince courts they are even immune from state antitrust law and consumer protection statutes For example, only a few weeks ago a case brought by West Virginia addressed the threshold Cable Act preemption issue in the context of a jurisdictional motion to dismiss West Virginia claimed that Capitol Cablevision, an American Television and Communications Corp ("ATC") subsidiary, violated West Virginia consumer protection and state antitrust laws ATC claimed the Cable Act preempted state law Fortunately, this judge disagreed

Meanwhile, other trial courts have begun to severely restrict the powers of local governments to provide some check on the market power of cable companies One court even went so far as to state that the purpose of the Cable Act was to foster the growth of cable -- as if cable were still a fledgling industry

Contrary to viewer preference, consumer interests and antitrust and unfair competition statutes, cable companies will use a combination of the Cable Act, court decisions and the First Amendment to assert the proposition that they have carte blanche to do whatever they want regardless of the injury to the consumers and the competitive process

Congress needs to focus its attention on the cable companies and recognize that cable companies act out of greed and not in the public interest or the consumers' interest

Our experience, which follows, is both not unique and unique Not unique insofar as the treatment we have received from cable companies Unique in that we have elected to fight, to commit the necessary resources, and to draw the line Fortunately, we can afford it Other stations cannot and consumers are being manipulated by a cable shell game of dropping and moving stations contrary to clearly demonstrable consumer preferences

With the elimination of must-carry and the introduction of new cable channels coming on each week begging for carriage, it is only a matter of time before wholesale dropping of local stations begins

IV KBHK'S CABLE RELATIONSHIP

Long before it became "fashionable" for a local broadcast station to work with cable companies, KBHK in the 1970s recognized that local broadcasters and local cable companies shared a symbiotic relationship San Francisco, known for its hills, was one of the early high cable penetration television markets During this period, cable merely retransmitted the existing television stations' signals And, in this period, Bay Area cable companies and KBHK were not competitors

KBHK, however, was carried on an array of different cable channels throughout the Bay Area A decision was made to try to persuade cable companies to move KBHK to one unified television market-wide cable channel Cable 12 was chosen even though on many systems KBHK was carried on lower numbers Also, at this time most cable systems were limited to 12 channels KBHK believed that if it could successfully unify itself on virtually all Bay Area cable systems, it could advertise its over-the-air channel with its cable channel and over time develop a dual identification

To achieve this goal, KBHK hired a full-time employee This person sought to educate cable operators as to how popular KBHK's programming was with viewers From time to time KBHK promoted the benefits of cable subscribership KBHK often paid to advertise local cable companies on billboards KBHK also bought technical equipment for cable companies to effectuate the station's move to channel 12

To unify KBHK on channel 12 was no simple task There were more than 65 Bay Area communities then served by more than 40 cable companies Nevertheless, unification of KBHK on virtually all Bay Area cable systems was achieved Almost 90 percent of all cable subscribers in the Bay Area received KBHK on channel 12

With this level of success, KBHK launched a massive identification campaign to identify itself as "Bay Area Cable 12 " KBHK became so identified as "Bay Area Cable 12" that this later became a registered tradename of KBHK

In the early 1980s cable companies began to realize success in offering cable exclusive programming This opened the way to competing for viewers and advertising revenue against such local stations as KBHK This changed their historical relationship with broadcasters from one of interdependence to one of being competitors for viewers, advertising revenue and syndicated programming

In late 1986, KBHK began to hear rumors about a market-wide cable channel repositioining plan by all cable companies in the market Further investigation proved that the rumors were valid, and that KBHK was slated to be moved from its long-established Channel 12 slot to an undisclosed position way up the dial

While KBHK obviously is aware of the benefits of channel unification, KBHK was already unified Nevertheless, we were destined to be moved to "Siberia " This, despite the fact that KBHK is a very heavily viewed station Viewed much more than any cable channel that might be offered to the public as a replacement

Years of unification, advertising, Bay Area Cable 12 identification, and providing the public with preferred programming, were about to go down the drain Moreover, viewers who preferred to watch us on Channel 12 might not be able to continue to view us if we were moved to a channel their particular television set could not receive

But the most bizarre aspect of all this is that, in the name of market unification, cable companies were intent on uprooting KBHK which was unified <u>already</u> The only reason for doing this was obvious It was for cable companies' economic benefit and not for the benefit of consumers, who had clearly demonstrated they prefer our programming, and who have long expressed a preference for the popular local stations to be grouped together on the low end of the dial

In the face of this market-wide unification attempt, KBHK first tried to impress upon 25 local municipalities that they,under their various franchise agreements, could protect local consumer preferences as to channel placement The cable companies with their expensive lobbyists and lawyers stormed the City Halls waving the Cable Act, First Amendment and threats of suits against the cities if they did anything of the sort The cities were clearly intimidated by the cable companies' efforts Thereafter, we examined our options and, ultimately, KBHK elected to bring a suit in state court for injunctive relief alleging violations of state consumer protection statutes in the form of antitrust violations and unfair competition violations

At this time KBHK and the named defendant in that suit have resolved our respective differences and are attempting to work together in a productive manner exploring ways to enhance the symbiotic aspect of the relationship that still exists

While KBHK's cable channel shifting circumstances appear to be headed in a productive direction, the problems are far from over In late 1986, the world's largest cable company, TCI, notified us that we would be moved from Channel 12 to different, higher channels on their six Bay Area systems By January 1986 we were moved on all six of these systems On five of the six systems TCI's owned Discovery Channel took our place TCI owns a substantial equity interest in this cable programming and also derives advertising revenue from the commercials sold in the program This move was contrary to demonstrable viewer preference and TCI admitted to throwing out more than 90 percent of the results of its own "consumer survey" on what viewers wanted regarding channel placement As of a month ago, we began to receive viewer complaints from one TCI system that the channel they moved us to often experiences cable technical interference difficulties

TCI has for the last year refused to address itself to this matter and currently we are exploring all of our options We are damaged by TCI's behavior which is not based on consumer preference, and we continue to suffer harm While viewers may not even be able to receive the programming they prefer, TCI nevertheless gets richer and bigger

In the Bay Area, KBHK is the only local station that buys advertising space in the multiple cable companies' cable guides

After we brought our lawsuit and without naming United Cable or Gill Cable to that suit, both companies declined to accept our advertising Moreover, United Cable, which imports a distant UHF signal from Sacramento which often duplicates much of the same programming KBHK airs, lists the Sacramento station in its Bay Area cable guide, but does not list KBHK This is true even though KBHK enjoys a far higher viewing level than that imported signal

Both United Cable and Gill Cable are TCI companies or will become TCI companies by 1991

Cable companies are motivated by profit So are local broadcasters. The difference is that because they are monopolists, cable companies have found ways to enhance their profits without being responsive to the consuming public while at the same time injuring their competitors

V CONCLUSION AND RECOMMENDATION

Cable is a competitor of local broadcasters It uses its monopoly power over the delivery of programming to unfairly compete with local broadcasters for viewers (which translates into competing for advertising dollars) This results in an anomalous economic gain to the cable companies while consumers are denied their viewing preferences Consumers and local broadcasters are being harmed by cable companies' unfair competition

Congress needs to specifically

A Investigate cable's increasing concentration of power at both national and local levels and how it abuses this power

B. Amend Cable Act where necessary to protect consumers and local broadcasters from cable's anticompetitive and predatory behavior.

C. Tie the compulsory license to must-carry and syndicated exclusivity.

D. Prevent channel shifting without a clear cut showing of consumer preference.

[John Siegel submitted additional documents with his testimony which may be viewed in the Antitrust, Monopolies and Business Rights Subcommittee upon request]

Senator METZENBAUM Thank you, Mr Siegel Mr Siegel, if you hear of a scintilla of evidence of retribution against you, do not call my staff, call me

Mr SIEGEL Thank you, Mr Chairman

Senator METZENBAUM I want to know about it the next day

Mr Chapman, how realistic is the possibility that in the next few years events like the Rose Bowl or the World Series or the Academy Awards, that millions of Americans now can watch on free TV, will become available only over cable?

Mr CHAPMAN Mr Chairman, I think the possibility of that happening is very great I would see it first to take place probably in sporting events Had it not been for the bidding turning out the way it did for the Sunday night football, it could very well have been on pay cable this year, the NFL And that was a 3-year contract and you may very well see when that contract is up, I would see extensive negotiation for those rights by cable

Mr MALTZ Mr Chairman, if I may respond to that question as well? A president of a rather large broadcast company who was trying to bid for the broadcast right for those Sunday night games called me and said he was being discouraged from bidding And he knew that I was a friend of an owner of an NFL team, would I make a call and find out what the problem was?

I made that phone call and I was told that those Sunday night games were designed because people would pay little, scant, attention to a Sunday night football game It was their chance to get on cable They did not want broadcasting to be involved regardless of cost It was the beginning of movement toward pay TV Even if it took 5 or 10 years, this was the beginning

Senator METZENBAUM The Chair has asked the antitrust division of the Department of Justice to inquire into the matter of the NFL games being—the ESPN contract with the NFL The Chair has very serious concerns about that The Chair very well may expand the area of that inquiry into other sports events as well

Mr Maltz, you attach a number of press clips to your testimony reporting plans that a number of Ohio cable companies had in late

1986 to drop a number of independent and public television stations Did the announced drops actually occur? And do you know what impact that had, if it did occur, on the stations involved?

Mr MALTZ The announcement was made and it was carried in all the newspapers and there was a tremendous response by citizens But apparently there was no response by the local cable operator I personally made a trip to Denver to meet with Mr John Malone, chairman of TCI, and persuaded him to leave well enough alone

So, in fact, it did not occur, but they did make the announcement that it was going to occur It was our station, another station or two in Cincinnati, a PBS operation and several Dayton stations They were going to bring in distant signals such as WGN in Chicago

Senator METZENBAUM Some have raised the question as to whether or not the free TV stations should be paying cable to carry your signal Is that an alternative?

Mr MALTZ Well, sir, let us put it this way At the present time, we are paying millions of dollars in copyright fees They are carrying our programming and paying nothing It seems to me that is a one-way road We cannot continue in business like that

I have been advised by one cable operator, "it is only a matter of time before we are going to charge you for carriage "

Look at it another way The owners of the software companies such as ESPN and the other program services do offer a discount on their charges to the local hardware dealer, the local cable operator, in exchange for better program location, such as the lower tier of channels Since we are giving our service away for nothing, how can we offer a discount?

Senator METZENBAUM Mr Triplett, how much of your programming is of local interest? Have you done anything——

Mr TRIPLETT We have provided a considerable amount of local sports like high school basketball in Columbus, going from a different game every week to give coverage of the city, plus melting Chillicothe into that matter And we also did a football game last fall This coming fall we expect to do a full football schedule locally and a full basketball schedule locally

We are commencing a local newscast in about 1 week As you probably know, sir, it is very expensive for a new entity to start news right away We are initiating that in about 1 week

Senator METZENBAUM Since you were dropped by Coaxial Cable, have your ratings dropped?

Mr TRIPLETT I am sure they have, sir And an even more deleterious effect is with your advertisers Because when you are dropped from that many or that large a percentage, about 30 percent, it is a serious problem out on the street for the sales people

Senator METZENBAUM How many viewer complaints, Mr Siegel, have you received since the TCI cable systems in the Bay Area moved you to a different number?

Mr SIEGEL Quite a few

Senator METZENBAUM Have your ratings been affected?

Mr SIEGEL The ratings have been affected There have been quite a few consumer complaints, both telephone calls and written complaints And only last month, Mr Chairman, I received a tape from a consumer/viewer in Redwood City wherein he says that he wanted us to know that our signal is being degraded on this newly moved channel that TCI moved us to

In other words, the channel that they moved us to, the signal is degraded That TCI has not responded to correcting this problem, and that basically TCI has sloughed him off He sent me a tape We have herringbones all over our programming

Senator METZENBAUM I want to thank this panel for cooperating with us and all the members of the panels You know, I have been here long enough—I came here from the business world And I think from the day I came here until today I constantly here the plaint of the business community to get the Government off our backs, keep Government out of free enterprise I was in the business community and I understand that approach

But this hearing today has pretty well convinced me that unless the industry itself does some things to correct its own activities and to get its own house in order, that the only possible solution is for Government to intercede And I believe, as I said earlier, that unless that does occur Government will intercede and the Chair of this committee will not be bashful in providing that leadership in order to facilitate such intercession

I would hope that would not be necessary Within 60 days we will take another look at the industry, whether by public hearing or on our own, and we will arrive at a conclusion at that point as to whether or not we believe that legislation is an appropriate action to take

I am very much disturbed at the threat to the free television industry, at the increase in rates that have occurred in some areas which would be appear to be excessive, and to the unavailability of product to those who are in the wireless TV end of the industry This is not the conclusion of this subject today, it is only the beginning

[Information for the record follows]

ML

MICHIGAN STATE UNIVERSITY

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March 8, 1988

Eddie Correia, Esq
Senate Antitrust Subcommittee
308 Hart Senate Office Building
Washington, D C 20510

Dear Ed

Pursuant to our telephone conversation earlier today, I am enclosing herewith the Adams/Brock article on recent developments in the video entertainment industry

I shall be pleased to have you include this article in the record of the hearings which Senator Metzenbaum plans to conduct on the subject, starting March 17

With best wishes to the Senator and you, I am,

Sincerely yours,

Walter

Walter Adams
Distinguished University Professor

WA/gt

enclosure

Los Angeles Times

Sunday, November 22, 1987 / Part IV 3

Hollywood Independents Start to Feel the Squeeze

By WALTER ADAMS and JAMES W BROCK

The threat of monopoly is once again casting its shadow over the entertainment industry. Major players in the industry—movie studios, theaters and the cable, pay and broadcast television networks—are caught up in a maelstrom of mergers and acquisitions, combining operations at the industry's three pivotal stages production, distribution and local exhibition

Consequently, vertically integrated giants have been established with the market power to thwart competition The big companies can make it difficult both for independent producers to market their work and for independent exhibitors to get these productions It is the kind of monopoly power that the Supreme Court in 1948 decided to neutralize by ordering the Big Five (Paramount, Loew's, RKO, Warner Bros and 20th Century-Fox) to divest either their production-distribution operations or their exhibition outlets

Today, the 1948 defendants are intent on re-establishing their control of the full breadth of the industry The top studios—which account for more than 80% of film production and distribution—are voraciously gobbling up theater chains Over the last two years, motion picture studios have acquired 14 theater chains, representing 4,224 screens.

For example, Universal Studios purchased controlling interest in Cineplex-Odeon—one of the largest theater circuits in North America, and Cineplex, in turn, has purchased the RKO Century, Septum and Essaness chains, among others. Other major studios are doing the same The recent turbulence in the stock market may put a temporary damper on this trend—the recent collapse of the proposed merger of United Artists Communications and United Cable Televi-

WALTER ADAMS *is a professor of economics and past president of Michigan State University* **JAMES W. BROCK** *is associate professor of economics at Miami University (Ohio) They are co-authors of "The Bigness Complex," which was published this year*

sion is a case in point—but the long-term outlook is unchanged

The studios also are acquiring local television stations Fox bought Metromedia—the nation's largest chain of independent stations—as well as WXNE in Boston Indeed, under the guidance of Rupert Murdoch, Fox is establishing a fourth national TV network For its part, Universal has purchased TV "superstation" WOR, which reaches 8 4 million subscribers via 1,400 local cable-TV systems In quick order, movie companies have come to own stations reaching an estimated 30% of the nation's TV homes

Furthermore, movie companies now dominate the production of programming for broadcast television Last year, the top studios accounted for 52% of all prime-time programming carried by the networks and 45% of all syndicated television programs

The story is similar in cable and pay TV Movie companies operate local cable systems. (Warner is the nation's sixth-largest operator of multiple cable systems nationally) They also have substantial financial interests in cable programmers such as HBO, USA Network, Nickelodeon and MTV that distribute viewing fare to cable systems And they have struck agreements to exclusively supply movies and programs to cable programmers and operators

The movie firms are not alone in their frenzied efforts Local cable-TV systems are being taken over and merged under centralized national control According to Michigan State communications professor Barry Litman, the nation's largest cable system operator, Tele-Communications Inc of Denver, has increased its empire from 1 3 million subscribers in 1981 to more than 7 million today The combined share of the top two multiple operators doubled between 1982 and 1986 At the present rate of consolidation, the five largest cable operators may control nearly half the business by 1990—up from 29% in 1982

Meanwhile, cable operators are also getting into program production and distribution For example, Tele-Communications has acquired a sizable stake in Turner Broadcasting For its part Turner—which produces and distributes Cable News Network and other cable programs—has acquired MGM

The TV networks are playing the game too CBS is a part owner of HBO, while Capital Cities/ABC operates ESPN In addition, the networks are demanding a relaxation of Federal Communications Commission rules limiting their ability to produce programs for their approximately 600 local affiliates

Pattern Is Emerging

Finally, an intricate pattern of cross-media combination is emerging—a pattern that cuts across the entertainment field and binds it tighter For example, the Columbia Pictures unit of Coca-Cola, CBS and HBO joined in 1982 to launch Tri-Star Pictures, a film production venture HBO was assigned exclusive rights to exhibit Tri-Star movies on pay TV, while CBS got exclusive rights to broadcast Tri-Star films on network TV (Now there are even bigger plans for Tri-Star Coca-Cola announced in September that it would fold its Columbia Loew's Theaters and Coca-Cola Television interests into Tri-Star, which will be renamed Columbia Pictures Entertainment.)

In sum, we are witnessing the re-linking of production, distribution and exhibition and the concentration of power across the whole spectrum of entertainment among fewer firms

Problem May Worsen

Once again, this raises the vexing vertical monopoly problems of a half century ago· What will happen to the ability of independent producers to compete as distribution channels and exhibition outlets are constricted and concentrated in the hands of a few corporate giants? What will happen to the competitive position of independent exhibitors (theaters, local TV stations and local cable operators) as production, distribution and programming are concentrated in the hands of those same giants? Will competition be undermined as it was 50 years ago? And what will happen to the diversity and creativity of viewing fare, when a handful of vertically integrated firms dominate all these fields?

The outlook is not reassuring The National Cable Television Assn charges that "the Hollywood studios have seemingly deprived independent theater owners of the theatrical releases they need to survive," that they "have begun to collaborate among themselves to jointly operate theaters and to jointly decide which theaters get their film products," that "independent film makers are virtually shut out by the major studios from distributing their films to neighborhood theaters" and that independent television stations "have been injured by Hollywood's hardball tactics."

For its part, the Motion Picture Assn. of America voices its alarm that "extraordinary power wielded by the largest [multiple-cable owners] has created serious disruptions in the program supply marketplace that will only grow worse as the growth in cable ownership concentration continues."

Of the efforts by the TV networks to move into program production, MPAA President Jack Valenti warned. "If you turn these companies loose, they're going to organize a monopoly"—a warning also sounded by independent TV stations.

Perhaps, these charges and countercharges underscore the central problem of vertical monopoly What if *all* of them are correct?

87-568 0 - 88 - 24

ATTORNEY GENERAL
CHARLIE BROWN

March 15, 1988
Contact. Marc Dann
304/343-8800

Statement

by

West Virginia Attorney General Charles G Brown

Today, West Virginia Attorney General Charles G Brown announced he is forming a multistate antitrust task force to investigate anticompetitive practices in the market for satellite delivered programming General Brown made the announcement in Washington, D. C. where he was attending meetings of the National Association of State Attorney Generals (NAAG) from the Association headquarters.

General Brown chairs the NAAG Antitrust Committee where he has been a leader in pursuing vigorous enforcement of antitrust law. The task force assembled by General Brown includes five states: West Virginia, Ohio, Texas, New York and Maryland.

POST OFFICE BOX [illegible]
CHARLESTON, WV [illegible]

General Brown hosted a workshop meeting in the United States Capitol Monday night, March 14 The meeting was attended by Attorney Generals and staff from several states as well as key Congressional staff involved in upcoming cable television hearings

"The workshop provided an opportunity for us to discuss whether there is adequate competition among cable, wireless cable, and other retail distributors of satellite-delivered programming," General Brown said.

General Brown commended Senator Howard Metzenbaum (D-OH) for holding antitrust hearings on this subject in Washington, D C on March 17, 1988 He also noted the leadership Senator John Kerry (D-MA) has exercised in investigating anticompetitive practices in the industry, such as recent wireline exclusivity proposals by programmers affiliated with big cable interests.

Last year, General Brown brought an antitrust action against a local cable television company operating in the State Capitol of Charleston. In the future, General Brown plans to develop an effective state-level strategy through his multistate task force and work closely with Congress as it addresses problems with the cable television industry

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March 16, 1988

The Honorable Howard M Metzenbaum
Chairman, Anti-Trust Subcommittee
Senate Judiciary Committee
Room 226 Dirkson Building
Washington, D C

Dear Chairman Metzenbaum

On behalf of the Trinity Broadcasting Network, National Minority TV, Inc , All American TV, Inc , and Community Educational Television, Inc , I am enclosing their Joint Comments in connection with the March 17, 1988 hearing deliberations of your Anti-Trust Subcommittee The commentors are nonprofit operators of independent UHF television facilities and their comments explain the anti-competitive, unfair and monopolistic activities of cable system operators, and the detrimental impact such activities have on free television, due to the District of Columbia Circuit Court's invalidation of the FCC's must-carry rules

It is respectfully requested that these comments be incorporated in the Subcommittee's written record

If any questions should arise please contact this office

Respectfully,

Colby M May

CMM gmcB06/B78
xc Nina Laury (308 Hart Building, Hand Deliver)
Mrs Jane Duff
Dr Paul F Crouch
Cruz S Arguinzoni
John DeS Casoria

M E M O R A N D U M

TO: THE HONORABLE HOWARD M METZENBAUM, CHAIRMAN, OF THE ANTI-TRUST SUBCOMMITTEE OF THE SENATE JUDICIARY COMMITTEE

FROM: UHF TELEVISION BROADCAST OPERATORS TRINITY BROADCASTING NETWORK, NATIONAL MINORITY TV, INC., COMMUNITY EDUCATIONAL TELEVISION, INC. AND ALL AMERICAN TV, INC

RE: JOINT COMMENTS ON THE MONOPOLY OF CABLE TELEVISION SYSTEMS AND THE DEMISE OF INDEPENDENT FREE TELEVISION

DATE: MARCH 17, 1988

These are the joint comments of the Trinity Broadcasting Network (Trinity), National Minority TV, Inc (NMTV), Community Educational TV, Inc (CET), and All American TV, Inc (All American) (jointly, Commentors), all of which are nonprofit organizations operating independent UHF television facilities throughout the United States Trinity and All American operate 12 and 4, respectively, full power independent television stations These independent stations provide family oriented and religious programming with significant amounts of public affairs, informational, and public service programming [1]

CET operates three noncommercial television stations, and provides educational, informational, public affairs, public service, and family oriented and entertainment programming [2] NMTV is constructing its first television facility in Odessa, Texas (KMLM-TV) NMTV and All American are minority controlled corporations

As operators of commercial and noncommercial television facilities, Commentors have experienced first-hand the far reaching and devastating impact caused by the effective demise of the "must-carry" rules in the wake of the District of Columbia Circuit Court's twin decisions in <u>Quincy Cable TV, Inc v FCC</u>, and <u>Century Communications Corp v FCC</u> [3] Prior to the Court's ruling in <u>Quincy</u> Federal Communications Commission Regulations for over 25 years had required cable systems to carry all television stations licensed to communities within 35 miles of the cable system These must-carry regulations survived several vigorous challenges, and the Supreme Court had even affirmed the FCC's authority to regulate cable television systems for purposes "reasonably ancillary" to the FCC's

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1/ Trinity and its wholly controlled affiliates, operate stations: KTBN-TV, Santa Ana, California; KPAZ-TV, Phoenix, Arizona, WKOI-TV, Richmond, Indiana; KTBW-TV, Tacoma, Washington, KTBO-TV, Oklahoma City, Oklahoma, WTBY-TV, Poughkeepsie, New York; KNAT-TV, Albuquerque, New Mexico, WHFT-TV, Miami, Florida, WDLI-TV, Canton, Ohio; WLXI, Greensboro, North Carolina, and WCLJ-TV, Bloomington, Indiana All American operates: KTAJ-TV, St Joseph, Missouri, KDOR-TV, Bartlesville, Oklahoma; WWTO-TV, LaSalle, Illinois, and WTJP-TV, Gadsden, Alabama

2/ CET operates KETH-TV, Houston, Texas, KLUJ-TV, Harlingen, Texas; and KITU-TV, Beaumont, Texas

3/ 768 F 2d 1434 (D C Cir 1985), <u>cert denied</u>, 106 S Ct 2889 (1986); and <u>Century Communications Corp v FCC</u>, ____ F 2d ____, 64 R R 2d 113 (D C Cir 1987), respectively regulatory responsibilities toward broadcast television, including must-carry "[4]

Following Quincy, the FCC voted unanimously on August 7, 1986, and again on March 26, 1987, that the health, even the survival, of a free over-the-air television service required the imposition on cable systems of modified must-carry rules [5]

The FCC's post-Quincy must-carry rules were written with an eye to satisfying the Court's concerns expressed in Quincy and were at least partially the product of an agreement between the broadcasters, represented by the National Association of Broadcasters (NAB), and operators of cable systems (hereinafter Cable Operators), represented by the National Cable Television Association (NCTA) The new must-carry rules did not specifically require the carriage of all local stations, but rather created a "pool" of qualified local signals from which Cable Operators could select, up to a maximum quota of roughly twenty-five percent of the cable system's activated channel capacity Nevertheless, even these modest must-carry requirements adopted with the acquiescence, even the active participation of the Cable Operators' largest trade association, were struck down by the Court in the Century case

Since the Quincy and Century cases were decided, the Commentors have collectively been removed from over 10 cable systems serving numerous local communities with nearly 230,000 viewers In some instances Commentors were removed from cable systems serving their communities of license, the communities which Commentors are obligated, by the terms of their FCC licenses, to serve (and failure by a television licensee to serve its local community could result in a loss of its five year renewal license) In addition, numerous cable systems, serving over 915,000 viewers, which were scheduled to begin carrying many of the Commentors' stations have in the wake of the Court's decisions unilaterally decided not to begin carriage of these local stations These actions by Cable Operators have not only economically harmed the Commentors, and collectively the construction costs for Commentors' stations represent initial capital investments of over 30 million dollars, they have effectively denied the Commentors access to the public they are licensed and required to serve

The demise of the must-carry rules has given Cable Operators the unlimited authority to choose the information which local viewers shall receive Moreover, unlike broadcast stations, this unlimited authority is largely unregulated by the federal government and, since the Cable Communications Policy Act of 1984,[6] cable is subject to only the least intrusive state or local regulation Nor are the Cable Operators subject to regulation by market forces since the compulsory copyright license[7] ensures that cable systems receive a majority of their product (programming) at a price set artificially low by

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4/ U S v Southwestern Cable Co , 392 U S 157 (1968); U S v Midwest Video Corp , 406 U.S 649 rehearing denied, 409 U S 898 (1972); and FCC v Midwest Video Corp , 571 F 2d 1025 (8th Cir 1978), aff'd, 440 U.S 689 (1979)

5/ Amendment of Part 76 of the Commission's Rules Concerning Carriage of Television Broadcast Signals by Cable Television Systems, 1 FCC Rcd 864 (1986), recon denied, 2 FCC Rcd 3593 (1987)

6/ 47 U S C § 521-29.

7/ 17 U S C § 111

government action, and whose only real potential competitors, in terms of capital assets and existing communications infrastructure, the telephone companies, are barred from competition

The demise of the must-carry rules, in conjunction with the Cable Communications Policy Act of 1984, the compulsory copyright license, and the prohibition of effective competition by banning telephone companies from the cable television industry, has allowed a federally and locally unregulated monopolist to function as a gatekeeper, deciding which broadcast stations have access to the communities they are obligated to serve As stated by FCC Commissioner James H Quello in his January 16, 1988 speech before the Alabama Broadcasters Association, no "monopoly or semi-monopoly transmission pipeline should be able to prevent or obstruct the licensed stations' local service to the public " Unfortunately, Cable Operators have rarely exercised their control over the information provided subscribers in the public interest, and the public has suffered accordingly

Cable's gatekeeping power is bad enough Incredibly, however, that power is also federally subsidized Cable Operators enjoy a significant competitive advantage over the same local television stations whose access to the viewers it controls, since, under the 1976 Copyright Act, the cable system may carry a local station's programming free of charge, without copyright liability, programming for which the station paid competitive high prices Cable Operators may then charge cable subscribers a monthly fee for the same programming it receives free of charge Programming costs for independent stations are continuing to escalate, particularly for the exclusive broadcast use of syndicated programming To make matters even more unfair, cable systems may telecast the same (duplicate) programming by carrying a non-local broadcast station When that happens the cable system pays only a small fraction of the local station's cost for the same programming, since cable only pays an artificially low and federally set price reflected in its compulsory copyright fees

As if these compounded advantages were not enough, Cable Operators also aggressively compete with local broadcasters for the same advertising and donor dollars which support free programming available to the public on commercial and noncommercial TV stations As Commissioner Quello noted: "[t]he potential scenario for a no 'must-carry' communications market is nothing but disaster for local broadcast service and eventually for continued free major sports events and fine quality programs "

Both Congress and the Federal Communications Commission do a disservice to local broadcasters and violence to common sense in attempting to legislate or regulate on the basis of a theory of market competition that does not exist The fact that dominates the communications marketplace is that, for cable television, there is no marketplace Cable television systems, once franchised, have no effective competition Absent must-carry rules cable systems are monopolies with no limit on their discretion concerning the information which they choose to provide subscribers The Cable Communications Policy Act of 1984 even denies local or state authorities the traditional tool used to regulate monopolies--rate regulation

While the FCC's post-Quincy must-carry rules had provided for an input selector switch (the A/B Switch) to permit cable subscribers to be able to switch from cable to over-the-air television, this requirement was vigorously opposed by the cable industry Even if the A/B Switch requirement were resurrected in some manner as a supplement or substitute for must-carry, it would provide little, if any, practical relief to local broadcasters With the up to 104 channels available on cable with superior reception, the subscriber's incentive to install an A/B Switch to receive (if at all) an off-the-air signal on an indoor antenna would be negligible

The demise of the must-carry rules also distorts, to the monopolist's benefit, the economic relationship between competitors for ever scarcer advertising dollars Make no mistake about it, the economics of advertising make local broadcasters and the cable systems competitors for advertising dollars, and create an economic and competitive rationale for denying local broadcasters access to the audience they are licensed (obligated) to serve Since cable subscribers must pay a monthly fee, they are, almost by definition, a more affluent market segment than that available to free over-the-air television When a cable system is able to function as the "gatekeeper" it may effectively monopolize for itself advertising dollars aimed at more affluent demographics, leaving the system's broadcast competitor with no access to the more desirable and more saleable demographics Prevented, or at least hindered, from competing for advertising dollars, the economic structure supporting free over-the-air television is further dangerously weakened

In view of the new economic universe in the 1980's, and the overwhelming competitive advantages enjoyed by cable systems, federally mandated programming subsidies, such as the compulsory copyright and the lack of syndicated exclusivity, which artificially limit the price paid by cable system's for programming, are unnecessary, uneconomic, anti-competitive and contrary to the public interest

For a local broadcaster, the cable system may telecast its programming without any cost at all For syndicated programming provided by distant stations, the compulsory license permits cable to take and retransmit broadcast programming without express permission and without regard to the contractual arrangements the broadcaster may have made concerning program distribution A cable system need only pay the copyright rate periodically set by the fiat of the Copyright Royalty Tribunal Whatever rationales justified the copyright license, such as the need to foster the infant cable industry, have clearly passed away over the last 12 years

Any concern that cable would be unable to handle the transaction costs of negotiating directly with copyright holders simply does not apply today Cable has proven itself capable of negotiating for cable program services In fact, cable already negotiates for three out of four program services it receives, as is certainly appropriate for a monopoly which controls program distribution to the most significant markets [8] Without must-carry, cable's compulsory license significantly distorts the cost of programming, depriving copyright holders of significant revenues Cable systems should buy and sell programming in a market bereft of such artificial and anti-competitive subsidies [9]

8/ 39 Federal Communications Law Journal 119 (May 1987)

9/ Primarily due to the vigorous arguments of cable, the Cable Communications Policy Act of 1984 cleared the way for Cable Operators to compete in an unregulated marketplace and deregulated its basic rate structure On the other hand, Cable Operators vigorously defend the compulsory license--a license which insulates Cable Operators from paying the market price for programming The cable industry should not have it both ways

To summarize, the cable monopoly, in the absence of any must-carry obligations, has unfair trade advantages compared to broadcast television in the acquisition of programming, in the sale of advertising, and in the limited competition it must face These anti-competitive advantages are magnified when Cable Operators may act as a gatekeeper in determining which of its potential competitors may have access to the community they are licensed to serve Economic equity, not to mention the restoration of a more level playing field in an economic marketplace which has been tilted almost entirely in cable's favor, requires that at least some of the advantages Cable Operators enjoy must be removed The gatekeeper, which under the current law retains many economic incentives to keep the gate closed, should be required to loosen its control of the gate The only effective way for this to be done is to reinstitute the FCC's traditional must-carry rules In addition, and at a minimum, the compulsory copyright license should be altered to reflect the real economic world in which cable and broadcast television compete to obtain and distribute programming

Respectfully Submitted,

TRINITY BROADCASTING NETWORK
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John DeS Casoria, President

LESEA BROADCASTING

March 17, 1988

Honorable Howard M Metzenbaum
Chairman
Subcommittee on Antitrust,
Monopolies and Business Rights
Senate Judiciary Committee
Washington, D C

Re Submission for Record of March 17, 1988 Hearings on Competitive Issues in the Cable Television Industry

Dear Mr Chairman

On behalf of LeSea Broadcasting, Inc ("LeSea"), I appreciate having this opportunity to inform the Subcommittee of severe anti-competitive conditions adverse to the public interest existing in today's cable television industry, particularly in the Tulsa, Oklahoma television market LeSea Broadcasting, Inc , the broadcasting division of Lester Sumrall Evangelistic Association, currently owns and operates four television stations in Indianapolis and South Bend, Indiana, Honolulu, Hawaii, and Tulsa, Oklahoma These stations are licensed by the Federal Communications Commission as commercial stations, but they differ from other commercial stations in that they offer specialty programming, primarily religious in nature

KWHB-TV, Channel 47 in Tulsa, Oklahoma, is one such station, acquired by LeSea in 1986 The Tulsa television market is the 52nd largest television market in the United States with approximately 460,000 television households according to the 1985-86 Arbitron Television Markets and Rankings Guide, and approximately 51% of those households subscribe to cable television There are six commercial television stations in the Tulsa market, including KWHB, and one non-commercial station, all of which are now carried on the local cable system at least part-time, except KWHB KWHB has never been carried on the cable system serving Tulsa

In June 1971, the City of Tulsa granted a franchise to Tulsa Cable TV, Inc ('Tulsa Cable"), which now operates the only cable system in Tulsa As of April, 1987, the Tulsa Cable system was the 13th largest cable system in the United States, wholly owned by United Cable TV Corporation ("United Cable"), the 7th largest multiple system operator ("MSO") in the country, with Tele-Communications, Inc , ("TCI"), the country's largest MSO, holding a large share of stock in United Cable Last week, United Cable announced that it reached an agreement to merge with United Artists Cable Television Corporation, to create United Artists Entertainment Company ("UAE"), an entity which would be the nation's third largest MSO, with TCI as the controlling shareholder

In 1987, Tulsa Cable served over 140,000 subscribers in fourteen different Oklahoma counties, more than 25% of all cable subscribers in the state of Oklahoma Many of Tulsa

Cable's subscribers receive television service exclusively through the cable system because off-air reception of television signals is not possible These households either lack access to a rooftop antenna or their television sets are not equipped for both cable television service and off-air reception Tulsa Cable is the "gatekeeper' of a monopoly, bottleneck facility for advertisers, local television stations, and other programming sources that seek access to this significant part of the local television audience which consists of captive consumers who can only receive television service through the Tulsa Cable's system KWHB's broadcasts cannot reach this audience, unless Tulsa Cable carries KWHB's signal on the system

Prior to the time that KWHB commenced operations, the Federal Communication Commission's rules would have mandated the carriage of KWHB as a local television station on the Tulsa Cable system However, in 1985, those rules were found to be overbroad under the First Amendment by the U S Court of Appeals for the D C Circuit Subsequently, under intense Congressional pressure, the FCC reluctantly reimposed interim rules in 1987 to require the carriage of only some local television signals for a 5 year period Recently, those rules were found to be unconstitutional, and all that remains in the way of federal regulation is a program for the dissemination of "input selector" switches, devices which are optional equipment for cable subscribers, incompatible with remote control devices, and which facilitate cable subscriber access to off-air reception only in instances where subscribers opt to have them installed at their own expense, and where subscribers have access to adequate antennas for off-air reception Currently, Tulsa Cable enjoys complete discretion to decide which local television stations will be carried on the system

As the only local television station in Tulsa without cable carriage, it is becoming more and more difficult for KWHB to attract and to satisfy programmers and advertisers Accordingly, KWHB has determined that carriage on the Tulsa Cable system is indispensable to its survival as a television station in the Tulsa market On numerous occasions, KWHB has requested carriage on the Tulsa Cable system and Tulsa Cable has refused to carry KWHB Recently, KWHB requested access under the leased access provisions of the Cable Communications Policy Act of 1984 (47 U S C § 532), and was refused the opportunity to lease a channel In addition, aside from leased access under the Cable Act's provisions, Tulsa Cable refused to discuss the carriage of KWHB on the Tulsa Cable system on any terms It appears that Tulsa Cable will not carry KWHB on the Tulsa system under any circumstances

The reasons why Tulsa Cable has flatly refused to carry KWHB and has declined to negotiate the price of carriage, are readily apparent Tulsa Cable is in direct competition with KWHB, by offering its own cable religious channel on the Tulsa Cable system Tulsa Cable offers time on this religious channel to various religious programmers and advertisers, including many who would ordinarily purchase time or advertisements on an over-the-air broadcast television station such as KWHB Essentially, Tulsa Cable deliberately excludes KWHB from its system and thereby forces religious programmers and advertisers to choose between circulation in cable homes on Tulsa Cable's religious channel, and circulation in non-cable homes on KWHB If religious programmers or advertisers want to reach the audience in Tulsa's cable households, they must place their programs and advertisements on the Tulsa Cable religious channel Moreover, because KWHB can only sell circulation in non-cable homes to advertisers, Tulsa Cable has placed a 'ceiling" on the rates which KWHB may charge its advertisers, and made KWHB a limited distribution medium in the Tulsa television market This severely impairs KWHB's ability to compete not only with Tulsa Cable's religious channel, but also with other broadcast television stations in the Tulsa market which are carried on the Tulsa Cable system

Tulsa Cable attempts to justify its decision not to carry KWHB by indicating it does not want to duplicate programming already on the Tulsa Cable system However, the only duplication which could occur on the Tulsa Cable system if KWHB were carried involves a small amount of religious programming and a small amount of syndicated programming to which KWHB purchases exclusive rights for the Tulsa market Tulsa Cable currently offers 3 music channels, 2 Super channels, 2 children's channels, 4 news channels, and 4 premium movie channels, but only one religious channel Ironically, Tulsa Cable explains its decision not to carry KWHB by stating that it prefers to avoid duplication in the types of programs offered on the system

Several national religious programmers have chosen Tulsa Cable's religious channel rather than KWHB Information about the rates which Tulsa Cable charges these religious programmers for access to its religious channel was unavailable However, it is conceivable that Tulsa Cable could charge little, or nothing, to carry this national religious programming Under Section 111 of the 1976 Copyright Act, Tulsa Cable enjoys a subsidy in the form of a compulsory copyright license which permits it to retransmit the programming of any broadcast television station, without prior consent from copyright holders and without negotiating fair compensation for those rights In contrast, KWHB must pay market prices for its programming, and it does not enjoy any subsidy of its programming costs

In sum, at the present time, Tulsa Cable competes with KWHB, a local independent specialty station, for both programming sources, advertisers, and audience for religious programming in the Tulsa market Tulsa Cable uses its monopoly bottleneck facility unfairly to discriminate against its competitor, KWHB Tulsa Cable limits KWHB's ability to compete with its religious channel and with other television stations in the Tulsa market by refusing to carry KWHB on any terms, and thereby abuses its monopoly power At the same time, Tulsa Cable enjoys a subsidy of its programming costs at the expense of copyright holders If the current situation continues, KWHB will likely not survive economically in the Tulsa television marketplace

The anti-competitive conditions in Tulsa, Oklahoma are not unique, but are merely illustrative of a climate which exists in many markets of varying sizes throughout the nation There are two significant trends in cable television industry which will continue to drive this anti-competitive situation on a national level First, the nation's MSO's continue to grow by acquiring each other and individual cable systems, apparently without any governmental attention Second, the largest MSO's are permitted to have growing financial interests in various programming sources As the large MSO's such as TCI and United Cable, soon to be UAE, increase their ownership interests in, or joint ventures with, programming companies such as Cable Value Network, American Movie Classics, Black Entertainment Television, the Discovery Channel, Event-Television (the new pay-per-view service), and the like, there will be even greater incentives for cable systems to abuse their monopoly power as gatekeepers of bottleneck facilities and to discriminate against local broadcast television stations, particularly independent specialty stations, using the method in which Tulsa Cable is now engaged — freezing out the competing broadcast station by absolutely denying it carriage on the cable system

Thank you for the Subcommittee's attention, and your interest in this matter

Sincerely,

Peter Sumrall
LeSea Broadcasting, Inc

Senator METZENBAUM Hearing stands adjourned

[Whereupon, at 12 03 p m , the subcommittee hearing was concluded]

APPENDIX

ADDITIONAL SUBMISSIONS FOR THE RECORD

Coaxial Communications

Technology and Service through Cable Television

Executive Offices

March 22, 1988

Senator Howard Metzenbaum
1240 East 9th Street
Cleveland, Ohio 44199

Dear Senator Metzenbaum

My name is Joel S Rudich I am the President and Chief Operating Officer of Coaxial Communications Coaxial is an Ohio based cable television company employing approximately 300 people and servicing approximately 75,000 households in the Columbus and Cincinnati metropolitan areas

On Thursday, March 17, 1988, you chaired a public hearing that dealt with several cable issues One of these issues dealt with the carriage of independent broadcast signals on cable systems, and one of the panelists, Mr Wendell Triplett, General Manager, WWAT-TV53, Chillicothe, Ohio, used this forum to unfairly disparage the name of our company, Coaxial Communications

Unfortunately, Mr Triplett misstated the facts regarding his signal not being carried on Coaxial's Columbus, Ohio cable system Because Mr Triplett's statements are so overwhelmingly inaccurate, I hereby request the opportunity to set the record straight since the Committee did not hear the real facts I respectfully request that this letter and attachments be included in the record of the hearing

In his testimony, Mr Triplett dwelt on his investment in his new UHF broadcast station Yet, at the same time, Coaxial made a major investment and took a sizeable risk to offer new local Columbus oriented programming and minority and special interest programming

During 1986/1987, Coaxial spent several million dollars to expand the capacity of its Columbus system by adding five additional channels. At that time, it was our plan to add the following additional programming during the fall of 1988 The Discovery Channel, Black Entertainment Network, The Weather Channel, Electronic Program Guide and "Coax 36", a composite program channel including local Columbus area high school, college and professional sports. Contract negotiations with all these program suppliers had begun well before the anticipated 1987 fall launch of these new services

While we were finalizing our fall marketing plans, we were formally notified by Mr Triplett that his new station, WWAT-TV53, Chillicothe, which, as you know, is located approximately 50 miles south of Columbus, was a "must-carry" station and demanded carriage on our cable system. At that time, acting in good faith, we took Mr Triplett at his word that, in fact, WWAT-TV53 was a "must-carry" signal even though they were not a "local" Columbus signal and their programming was nothing more than 24 hours a day of shopping from America's Value Network We began carrying WWAT as part of the Basic Service on our cable system on October 1, 1987

In December, 1987, when the U S Appeals Court overturned the "must-carry" rules, I personally contacted the local broadcast stations (both VHF and UHF) and informed them that, despite the court's decision, Coaxial had no plans to make any changes to our channel line-ups that would adversely affect them in any manner whatsoever Indeed, we continued to carry TV53 into 1988

However, on January 20, 1988, Coaxial was informed by its FCC counsel that, contrary to Mr Triplett's claims, WWAT-TV53 was not, and had never been a must-carry signal under the FCC rules In fact, carriage of WWAT would cause Coaxial to incur significant potential copyright liability which could range between $180,000 and $700,000 per year since WWAT-TV53 was a "distant" signal under the cable copyright law

Upon learning of WWAT-TV53's erroneous representations, Coaxial dropped WWAT from carriage on its cable system, and, we informed Mr Triplett, in writing, of the financial exposure to Coaxial Mr Triplett then advised Coaxial that Channel 53 would assume total copyright liability However, his assumptions as to the copyright fees grossly underestimated the amount that Coaxial would be liable for

Since that time, Coaxial Communications has made repeated attempts to have Mr Triplett clarify his assumption of copyright liability Contrary to Mr Triplett's testimony that WWAT would cooperate fully to protect Coaxial the attached letters from me to WWAT-TV53 clearly show that this statement is absolutely inaccurate These letters represent only a few of the unanswered letters sent to WWAT-TV53 seeking clarification

Senator Metzenbaum, as you know, the copyright laws specify that the carriage of any distant signal (regardless of whether it is for one minute or for one month in any six-month accounting period) imposes significant copyright liability on a cable company As a result of this law, the carriage of WWAT would impose a minimum $180,000 annual increase in copyright liability As Coaxial grows, this payment could increase to approximately $700,000 annually Thus, it is critical that we obtain from Mr Triplett guarantees that he would make specific arrangements to deposit the funds reimbursing us for this expense incurred solely due to the carriage of WWAT Coaxial will suffer this huge liability from the carriage of WWAT-TV53 regardless of whether Mr Triplett is unable to reimburse us after carriage is instituted We have simply requested Mr Triplett insure that the station pay these costs But, contrary to his testimony, the attached letters clearly show that Mr Triplett acknowledges the copyright liability that WWAT-TV53 would impose on Coaxial and that he has refused to respond to this issue

To the extent Mr Triplett got bad advice regarding WWAT-TV53's must-carry status in Columbus, the bottom line is that TV53 was never a must-carry signal under FCC rules In fact, WWAT-TV53, as a distant station under the copyright law, imposed major potential copyright liability on Columbus cable systems Having relied on Mr Triplett's earlier erroneous statements regarding his must-carry status, Coaxial now wants more than empty, ambiguous and unenforceable statements that the station will take care of us

In summary

1) WWAT is not and has never been a must-carry signal for Coaxial Communications

2) Carriage of WWAT by Coaxial Communications would create a copyright liability of $180,000 to $700,000 for Coaxial

3) Mr Triplett has continually refused to respond to Coaxial's request regarding insuring Coaxial protection from the copyright liability related to WWAT's carriage

4) Coaxial currently carries all local signals carried under the recently overturned must-carry rules and we have no plans to do otherwise I personally contacted these local stations in December, 1987 and informed them of this fact

Senator Metzenbaum, I trust this provides both sides of the story regarding the signal carriage of WWAT on Coaxial's Columbus, Ohio cable system Mr Triplett hoped to guarantee his success in the broadcast business based on his Chillocothe signal being carried on the Columbus cable systems 50 miles away regardless of the nature of the copyright laws He did not fully understand the laws regarding cable's copyright liability in carrying distant independent signals As such, it is not accurate to blame Coaxial for Mr Triplett's mistake Coaxial has acted in complete good faith in its efforts to accommodate the carriage of WWAT

I look forward to meeting with you on your next visit back home to either Cleveland or Columbus In the meantime, if I can be of any further assistance to you on this matter, please let me know

Sincerely,

Joel S Rudich
President and
Chief Operating Officer

/gg

Enclosures

cc   Preston Padden, President, INTV

Channel 53 Television
CHILLICOTHE / COLUMBUS

[redacted]

Joel Rudich
Coaxial Communications
3770 East Livingston Avenue
Columbus, Ohio 43227

Dear Mr Rudich,

This is to notify you that WWAT-TV channel 53 signed on Monday August 31, 1987 The Broadcast License is on Chillicothe, Ohio which means that channel 53 is a must carry station in the Columbus market (Coaxial headend is well within 50 mile limit of must carry)

We are officially requesting that you add us to your system In accordance with our meeting of October 29, it was agreed that Coaxial would commence carrying channel 53 on Monday November 2, 1987

I look forward to working with you to give central Ohio viewers the best possible programming

Sincerely,

Terry Penrod

Terry Penrod
Program/National Sales Manager

TP/lj

2698 Sawbury Blvd • Worthington, Ohio 43085 • 614-766-9603

Coaxial Communications

Technology and Service through Cable Television

Executive Offices

[redacted]

Mr Wendell A. Triplett
General Manager
WWAT-TV
2698 Sawbury Blvd
Worthington, OH 43085

Dear Mr Triplett

We understand that Channel 53 (WWAT) is currently switching from a primarily home shopping format to a significant amount of regular programming Under the must carry rules recently in effect, Coaxial was obligated to carry Channel 53 These same rules, however, excuse Coaxial from carrying any signal if such carriage would subject Coaxial to additional copyright liability Since Channel 53 would not be a must carry under the 1976 rules (the rules to which copyright liability is tied) Channel 53 is a distant signal to Coaxial

Since Channel 53 (WWAT) is going to a non-specialty format, and since Coaxial already carries more than its quota of independent signals, carriage of Channel 53 would cost Coaxial the maximum copyright liability - 3 75% of gross non-premium revenues In light of this additional burden, Coaxial will delete the carriage of Channel 53 (WWAT) effective immediately

Sincerely,

Joel S Rudich
President and
Chief Operating Officer

/gg

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Executive Offices

[redacted]

file

Mr Terry Penrod
~~Program~~/National Sales Manager
~~Channel 53 Tele~~vision
2698 Sawbury Boulevard
Worthington, OH 43085

Dear Mr Penrod

Thank you for your letter of January 27, 1988 in which you propose to reimburse Coaxial for both annual copyright and marketing promotional costs

While this is certainly an interesting proposal, I believe that you have made a significant miscalculation in the computation of potential copyright liability as noted in Appendix 1, Item A as $50,528 I believe you have failed to recognize that copyright is an annual liability and could go as high as $650,000 under the current rate structure I think it should now be clear to you the impact copyright liability has on the decision process regarding the carriage of WWAT

With regard to the use of Channel 53 for promotional advertising, the total value that you have assigned to items B and C are imputed based on your assessment, and do not correspond to value that we would place on them. Unless, of course, you are offering us this amount for us to use on TV advertising as we see appropriate consistent with our overall marketing plans to increase our cable penetration

As you can see our decision not to carry WWAT is based on our recognition as well as the FCC's which recognizes that copyright liability justifies the action we have taken particularly when the programming mix does not dictate otherwise

Sincerely,

Joel S Rudich
President and
Chief Operating Officer

/gg

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[redacted]

Mr Donald S Berman
General Sales Manager
Channel 53 Television
2698 Sawbury Blvd
Columbus, OH 43235

Dear Mr Berman

This letter is a follow-up to our telephone conversation today which was in response to your letter of February 16, 1988

As I mentioned to you, the specific purpose of my call was to obtain a clarification of item "1" in your letter "WWAT-TV53 will assume total copyright liability " On January 27, 1988, Mr Terry Penrod wrote to me with the exact same proposal On January 28, 1988, I responded in writing to Mr Penrod and requested that he clarify his proposal which stated "WWAT-TV53 will assume total copyright liability " As of this date, Mr Penrod has not responded to me

The question remains, what do you mean by this statement? We estimate that the current liability that we would incur if we carried WWAT to be approximately $180,000 per year and that this could go as high as $700,000 per year as our system expands beyond the Grade B contour

You have stated to me that you will make this payment However, full liability for each six-month period is incurred the moment we carry one program from TV53 and cannot be avoided if we drop TV53 for failure to meet its commitment to Coaxial Thus, we would request that a sufficient escrow account be established by WWAT prior to our carriage of TV53 to cover 1) the current six-month period's liability, and 2) that funds be deposited thirty (30) days in advance of each upcoming copyright period Since you were not prepared to commit to providing the funds concurrent with Coaxial liability, it was agreed that you would have Mr Triplett respond to me in writing with his reply.

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Mr. Donald S. Berman
February 19, 1988
Page No. 2

We believe this requirement is crucial to protecting Coaxial against enormous liability should carriage of TV53 be undertaken as a non-must carry signal. Indeed, I believe that Coaxial acted in good faith from the very beginning. In October, 1987, we accepted WWAT's representation that they were, in fact, a must carry signal In fact, WWAT was not and has never been a must carry signal for Coaxial and, as a result of our acceptance of your verbal representation, we have suffered significant copyright liability. I do not intend to ever allow this to happen again. Thus, we are attempting to document all of our discussions so that no one can be unfairly accused of acting unfairly.

Coaxial currently carries all local signals required under the recently overturned must carry rules and we have no plans to do otherwise I personally contacted these local stations in December, 1987 and informed them of this fact.

I look forward to your written reply.

Sincerely,

Joel S Rudich
President and
Chief Operating Officer

/gg

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Executive Offices

[redacted]

Mr Terry Penrod
Program/National Sales Manager
Channel 53 Television
2698 Sawbury Boulevard
Columbus, OH 43235

Dear Mr Penrod

Thank you for your letter of February 24, 1988 in which you request that our attorneys contact Mr Perkins, your Washington attorney "to construct an agreement that will answer the copyright issue"

I'm not quite sure that I understand this current request The copyright issue is clearly spelled out by the FCC and I don't believe that I need to incur additional legal expense to "construct an agreement" that already is part of the law

I am also quite concerned about the approach you (WWAT) are taking in this matter I responded to your letter of January 27, 1988 on January 28, 1988 I still have not received a reply to my letter.

On February 12, 1988 Mr Donald Berman, General Sales Manager for WWAT, called my office to inform me of a "new" proposal he had for Coaxial to consider He wrote to me on February 16, 1988 with this "new" proposal which turned out to be the exact same proposal you made to me on January 27th I called Mr Berman on February 18, 1988 to discuss his proposal, and, interestingly enough, he said that he was totally unaware of your letter! I asked Mr Berman if he could clarify his and your proposal "WWAT-TV53 will assume total copyright liability"? His response was that WWAT was prepared to pay our total copyright liability, but, he didn't know how much money was involved When I told him that it could range between $180,000 and $700,000 per year and that we would require that this liability would have to be placed in an escrow account to protect Coaxial against enormous financial copyright liability, Mr Berman then said

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Mr Terry Penrod
February 25, 1988
Page No. 2

that only Mr. Triplett could respond to this issue He informed me that Mr Triplett was out of town, but would return the next day with an answer It is now a week later and I have not heard from Mr Triplett.

Mr Penrod, I think it is about time that you begin to represent the issues involved in this case in a full and forthright manner WWAT was not and has never been a must carry signal for Coaxial and, as a result of our good faith acceptance of your verbal representation, we have potential significant copyright liability

It is regrettable that you entered the broadcast business without having fully understood both the must carry and copyright rules - but, that is not Coaxial's fault It is also regrettable that you continue to attempt to gain media attention without fully stating all the facts This approach has caused Coaxial to spend enormous amounts of its management time plus the incurrence of substantial legal fees In the same regard, Coaxial is formally requesting that you immediately cease from including our name in your newspaper and TV Guide advertisements indicating that WWAT is carried on Coaxial's Channel 19 since these ads are false and misleading

Although I have tried to respond to WWAT's requests in a timely manner, it appears that you have several different agendas with regard to this issue depending on your "audience". Therefore, I am advising you that I will no longer respond to any more of your letters and/or requests until you formally acknowledge in writing that (1) you are not and have never been a must carry signal for Coaxial, and that your written request dated October 30, 1987 informing Coaxial that WWAT was a must carry signal and requesting addition to our system was improper, and, (2) you are fully prepared to cover our copyright liability by placing in escrow the total amounts of funds that Coaxial could be required to pay

Coaxial currently carries all local signals carried under the recently overturned must carry rules and we have no plans to do otherwise. I personally contacted these local stations in December, 1987 and informed them of this fact

I look forward to your written reply

Sincerely,

Joel S Rudich
President and Chief Operating Officer

/gg

cc Mayor Rinehart, City of Columbus

Coaxial Communications

Technology and Service through Cable Television

Executive Offices

[redacted]

Mr. Wendell Triplett
CEO/General Manager
Channel 53 Television
2698 Sawbury Blvd.
Columbus, OH 43235

Dear Mr. Triplett

I am in receipt of your letter dated March 8, 1988 It is indeed regretable that you continue to respond to the signal carriage issue in the manner you have chosen As you know, your Washington attorney, Mr. Roy Perkins, talked with our attorney and Mr. Perkins acknowledged that WWAT was never a must carry signal.

However, the question still remains, "How do you propose to deal with the copyright liability issue that Coaxial would be faced with by carrying Channel 53?" This question has been raised in correspondence with Channel 53 dated January 20, 26, 28, February 12, 16, 18, 24, and 25, 1988 - and, still we have no reply from you.

As I have stated in the past, Coaxial currently carries all local signals carried under the recently overturned must carry rules and we have no plans to do otherwise. I personally contacted these local stations in December, 1987 and informed them of this fact.

Sincerely,

Joel S. Rudich
President and
Chief Operating Officer

/gg

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CORPORATION FOR PUBLIC BROADCASTING

Donald E Ledwig
President and
Chief Executive Officer

April 8, 1988

Honorable Howard Metzenbaum
Chairman, Subcommittee on
Antitrust, Monopolies and Business Rights
Committee on Judiciary
United States Senate
308 Hart Senate Office Building
Washington, D C 20510

Dear Mr Chairman

Please include in the Record of your recent hearing on cable television the views of the Corporation for Public Broadcasting (CPB) on the issue of assured cable carriage of local public television stations

Public television applauds your decision to conduct this hearing on the problems and policy dilemmas resulting from the growth of cable television service in the United States Without a doubt, cable has revolutionized the electronic mass media, but the revolution has been a mixed blessing for the American people Indeed, through cable, multiple and diverse video services and programming are now available to millions of viewers However, the drastic regulatory changes that were made to accommodate cable's explosive growth may severely reduce the availability of a vital public service that should be universally available to all Americans public television

1111 16th Street NW
Washington DC 20036
(202) 955 5275

Public Television Provides Americans The Finest Quality Programs Available--For Free

Public television provides the American people the highest quality and most diverse programming available without charge on television today. Over ninety million Americans tune in to public television every week for the in-depth news coverage of MacNeil/Lehrer NewsHour, the hardhitting documentaries of Frontline, the original American drama from American Playhouse, live opera, ballet and symphony concerts on Great Performances and Live From Lincoln Center, the only high-quality educational programming available for our children, such as Sesame Street, Square One TV, and Three-Two-One Contact; and for a myriad of other diverse and stimulating programs Quite simply, public television challenges Americans to be citizens, thinkers, and achievers, not just consumers Moreover, public television is available over the air, free to all citizens, not just to those who are wired and can afford to pay for cable service

However, as a result of a regulatory and judicial process that has stood the public interest on its head, millions of American viewers could be denied these important public television benefits which they, through their taxes, have helped finance Loss of assured carriage on cable will harm the public television system in several ways

Carriage Loss Reduces Program Diversity

Without mandatory carriage, there is no guarantee that cable systems will carry even one local public television station Instead, if they decide to carry any public television station at all, they could opt for a distant, larger, more powerful public television station Even if they carry one local public television station, however, they will likely not carry a second or third local public television station, on the assumption that only the programming fed by PBS needs to be included on the cable This assumption ignores the plethora of educational programming geared to the local community that is provided by public television stations throughout the day, as well as the wealth of regional programming not distributed through PBS Such programming differs greatly from station to station within the local market Thus, without mandatory cable carriage, there will be a severe reduction in the diversity of programming available through public television stations to the American people

Carriage Loss Undermines Public Television's Revenue Base

Each public television station that loses cable carriage suffers a loss in audience and viewer contributions, which reduces the ability of that station to acquire programming to serve its community This loss of carriage of individual stations exerts a cumulative drag on the ability of the system to finance production of new and innovative programming, because public television funds many of its programs collectively through such mechanisms as the Station Program Cooperative and the Program Challenge Fund Thus, carriage loss not only harms each individual station that is dropped, but also harms the overall public television system

Carriage Loss Could Jeopardize Congressional Policy of Federal Financing For Public Television

Finally, loss of cable carriage could harm the public broadcasting system in an indirect but very important manner The Public Broadcasting Act authorizes financing for public broadcasting stations on the basis of a matching formula of nonfederal to federal financing Today, public television stations exceed their matching requirement to receive the full amount of funds authorized by the Act However, if enough stations suffered a substantial reduction in their contributions as a result of loss of carriage on their local cable systems, the overall amount of federal financing intended by Congress to be available to public broadcasting could be reduced

As President of the only public broadcasting organization statutorily accountable to Congress for the welfare and performance of the public broadcasting system, I feel obligated to inform the Subcommittee of the serious impact that loss of assured cable carriage will have on the public television system

I appreciate the opportunity to include this letter in the Record of your hearing on cable-antitrust issues I would be happy to elaborate on the implications of cable carriage loss for public television in any follow-up hearing you conduct

Thank you for the strong support you have provided public broadcasting over the years and for the Congressional attention you are focusing on this serious problem facing public television

Sincerely,

Donald Ledwig
President and
Chief Executive Officer

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