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VERTICALLY INTEGRATED SPORTS PROGRAMMING: ARE CABLE COMPANIES EXCLUDING COMPETITION?

HEARING

BEFORE THE

COMMITTEE ON THE JUDICIARY
UNITED STATES SENATE

ONE HUNDRED NINTH CONGRESS

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THURSDAY, DECEMBER 7, 2006

UNITED STATES SENATE,
COMMITTEE ON THE JUDICIARY,
Washington, DC.

The Committee met, pursuant to notice, at 10:03 a.m., in room SD–226, Dirksen Senate Office Building, Hon. Arlen Specter, Chairman of the Committee, presiding.

Present: Senator Specter.

OPENING STATEMENT OF HON. ARLEN SPECTER, A U.S. SENATOR FROM THE STATE OF PENNSYLVANIA

Chairman SPECTER. Good morning, ladies and gentlemen. The Judiciary Committee will now proceed with a hearing on the subject of whether consumers are being fairly treated by owners of sports franchises and cable and satellite companies with the overriding question as to whether activities now being undertaken violate the antitrust laws or whether the antitrust laws ought to be amended to provide fairness to the consumers.

The backdrop is America's love affair, America's infatuation with sports, a national addiction to which I include myself, and we witness a rising cost of people watching pay television on cable television.

We had a hearing earlier on the implications of the activities of the National Football League on their practices, and today we take up the question as to vertical integrated sports programming, whether the consumers are being unfairly treated.

When we talk about integration, there are quite a number of situations where the cable companies own sports franchises—Cablevision with the Knicks and the Rangers and Cox with the Padres and Time Warner with the Braves and Comcast with the Flyers and '76ers and Charter with the Seattle Seahawks and the Portland Trail Blazers. And the issue is whether the failure to provide programming to competitors is a violation of the antitrust laws, with the Seventh Circuit decision in *MCI Communications* v. *AT&T* holding that Section 2 of the Sherman Act is violated if the so-called four-part test is met under essential facilities.

The Congress legislated in 1992 to prohibit vertically integrated companies, those that have ownership in programming, sports programming specifically our hearing today, from refusing to make their cable contact available to competitive multi-channel video

programming. And the Congress applied this only to programming delivered via satellite. It is questionable whether it ought to be applied to programming delivered by cable, terrestrial transmission as well.

The Commerce Committee considered a change in that law, and at least as of this time, Congress has not moved in that direction but perhaps we should. There are some strong arguments for moving in that direction.

In July of this year, the FCC required Time Warner and Comcast to provide competitors with access to their sports programming as a condition to their acquisition of the assets of Adelphia. But the FCC did not impose this requirement on Comcast SportsNet Philadelphia, and one of our points of interest would be why the distinction there.

We do not have anybody from Cablevision with us today, which I think is unfortunate. We gave Cablevision a lot of notice, and no reason was advanced why Cablevision could not cooperate with this Committee. And when we review the matter, seek any further explanation at our next hearing, people should know that the Committee does have the subpoena power. I do not want to lecture to the choir here, preach to the choir. All of you have come in on our invitation. But we do expect cooperation from companies who are programming and who are undertaking activities which affect consumers, affect the laws of the United States within the jurisdiction of the Judiciary Committee. We ought to have the cooperation from those folks coming forward.

We have a very distinguished panel this morning, and our lead witness is Mr. John Goodman, who is President of the Coalition for Competitive Access to Content. He was Executive Director of the Broadband Service Providers Association. He had operating roles in Astound Broadband and also served with Motorola, holds an MBA from Northwestern University and a bachelor's degree from Bethel College in psychology.

Thank you for joining us, Mr. Goodman, and we look forward to your testimony.

STATEMENT OF JOHN GOODMAN, PRESIDENT, COALITION FOR COMPETITIVE ACCESS TO CONTENT, WASHINGTON, D.C.

Mr. GOODMAN. Good morning. I want to express my appreciation to you and other members of the Judiciary Committee for the opportunity to participate today. I am pleased to represent the Coalition for Competitive Access to Content. It is a very diverse group of companies, including DBSs, BSPs, telco entrants, trade associations, and consumer groups that are all committed to expanded competition. These member organizations disagree on many public policy issues, but, nonetheless, they have come to the same conclusion regarding program access reform: assured access to content, particularly regional sports programming, is essential to the development of high-capacity networks that provide not only video but broadband competition.

Congress has long recognized the direct linkage between access to programming and additional video competition. In 1992, Congress did promulgate the original program access rules that re-

quired that video content owned by cable operators be made available to new entrants on fair and nondiscriminatory terms.

Access to content today is every bit as important as it was then. The FCC reviewed the application of certain program access rules in 2002 and concluded they were still essential, and they extended them for 5 years. More recently, Senators Kohl and DeWine have sponsored several valuable GAO studies that document both the need for more wireline competition and the relationship between access to content and the ability to compete. Regulators reviewing media mergers, as you referenced, also came to the same conclusion. Proceedings for DirecTV/NewsCorp and for Comcast, Time Warner, and Adelphia transactions were both approved with program access conditions both related to sports and other programming. While we applaud the FCC's vigilance in this area, the CA2C believes that a statutory mechanism—not piecemeal adjudication—is necessary and justified to assure access to content.

The current level of vertical integration continues to be significant and expanding. Incumbent cable operator ownership of professional sports franchises and sports programming has actually expanded since 1992. In addition, a substantial portion of current vertical integration is concentrated in programming that has the highest viewership and, therefore, value. The CA2C has attempted to document the current level of vertical integration. As we submit some summary profiles today, we ask the Committee to feel free to share this information with all parties involved so that this information can be validated, corrected, and expanded as may be appropriate. And I have these here if you want to see them.

Unfortunately, Congress's program access provisions, written in 1992, have not kept pace with today's technology and market structure. Cable operators can control exclusive rights to programming delivered over their headends by fiber as opposed to satellite. This is called the "terrestrial loophole." That is why a DBS subscriber in Philadelphia cannot receive Comcast's Sports Network with Flyers, Phillies, and '76ers games. It is why a DBS subscriber in San Diego cannot receive Cox's sports network for Padres games. The FCC has looked at this issue several times and concluded it has no authority to deal with terrestrially delivered content unless there are changes to the current law.

Accordingly, the CA2C provided input for the "Sports Freedom" provisions in the telecommunications legislation introduced by Senators Stevens and Inouye. These provisions closed the terrestrial loophole and enhanced the framework related to sports programming by, among other things, applying binding arbitration proceedings to certain disputes. These provisions were similar to the conditions created in the DirecTV/NewsCorp merger.

We supported new legislation because it will have equal applications to all MVPDs, and it will sustain the right market structures to promote competition. We should not rely on mergers, acquisitions, or other market events to address these industry-wide matters. Moreover, the FTC and the FCC should be directed and empowered to deal with anticompetitive issues. In short, we do not seek for Congress to establish an entirely new legal framework of economic regulation or price controls, nor should particular players

in the market be singled out. Rather, a rational and measured updating and extension of the rules is in order.

Opponents to program access legislation have publicly acknowledged that the existing rules have been effective within their current application. However, they now oppose program access rules. They claim these rules are not needed because current markets are fully competitive and that there are limited examples of abuse or denied access. But the market reality of key programming, especially local and regional sports, is that it is concentrated in the hands of a few cable operators, and that undermines this view.

Even incumbent cable operators have asked for conditions guaranteeing access to content. The DirecTV/NewsCorp merger was the first time that an incumbent video provider faced a potential threat of some other network operator having control of essential content. Suddenly, they were asking for merger conditions that sounded a lot like the standards CA2C members have promoted to bring video competition to the market.

I want to again thank you for this opportunity to be with you this morning, and I look forward to your questions.

[The prepared statement of Mr. Goodman appears as a submission for the record.]

Chairman SPECTER. Thank you very much, Mr. Goodman. We now turn to Mr. David Cohen, Executive Vice President of Comcast Corporation; had been a partner and Chairman of the firm of Ballard Spahr Andrews & Ingersoll, one of the largest law firms in the country; served with great distinction as chief of staff to Mayor Ed Rendell of Philadelphia; bachelor's degree from Swarthmore and University of Pennsylvania Law School graduate summa cum laude.

Thank you for coming in today, Mr. Cohen, and the floor is yours.

STATEMENT OF DAVID L. COHEN, EXECUTIVE VICE PRESIDENT, COMCAST CORPORATION, PHILADELPHIA, PENNSYLVANIA

Mr. COHEN. Thank you very much, Mr. Chairman, and thank you for the opportunity to testify today on vertical integration in sports programming. I would like to highlight three main points from my written testimony, which I understand will be made a part of the record: first, vertical integration is commonplace in commerce and can have real consumer benefits; second, there has been a dramatic decrease in vertical integration in cable; and, third, competitors to cable are getting access to all the programming they need, so there is no longer a need for special Government rules on program access. Let me briefly expand.

When Congress passed the 1992 Cable Act, it was concerned that cable operators that owned programming networks would have the ability and incentive to withhold that programming from competing distributors, particularly the then-fledgling satellite operators. So Congress told the FCC to adopt special program access rules to ban exclusivity and ensure that all satellite-delivered, vertically integrated cable networks are made available to all competitors.

Back then, many cable operators were vertically integrated. They had an attributable financial interest in almost 60 percent of the

68 or so national cable networks then in existence. But as our industry grew and as we built more and more channel capacity the market for programming has exploded. Today, of the more than 530 national cable networks, the FCC reports that cable operators have an interest in approximately 20 percent of them, although our data shows that number is closer to 12 percent. By any measure, though, vertical integration today is substantially less than what it was in 1992.

I would also like to stress that Comcast is among the least vertically integrated companies in the entertainment industry. We have an interest in a total of only 22 networks. Half of those carry sports, and eight of those would be considered regional sports networks. On a typical cable system, we are affiliated with only about 7 percent of the full-time networks that we carry. In comparison, our biggest competitor today, DirecTV, is owned by NewsCorp, which has a financial interest in over 30 of the networks that it carries—26 of those are sports networks, including 21 regional sports networks. The number of affiliated networks that DirecTV carries is, therefore, almost twice as many as Comcast carries.

In today's marketplace, as I explain in my written testimony, there is simply no justification for the FCC's current program access rules. Those rules were an unusual exception to a well-established principle of law and economics: that vertical integration can have very positive pro-consumer effects. Vertical integration allowed cable to create innovative programming when others would not. This led to valuable networks like CNN, the Discovery Channel, TV One, and C–SPAN, among others. Those investments helped to make cable the preferred choice of American viewers.

Let me give you another specific example that I know is near and dear to the Chairman's heart and that is near and dear to my heart. Sports fans in our hometown of Philadelphia had to settle for 2 second-rate regional sports networks until Comcast acquired the Flyers and '76ers and bought out those two networks in the mid-1990's. We then created Comcast SportsNet Philadelphia, which is exempt from the program access rules because it is terrestrially delivered. Congress permitted this limited exclusivity for a reason—not to prevent competition but because it did not want to deter investment in high-quality local programming. In fact, Congress wanted to make sure that it would continue to encourage such investments. In specific reliance on this exemption, Comcast has since invested over $450 million to build up SportsNet to the network that it is today. And although we make Comcast SportsNet Philadelphia available to every one of our terrestrial competitors, including Verizon and RCN, we do not make it available to our DBS competitors. However, in the seven other markets where Comcast has subsequently created regional sports networks, we make them available to all of our terrestrial and satellite competitors.

We think that some exclusivity of programming can be a good thing, because it permits competitors to distinguish themselves from one another. And I realize that the satellite providers are unhappy that they cannot provide SportsNet Philadelphia to their customers. But I will admit to you that we are a little unhappy

that DirecTV has exclusive rights to the NFL Sunday Ticket and that we cannot provide this service to our cable customers.

The simple fact is that exclusivity can't simultaneously be a good thing when our competitors have it but a bad thing when we have it. It is one or the other.

So thank you for the opportunity to testify today. I want to conclude by saying that it is past time to repeal the program access rules, especially the ban on exclusivity that is set to expire next year. Congress can reasonably rely upon the antitrust laws to guard against any problems here, and I will be happy to expand upon that in the question-and-answer session.

Thank you.

[The prepared statement of Mr. Cohen appears as a submission for the record.]

Chairman SPECTER. Thank you, Mr. Cohen.

Our next witness is Dr. Mark Cooper, Director of Research for the Consumer Federation of America, also President of Citizens Research, and a fellow at the Stanford Center on Internet and Society; the author of four books; undergraduate degree from CCNY, master's from University of Maryland, and a Ph.D. in sociology from Yale.

We appreciate your coming in today, Dr. Cooper, and look forward to your testimony.

STATEMENT OF MARK COOPER, DIRECTOR OF RESEARCH, CONSUMER FEDERATION OF AMERICA, WASHINGTON, D.C.

Mr. COOPER. Thank you, Mr. Chairman, and I appreciate the opportunity to appear today to testify on one of the key aspects of the continuing failure of competition to protect the consumer in the cable industry. This continuing market failure is evident in rising prices for monthly service, discrimination in carriage of programming by cable operators, refusal to offer critical marquee programming to competing delivery systems, and anticonsumer and anticompetitive bundling.

Entry into the industry remains extremely difficult from both the content and distribution sides. Satellite has been unable to discipline cable market power, and it appears that the entry of telephone companies is equally ineffective. Monthly prices for basic and expanded service have just about doubled since the passage of the Telecommunications Act of 1996. Just last week, the two largest theoretical competitors in the Northeast each upped their rates dramatically, by 4 to 5 times the rate of inflation.

Intermodal competition and a cozy duopoly is not enough to discipline the abuse of market power in this sector. Every traditional measure of market structure—concentration ratios, the Lerner index, Tobin's q ratios—indicates the existence of market power in the cable industry. This market power stems primarily from a lack of competition at the point of sale. The market exhibits not only the classic barriers of entry, such as high capital costs, specialized inputs, and economies of scale, but cable operators have built barriers to entry with their regional concentration, vertical integration, and bundling strategies.

The topic of this hearing, the withholding of vital geographically specific marquee programming from alternative distribution plat-

forms, is one of the elements in a tightly woven web of business practices that have dampened competition in the sector.

The incessant reduction in number of cable operators and their increasing size has led to the aggregation of cable systems into large regional clusters. Market power at the point of sale to the public and monopsony power at the point of purchase from programmers combine to undermine competition. Large MSOs have come to dominate specific regions of the country. They have moved into regionally specific sports programming that is itself a monopoly. They embed this programming in huge bundles, forcing consumers to pay for it all. They then deny access to this programming to competing distributors or make it available on anticompetitive and unfriendly terms and conditions.

Their monopsony power is grounded in their market power at the point of sale, and the huge regional clusters and concentrated national market created over the past decade gives them the ability to secure control over this regionally specific programming. Since the programming is regional, it is rarely distributed through terrestrial means, subject to the so-called terrestrial loophole. Therefore, the programming can be withheld from competing distribution.

As cable operators gain control of large contiguous geographic areas, they also are more able to obtain exclusive rights to programming they do not own. Restricting the flow of programming to alternative distribution platforms blunts competition at the point of sale. If the Congress intends to rely on market forces to discipline the market power of cable operators, it will have to break the stranglehold that the handful of vertically integrated, horizontally concentrated firms use to dominate the sector.

Antitrust-type structural remedies that apply to the supply side and are very much in the tradition of antitrust and were not well crafted in the 1992 and 1996 Acts including the following: Congress should impose a strict horizontal limit on cable ownership to diminish cable's monopsony power in the programming market; Congress should ban the abuse of vertical leverage, both by closing the terrestrial loophole and adopting an effective policy to prevent discrimination in carriage; Congress should prohibit contractual anticompetitive tying arrangements by dominant media programmers that force distributors to carry all of a network's or all parent owner's cable channels just to receive the small number that the consumers want.

We also think Congress should require cable operators to make available to consumers on an unbundled basis all programming that they choose to bundle. This will enable the demand side of the market to discipline the cost of programming and the size of their cable bill.

I appreciate the opportunity to testify and look forward to any questions. Thank you.

[The prepared statement of Mr. Cooper appears as a submission for the record.]

Chairman SPECTER. Thank you very much, Dr. Cooper. Without objection, we will admit into the record the statement of Senator Herb Kohl, who is Ranking Member of the Antitrust Subcommittee.

Our next witness is Mr. James Baller, Senior Principal of Baller Herbst Law Group, a firm specializing in telecommunications; led

the successful challenge to Virginia's and Missouri's barriers to municipal entry into the telecommunications field; graduate of Dartmouth and Cornell Law School.

We appreciate your being with us today, Mr. Baller, and the floor is yours.

STATEMENT OF JAMES BALLER, SENIOR PRINCIPAL, THE BALLER HERBST LAW GROUP, PC, WASHINGTON, D.C.

Mr. BALLER. Thank you very much, Chairman Specter. I appreciate your invitation to testify, and I am honored to be here today.

Since 1992, I have provided legal services to dozens of public and private providers of competitive communications services, and I have assisted several national and State associations that support such endeavors.

Over the years, I have seen at first hand a wide range of practices through which established cable operators have sought to thwart competition from my clients and similarly situated new entrants. At a hearing in this room in February of 2004, we presented documentation of dozens of such practices. Many are still occurring, and they need to be curbed once and for all. I applaud you, Chairman Specter, for focusing on programming access issues at this hearing, and I hope that the Committee will focus on some of the other practices in the year ahead.

In my testimony, I would like to focus on three points. First, I believe it is critically important not to treat programming access just as a cable entertainment issue, but to also see it as an infrastructure development issue that is essential to America's local, regional, and global competitiveness.

As the Committee knows, America's international ranking in broadband deployment has fallen precipitously over the last decade, from first in the world in the mid-1990's to as low as 21st today in some studies. The U.S. is also falling increasingly behind the leading nations in access to high- capacity Next Generation Networks and in cost-per-unit of bandwidth, where we are now ranked sixth, according to the International Telecommunications Union. These are alarming trends because virtually everything that we do at home, at the office, and at play will increasingly be done over broadband platforms in the future. As a result, the nations that lead the way in developing Next Generation Networks will be the ones that are most successful in the emerging information-based global economy ahead. I have given the Committee a handout that documents this point in greater detail.

A century ago, when electricity was the must-have technology of the day, the private sector alone could not electrify America quickly enough to meet demand, particularly in rural areas. Recognizing that electrification would significantly enhance economic development and quality of life, thousands of communities in underserved or unserved areas stepped forward to form their own electric utilities. Most that did thrived, while many that waited for the private sector to get around to them, in some cases up to 50 years, did not.

Today the history of electrification is repeating itself in the communications area, and many communities across the United States are ready, willing, and able to do their part to help America develop high-bandwidth Next Generation Networks as rapidly as pos-

sible. In this, they want to stay abreast of the most progressive municipalities abroad, and in my second handout, I have presented information about what is happening in some of the other leading cities in the world.

If we are to succeed as a Nation in developing Next Generation Networks, these networks must be economically viable. To do that, they must be able to provide all services that they are capable of providing, including video programming. And to deny access to key video programming has implications not just in the entertainment field but in the development of these systems.

Second, my second point is that the FCC has over the years supported the safeguards in the 1992 Cable Act. I completely agree with Mr. Goodman's testimony that it is essential that these safeguards be preserved and extended. If Congress wants to retain a competitive environment in the cable communications field, it is essential that all entities have access to critical programming. I can cite many examples where that need still exists today and, in any event, it is important to prevent such things from happening in the future. We cannot allow established cable operators to create or remove access to programming at their discretion.

My last point is that when we look at antitrust remedies, it is important to recognize that for small to medium-sized entities, antitrust remedies are illusory. The time, cost, burdens, and risks involved make antitrust remedies essentially worthless to small operators. What we need are clear, unambiguous, enforceable standards that supply and provide sufficiently onerous multiple damages, penalties, and attorneys' fees to deter noncompliance. Also, we need help from the major agencies to step in and provide service to provide protection that small providers cannot provide for themselves.

Thank you very much, and I look forward to answering questions that you may have.

[The prepared statement of Mr. Baller appears as a submission for the record.]

Chairman SPECTER. Thank you, Mr. Baller.

Our final witness on the panel is Mr. Michael Salinger, Director of the FTC's Bureau of Economics, currently on leave from Boston University's School of Management, where he is a professor of economics. He previously taught at MIT, Columbia, and served as an economist with the FTC's Antitrust Division; a magna cum laude graduate of Yale and a Ph.D. from MIT in economics.

Thank you, Mr. Salinger, for your contribution here, and we look forward to your testimony.

STATEMENT OF MICHAEL SALINGER, DIRECTOR, BUREAU OF ECONOMICS, FEDERAL TRADE COMMISSION, WASHINGTON, D.C.

Mr. SALINGER. Mr. Chairman, my name is Michael Salinger. I am, as you said, Director of the Bureau of Economics at the Federal Trade Commission. I am pleased to appear before you to present the Commission's testimony on the FTC investigation earlier this year into the acquisition by Comcast and Time Warner Cable of Adelphia's cable assets and into related transactions in which Comcast and Time Warner Cable swapped various cable sys-

tems. After a thorough investigation, the Commission closed the matter without taking any action. The Commission's decision not to file an antitrust case was explained in a statement by Chairman Majoras and Commissioners Kovacic and Rosch and in a second statement, concurring in part and dissenting in part, by Commissioners Harbour and Leibowitz. I have submitted a written statement which represents the testimony of the Commission. My oral presentation and answers to questions represent my views and not necessarily the views of the Commission or any of the individual Commissioners.

Neither the acquisition of the Adelphia assets by Time Warner Cable and Comcast nor the system swaps between Time Warner and Comcast represented the acquisition of a direct competitor. In other words, this was not the kind of transaction that gives rise to most of the merger challenges under the antitrust laws. Moreover, several aspects of the transaction were likely to be beneficial to competition and to increase economic efficiency. Cable systems within a metropolitan area can be complementary to each other, as consolidation can make it possible to achieve economies of scale in creating a second wireline communications network that competes with the network of the incumbent local exchange company.

To be sure, the transaction did raise some competitive concerns, which the staff spent 7 months investigating. The most important of these was that a cable operator with a sufficiently large share of a metropolitan area might enter into an exclusive contract with a regional sports network, or RSN, that would make the RSN unavailable over competing media. Using economic analysis, the staff concluded that the transaction did not create an incentive to enter into such an exclusive agreement.

Of course, economics is an inherently imprecise discipline, so one must consider the possibility that developments could run counter to the staff's prediction. If that were to happen, however—that is, if Comcast or Time Warner Cable do enter into exclusive agreements with RSNs—those agreements would themselves be subject to antitrust review.

Exclusive agreements are not per se violations of the antitrust laws. Even if we knew with certainty that exclusives would be a likely result of the merger, the Commission would have to evaluate whether they are harmful to competition. Such a finding would require a showing of net harm to consumers, not just harm to competitors. That is a very hard determination to make without knowing the details of the agreement to be considered. In my opinion, the opportunity to revisit the issue if it does, in fact, arise was an important consideration in the Commission's decision.

Thank you for your attention. I would be pleased to respond to any questions.

[The prepared statement of Mr. Salinger appears as a submission for the record.]

Chairman SPECTER. Thank you, Mr. Salinger.

We have a vote, which was just started a few minutes ago, and I am going to recess the hearing for a short time to go vote and come back, and we will then begin the questions and answers.

Thank you. We stand in recess.

[Recess 10:35 a.m. to 11:05 a.m.]

Chairman SPECTER. The hearing will resume.

Mr. Baller, you say that the antitrust laws are worthless as remedies. Would you amplify your view on that a bit?

Mr. BALLER. Yes, I would be glad to, Chairman Specter. For a small company encountering anticompetitive activity, the cost involved—hiring expert testimony, engaging in time-consuming and expensive discovery, the burden involved, the—

Chairman SPECTER. You are talking now about private right of action and private litigation—

Mr. BALLER. That is correct.

Chairman SPECTER. Seeking treble damages or injunctive relief?

Mr. BALLER. That is correct. If—

Chairman SPECTER. But how about if Mr. Salinger and the FTC comes swooping in and provides these fancy economists with their extraordinary pedigrees and high- priced lawyers to bring justice to clients.

Mr. BALLER. We would love for that to occur.

Chairman SPECTER. Then the antitrust laws would be effective, wouldn't they?

Mr. BALLER. Yes, they would. They would be more effective but not entirely effective because, as Mr. Salinger said, the demonstration—

Chairman SPECTER. Why not entirely effective? They get equitable relief. They get court orders prohibiting the inappropriate conduct. They bring you lots of money in treble damages. What more do you want?

Mr. BALLER. The showing of harm to competition as distinguished to competitors makes the antitrust showings very difficult and very complex and time-consuming, even if a major—

Chairman SPECTER. To prove the case.

Mr. BALLER. Correct.

Chairman SPECTER. But the cases can be proved.

Mr. BALLER. But over what period of time? Assuming that a small competitor—

Chairman SPECTER. What would you suggest as a preferable remedy?

Mr. BALLER. Well, I suggest, No. 1, strengthening the antitrust laws. I am not suggesting that that alternative not occur.

Chairman SPECTER. Move to No. 2. You have already told us all the reasons the antitrust laws are not sufficient.

Mr. BALLER. I believe that, in addition to strengthening the antitrust laws, we should also have specific standards that are easy to understand. For example, closing the terrestrial loophole is very easy to understand. That can be effectuated. We can remove exceptions that make it difficult to apply and make the criteria more absolute, clear, give the Federal Trade Commission, the Department of Justice, or the Federal Communications Commission clear mandate and a sense of the Congress that it seeks to protect the interests of small competitors as well as the very large competitors.

Chairman SPECTER. Mr. Salinger, the 1992 legislation enacted by Congress dealt only with satellite transmission and not with cable, and the proposal was made earlier this year, taken up by the Commerce Committee, which would have primary jurisdiction on that issue, they did not pursue that, or at least not at the present time.

What reason would there be for not including cable terrestrial transmission under the prohibitions of the 1992 Cable Act?

Mr. SALINGER. Senator, you are referring to a provision that relates primarily to FCC regulations, so in general, we would defer to our sister agency for their opinion on that. But the specific answer to your question I do not know.

Chairman SPECTER. Well, the FTC has considerable expertise. You have blue-ribbon credentials: a Ph.D. in economics from MIT, magna cum laude from Yale. This is an antitrust issue. It involves a provision that Congress prohibited vertically integrated cable companies from refusing to make their contact available to competitors. And it applied only to satellite transmission and not to cable or terrestrial transmission.

What is the rational basis for that distinction?

Mr. SALINGER. As a matter of economics, it is hard to understand why there is any rational basis for distinguishing between terrestrial distribution and satellite distribution.

Chairman SPECTER. Well, would you recommend that Congress change it to include cable and terrestrial distribution?

Mr. SALINGER. Well, I think they should be treated consistently. As to whether the prohibition on exclusivity is appropriate raises more general antitrust issues, which are not so clear-cut.

Chairman SPECTER. So you are raising a question about whether the prohibition really ought to be continued. But if you did continue the prohibition, you say there is no distinction as far as your economics training would say between satellite and terrestrial.

Mr. SALINGER. Yes, that is right.

Chairman SPECTER. Mr. Cohen, I notice you having some body language in opposition.

[Laughter.]

Chairman SPECTER. You can expand on that.

Mr. COHEN. I was even going to volunteer to comment on that, although I—

Chairman SPECTER. I was coming to you in any event.

Mr. COHEN. I figured I was not going to escape here unscathed.

Chairman SPECTER. Because you already said there is good reason for it, so tell us the reason.

Mr. COHEN. First of all, I would say this: I want to second at least the implication of Mr. Salinger's comment that if we are going to look at this, I actually think the fresh look should be whether there should be any prohibition of satellite or terrestrial delivery. I believe that a rigorous economic analysis of the competitive situation today would lead to the conclusion that the prohibition on exclusive arrangements with respect to satellite-delivered programs should disappear, in which case you would have your uniform treatment between the two.

I do not want to compare my economics credentials to Mr. Salinger's. I only majored in economics at Swarthmore College.

Chairman SPECTER. Wait, I do not understand that. You were summa. He was only magna.

[Laughter.]

Mr. COHEN. He actually has a degree in economics. I do not.

Chairman SPECTER. I thought "summa" covered everything.

Mr. COHEN. Well, I will not say that. And, of course, he has Yale on his resume, and I am missing that on mine, as you have frequently observed in the past.

Chairman SPECTER. Having frequented both Yale and Penn, you do not have to take second place in any respect.

Mr. COHEN. Well, I appreciate that, and so will Andy Gutman. But there was a rational justification for the distinction between satellite-delivered programming and terrestrially delivered programming in 1992, and that is that terrestrially delivered programming was viewed by the Congress as being a more limited mode of distribution, a mode of distribution that would be primarily used for local programming. And there was a considerable legislative record on this distinction and a considerable record, by the way, supported by economists at the time that there would be a risk of anticompetitive, anticonsumer, I guess I should say, activity if you were to discourage investments in high-quality local programming. And it, therefore, is a very conscious decision to say we recognize that we are going to come in as the Government and interfere with the market here. And so, in interfering with the market, let's interfere with the market at the level where we have the greatest concern, which is the creation of national cable programming that needs to be available to this fledgling industry that we are trying to stimulate and we are trying to develop and we are trying to encourage the development of. But let's not get in the way of investments that cable companies might be prepared to make in locally delivered content, which would presumably be delivered over a terrestrial network.

I would say that Congress's judgment here proved not to be terribly mistaken. This is not an exemption—

Chairman SPECTER. Congress's judgment was not terribly mistaken?

Mr. COHEN. That is right.

[Laughter.]

Mr. COHEN. Well, I might quibble with the need to have had the—

Chairman SPECTER. Do you know that that is the nicest thing that has been said about Congress all week?

[Laughter.]

Chairman SPECTER. Go ahead.

Mr. COHEN. In fact, if we were sitting here today and there were 67 terrestrially delivered networks that were being provided exclusively on cable, and all around the country satellite or wireline overbuilders were having difficulty gaining access to all of this content, then I think there would be a legitimate question about this. But the examples of where terrestrially delivered programming is not available to competitors are so few and so far between that it is hard for me to accept that a credible, independent economist could make the case that there is any significant impairment to competition that is taking place as a result of the terrestrial exemption today.

Chairman SPECTER. Mr. Cooper, I will come to you in just a minute because I know you want to comment. But I want to follow up in a couple of regards with Mr. Cohen before moving on.

Comcast has made available to Verizon Philadelphia SportsNet, correct?

Mr. COHEN. That is correct.

Chairman SPECTER. Why did you do that on a voluntary basis?

Mr. COHEN. I think it is a question of looking at our business and looking at the business model, and we have consistently said in testimony before this Congress—

Chairman SPECTER. I commend you for doing it. I think it is very good because it helps the consumers. They do not have to make a choice based on Philadelphia SportsNet. But there is a competitive disadvantage to you to give that to Verizon, a competitor.

Mr. COHEN. That is correct.

Chairman SPECTER. And that obviously prompts the question as to why you did it.

Mr. COHEN. We made an assessment based on the overall balance of the expected size and scope of that competitor for reasons that we can discuss in another hearing. We do not believe Verizon is, for example, going to be providing service in the city of Philadelphia anytime in the near future because their business model is not to roll out their service in the city.

Chairman SPECTER. Do you think there are really not going to be real competitors to Comcast?

Mr. COHEN. No, they are going to be a competitor in the Philadelphia suburbs and in South Jersey and in wealthier communities surrounding the city of Philadelphia, but not in the city of Philadelphia per se. But, more importantly, we—

Chairman SPECTER. But Comcast relies upon the areas beyond the city of Philadelphia very heavily.

Mr. COHEN. That is correct. We have a number of ways in which we competitively differentiate ourselves from our competitors. Comcast SportsNet in Philadelphia is one of those methods. It is not the exclusive method. The bottom line here is that we have consistently represented in Congress and in front of the FCC that it is not our intention to abuse the terrestrial exemption—by the way, it is an exemption, not a loophole, that we would make the content available to wireline, facilities-based competitors, and that we do so in all of our markets. And giving access to Comcast SportsNet to Verizon was consistent with that position that we have taken.

What we say is that we have not made it available to our satellite competitors because they aggressively distinguish themselves competitively from us with their exclusive content. And what is sauce for the goose is sauce for the gander. If exclusive content on DirecTV, and in particular, the NFL Sunday Ticket, which is the single most valuable piece of exclusive sports content in the United States of America today—and if that is permissible, if that is acceptable, if that is not a problem for the United States Congress, for the Federal Communications Commission, with all due respect for everyone on this panel, then it should also be acceptable that in one market in this country we have the right to competitively differentiate ourselves with a network that we invested over $450 million in building in reliance on an exemption created by this Congress. And I would ask: What is the investment that DirecTV has made in sports programming around the country? What is the in-

vestment that DirecTV or EchoStar has made in any kind of programming around this country? What is the investment that they have made in jobs in Philadelphia? What is the investment that they have made in the community in Philadelphia? The investments that Comcast has made in programming, in jobs, in community development, are the pro-competitive, pro-consumer benefits that you get from the terrestrial exemption and from the structure of the program access rules under the status quo.

Chairman SPECTER. Do you feel strongly about that?

[Laughter.]

Mr. COHEN. I feel passionately about it.

Chairman SPECTER. That is a big subject, and I intend to come back to it because that involves the first hearing we had on NFL, and I want to move through the subject of integration and cable, but that is very much on the agenda for today. But it comes in Phase 2.

As to Comcast making your sports programming available to other cable companies, do you do that?

Mr. COHEN. We do.

Chairman SPECTER. No exceptions?

Mr. COHEN. There are no exceptions other than Comcast SportsNet Philadelphia and there are no exceptions for wireline, facilities-based competitors anywhere in the country. There are no exceptions for satellite anywhere else in the country other than Comcast SportsNet Philadelphia.

Chairman SPECTER. Okay. Dr. Cooper, you had a comment?

Mr. COOPER. Well, with respect to the terrestrial loophole and what Congress did in 1991, let us be clear that in 1992 regional clusters were a very small part of this industry. They have increased many times over since then.

Second of all, the capacity to distribute content through high broadband networks has increased dramatically, so what you now have today on a regional basis is exactly the condition that was perceived to be the problem for the Nation in terms of satellite-delivered programming. So that these clusters have grown to such an extent—we have gone from maybe 20 percent to well over 50 percent, 60 percent of systems being clustered, and those are clustered in major metropolitan areas—each of which, by the way, has a monopoly sports franchise in each of the major leagues.

So the problem that is identified here, in fact, has grown to be a regional problem, and so if Congress were to revisit this issue today, they might well look at that situation and conclude that it is exactly the difficulty of distributing content in an integrated network that they addressed with satellite for the Nation, they now need to address with terrestrial distribution for these massive regional clusters that have grown in the past 15 years.

Chairman SPECTER. Mr. Goodman, at your request we will put into the record, without objection, the documents which you have presented captioned, "Coalition for Competitive Access to Content: Vertical Integration relevant to Program Access Legislation Draft 1990–1994–2006 Comparison." That will be made part of the record.

Mr. Goodman, the Court of Appeals for the Seventh Circuit in *MCI Communications* v. *AT&T* dealt with the doctrine of essential

facilities and developed a four-part test to determine whether there would be a violation of Section 2 of the antitrust laws. And it would require first the control of the essential facility by the monopolist; second, the competitor's inability practically or reasonably to duplicate the essential facility; third, the denial of the use of the facility to a competitor; and, fourth, the feasibility of providing the facility.

Is that essential facilities—and the Supreme Court of the United States in *Turner Broadcasting* v. *FCC* implicitly endorsed the application of that standard, and in a concurrence, Justice Stevens makes a specific reference to it. The question with that introduction so that there is an understanding of what it is: Does the vertical integration sports programming arguably run afoul of that doctrine?

Mr. GOODMAN. That is not a question I am prepared to answer in the context of that. I am not an attorney per se. The vertical integration in sports is clearly a condition that can be used as leverage to deny access, and sports programming has been declared by most of the consumers that are trying to make a decision about when to buy a service that it can be essential.

Chairman SPECTER. Mr. Baller, what is your legal judgment on that? Is the integration we are talking about here today, the vertically integrated sports programming arguably a violation of the essential facilities doctrine?

Mr. BALLER. I would argue it is arguably a violation, but the essential facilities doctrine is not recognized by all circuits, and as you say, the Supreme Court has not explicitly adopted it as well.

Chairman SPECTER. So you do not think that this integration runs afoul of that doctrine?

Mr. BALLER. I would personally say I believe it is, but that does not mean that the courts necessarily have recognized the doctrine at all.

Chairman SPECTER. Well, okay. But you are a lawyer in this field. You are a specialist in antitrust laws.

Mr. BALLER. I have had experience, but I would not call myself an expert in antitrust law.

Chairman SPECTER. What is your view of it, Dr. Cooper?

Mr. COOPER. If you look at the four tests, it clearly qualifies in the sense that they control it, they have an exclusive, it is irreplaceable. There is, you know, only one baseball team in Philadelphia. And we looked—actually in my testimony, I look around and you will discover that if you look across all the major leagues, certainly in the top 25 markets in which Comcast and Time Warner are now highly concentrated and clustered, there are very few exceptions where you have more than one team in each of those sports. So it does have those characteristics that you mentioned: they control it on an exclusive basis, it is irreplaceable, there is only one team there, and if they deny the access to it, then, in fact, it meets those four tests.

Chairman SPECTER. Mr. Salinger, what is your view? I am coming to you, Mr. Cohen. I know you have a view on this.

Mr. SALINGER. I am no doubt going to get in trouble with the lawyers at the Commission for opining on the essential facilities doctrine, but—

Chairman SPECTER. Well, there is one lawyer here you will not get in trouble with.

Mr. SALINGER. Thank you, Senator.

I do not think it applies to all sports programming.

It might apply to some sports programming.

Chairman SPECTER. What is your view—Mr. Cohen, you have given a pretty good exculpatory statement already in addressing this because you are making it available to your competitors, except for DirecTV, for which you have a very strong economic reason, strong factual basis. And I am sorry that we do not have a broader panel to take a look at the other integrated operations, the Padres, et cetera, the Braves. But would this doctrine apply anywhere on the integrated line?

Mr. COHEN. I have two comments.

First of all, let's remember that under the essential facilities doctrine, you ultimately have to have an umbrella of competitive harm—harm to competition. It is not a per se violation. And I think that for anyone to—I think you have to look, and I was nodding when Mr. Salinger was talking—I think it depends on the sport and the market to be able to answer your question in an appropriate way because of the required and appropriate analysis of the impact on competition.

No. 2, I think sports is a very interesting case, and this will get me in a little bit of trouble in Philadelphia, but not anywhere else, which is that the true integration here is not the integration between the control of the network and the distribution mechanism. The true integration here would be an integration that runs from the control of the rights to the network and the distribution mechanism.

So Dr. Cooper, for example, makes reference to one baseball team being in Philadelphia. We do not own the baseball team in Philadelphia. We do not own the baseball rights in Philadelphia. And the Philadelphia Phillies, who are completely separately owned, have their own rights and their own ability to make their own programming deal. And, in fact, to require, as teams like the Chicago Cubs in the Chicago sports market—in making the deal require that that distribution be made available to all competitors, all multi-channel video competitors in the marketplace. So in the absence of what I would call full integration from ownership of the rights down to the distribution mechanism, I actually think that you probably do not qualify under the Seventh Circuit's test as an essential facility.

Chairman SPECTER. Your response, then, suggests that before you can make an evaluation of, say, Cablevision with the Knicks and the Rangers or Cox with the Padres, Time Warner with the Braves, and Charter with the Seattle Seahawks and the Portland Trail Blazers, you would have to have a market analysis, but the essential facilities doctrine might apply in those areas?

Mr. COHEN. I think it could apply, depending on the market, but it is interesting. You have ticked off a bunch of markets with a bunch of different characteristics. Take the New York market and Cablevision and its control of the MSG regional sports network. MSG used to have rights to televise the Knicks, the Mets, the Yankees, the Devils and the Rangers—had the rights to control all of

those teams. It goes to my point that to have full vertical integration, you actually have to own the teams, too, because what is happening in the New York market is that the owners of the Yankees, the Mets, the Devils, and the Rangers have all taken their sports rights elsewhere. They no longer have carriage agreements with MSG. Each of them—the Yankees, Mets, and Devils have a deal with YES, which is a non-vertically integrated regional sports network, and the Mets created their own regional sports network, which is partially owned by Time Warner, Comcast, et cetera. So that would be a vertically integrated regional sports network.

So Cablevision, which used to own the rights for all of these teams, or used to control the rights for all of these teams through contract, has now lost the rights for all the teams other than the Knicks and the Rangers, who remain on MSG.

So it is a perfect example of the fact that the controller of the rights ultimately has the ability to dictate the distribution.

Chairman SPECTER. Dr. Cooper, in your written statement, you indicate that during the dispute between Cablevision and the Yankees Entertainment Sports, known as YES Network, which owns the television rights to the Yankees, Cablevision demanded an equity stake in the Yankees Network. Could you elaborate upon what happened there?

Mr. COOPER. Well, it is interesting that he raises the point of YES because, in fact, that was a fairly ugly—

Chairman SPECTER. I am not raising the point of YES. You raised the point of YES.

Mr. COOPER. I mean Mr. Cohen did. As I understand it- -and that is just a recounting of the allegations in the lawsuit that was filed, and ultimately it went to arbitration. It was a lawsuit over carriage on a cable operator who has substantial market power in that market. And so as I understand it, I am not entirely—you know, those were the allegations that that had been demanded as part of the negotiation for carriage. And in the end, I believe YES was substantially vindicated in its court case and got carriage under terms that were favorable to it.

The suggestion here is that maybe the Congress needs to look at the exclusivity of the rights, which is something we would encourage. In either event, Comcast would lose its power to pick and choose which competitors through its distribution network would have access to the programming it controls. He has argued that, well, I do not own the team and, therefore, I have made a deal with the team to carry its programming; they did not require me to do it on a non- exclusive basis; therefore, I cannot impose exclusivity. And then he will pick and choose which competitors have access to this vital marquee programming.

If you want to solve the problem by banning exclusive rights in sports programming, that would do the job, too, because then he could not make that anticompetitive choice. He would be required by law to make that programming available to the competing systems.

Chairman SPECTER. Well, would it be desirable as a matter of public policy to prohibit exclusivity of rights?

Mr. COOPER. Where you have an underlying monopoly, it may well be, absolutely.

Chairman SPECTER. What do you think, Mr. Cohen?

Mr. COHEN. I think that is the right question, and not whether the terrestrial exemption should be continued or eliminated.

Chairman SPECTER. Well, I am glad we got to the right question.

Mr. COHEN. I think we have to be careful in answering the question because there are clearly pro-competitive benefits to exclusive arrangements. They do enable competitors to differentiate themselves from each other. And I think that is the balance of giving up the pro-competitive benefits of competitor differentiation in the market as opposed to the clear consumer benefits from an open access to what I think—if there is anything that is an essential facility, by the way, I would think that it would be the rights themselves, not the carriage of those rights. And to open those rights up to all competitors, I think, has a procompetitive benefit. And it is the balance between those two elements that makes the policy judgment difficult.

Chairman SPECTER. Mr. Cooper, coming back to your written testimony, where you raise the issue of Cablevision demanding an equity stake in the Yankees Network, can you amplify the circumstances? What are the underlying factors of the relationship and market power and distribution, et cetera, which would enable a cable transmitter to make that kind of a demand?

Mr. COOPER. Well, the general proposition I can address. It was the details of what was asked, and you ought to get the people from YES. But it is the experience in the video industry that distributors, both on the cable side, which is why we had the 1992 Act, and on the broadcast side, distributors control a vital vertical lever here. And one of the things that distinguishes this particular industry, and the telecommunications industry as well, is that that lever is a live-or-die situation for a local team to reach its local market. Where you have a substantial market penetration of that distribution mechanism, denial of access to the public gives you tremendous market power over the team. If the Yankees cannot get to the households that subscribe to cable, they have a severe problem.

So the market power inherent in that bottleneck facility is extremely strong, and it gives the owner of that facility—and it has occurred in programming both broadcast and cable, to demand unacceptable terms and conditions.

Chairman SPECTER. Okay. If Cablevision had the power to make that demand on a realistic or reasonable basis, then you are saying that the Yankees had no place else to go to have their team shown?

Mr. COOPER. Well, that was one of the four tests. Cable is the dominant medium for distributing video content in America today.

Chairman SPECTER. Well, factually, did the Yankees have nowhere else to go but Cablevision?

Mr. COOPER. In some of the market segments, they had that problem. You know, the cable companies are franchises. At the time there was no overbuilder. You have heard the proposition here that one of the economic bases on which Comcast gave Verizon the right to distribute their programming in certain suburbs was the assumption that there would not be a competitor in Philadelphia. That was the statement you heard today. It is a wonderful statement. I am going to quote it and get the record frequently, right?

Because that has been our complaint. So that was a business judgment, is that they gave them the rights because they do not expect them to be a competing multi-channel video delivery system in Philadelphia.

Chairman SPECTER. But Verizon could be a competitor in Philadelphia if it chose to do so.

Mr. COHEN. Absolutely.

Chairman SPECTER. Do you want to adopt Mr. Cohen's answer, Dr. Cooper?

Mr. COOPER. Frankly, we have been making this point. Actually, in the other Committee that deals with this, we call it redlining, you see? So, in fact, it is an interesting observation. Our complaint—and, of course, Comcast was required to build out throughout its service territory as an obligation of its franchise. And Verizon has been trying to get out of that. I was the expert witness in Montgomery County where they recently agreed to very favorable terms from my point—

Chairman SPECTER. You referred to a lawsuit. Would you amplify that?

Mr. COOPER. The lawsuit in—

Chairman SPECTER. You just said you were going to utilize what—

Mr. COOPER. Verizon sued Montgomery County claiming that its cable ordinance violated the First Amendment, and the judge ordered them—

Chairman SPECTER. Well, how are you going to use Mr. Cohen's statement in your lawsuit?

Mr. COOPER. One of the conditions that was being argued over was the build-out provision. Who are they going to serve? And the local franchising authority—and Mr. Cohen has been subject to this in his franchise agreements. The local franchising authority requires the complete build- out across the entire area of that franchise as part of his agreement. Verizon is taking the position that they do not want to have to serve everybody in the local franchising area. In the settlement, we got almost 100 percent of that build-out requirement, which is very important in the Commerce Committee.

Chairman SPECTER. I am advised that more than 3 million subscribers had Cablevision as their only choice for cable service, and in those areas, Cablevision had a 90- percent market share. I am sorry that Cablevision did not send a witness here. They were given a lot of notice, and they had no understandable explanation as to why they did not, and we may have to continue this hearing with a subpoena for Cablevision so that we can find out what is going on here.

But the ramifications and tentacles of the market share and the dominance so that Cablevision, the cable company, can make a demand for an equity share in the Yankees to get a preferred position as an ownership interest is surprising, to say the least.

Mr. Cohen, you have your hand up.

Mr. COHEN. If I can, Mr. Chairman, I do not want to attempt to speak for Cablevision, but I know a little bit about the subject in general, so it might be a little helpful to make some comments.

Chairman SPECTER. Please do.

Mr. COHEN. First of all, I do not believe that even the allegation was that Cablevision was making a demand for equity in the Yankees. I think what may have been under discussion was whether Cablevision should get an equity interest in the network itself on the theory that it was Cablevision's distribution that was going to be bringing the value to the network—not the team itself, but to the network.

I would note that recent press reports suggest that the owners of Yankees Entertainment Sports, which are the Yankees, the Nets, and principally Goldman Sachs and private equity investors, are thinking about putting the network on the market, and the asking price is on the order of $3 billion. That is billion with a B. That would make the network worth approximately three times what the Yankees are worth as a franchise. And with all due respect, the value of that network, although it comes in part from the value of the Yankees as a franchise and the Yankees as something that people want to watch, it also comes from the distribution that was required to the YES Network from Cablevision, from Time Warner, from Comcast, from DirecTV—and I forget whether EchoStar distributes the YES Network or not. So there is some justification from the distribution side of saying that it is the distribution that is giving value to these networks in addition to the franchises themselves.

Number two—and this is particularly important—if you look at the whole YES Network area, when you have a statistic like Cablevision had 3 million customers, I think Yankees Entertainment Sports is in a metropolitan area with something like 8 or 9 million customers. You have Cablevision, Comcast, Time Warner all in that territory. So when you look at 3 million customers, you are looking at a sub-segment of the YES Network's market, not the entire market.

With all due respect to that statistic, in virtually every place where Cablevision was providing service, there were at least two other competitors that were available for carriage of the YES Network—DirecTV and YES. And I know that DirecTV—I do not know about—

Chairman SPECTER. Carrying the YES Network, too?

Mr. COHEN. They were.

Chairman SPECTER. DirecTV and who?

Mr. COHEN. Well, EchoStar, the Dish network. I don't know whether Dish was carrying YES. I know DirecTV was.

Chairman SPECTER. The consumers are going to have to go to—

Mr. COHEN. They would go to a satellite.

Chairman SPECTER. To a satellite.

Mr. COHEN. Correct.

Chairman SPECTER. They would have to buy a whole new system.

Mr. COHEN. Well, they did not have to buy a whole new system because the YES Network and DirecTV ran a massive and major promotion during the course of this dispute where they offered a free dish and free multi-television set-top boxes for any Cablevision customer who would switch to DirecTV; in addition, offering discounted service for an entire year for that switch. And—

Chairman SPECTER. Do you ever have any concerns about the free offers and the discounted service for a time as to how it is going to be made up later? Is there such a thing as—

Mr. COHEN. I think it—

Chairman SPECTER. Wait a minute. Is there such a thing as a free lunch here?

Mr. COHEN. There probably—

Chairman SPECTER. Don't they have a plan to collect later?

Mr. COHEN. In the long run, that would definitely be the case, but in DirecTV's case, in cable's case, there is something called subscriber—it is called SAC charges. They are the charges, the marketing costs you expend to get new subscribers. All I can tell you is that YES publicly said that they had switched somewhere between 25,000 and 30,000 Cablevision customers to become DirecTV customers, and that YES has said that the ultimate resolution of this dispute, which by the way, was not through the litigation because there was never a decision in this litigation, was because of the pressure that was put on Cablevision through the market, that is, customers leaving and threatening to leave the DirecTV if Cablevision did not pick up the YES Network.

So I believe that the bottom line here is the market worked in the YES situation. That is why YES now has ubiquitous distribution. That is why YES is now worth $3 billion.

Chairman SPECTER. Ubiquitous distribution?

Mr. COHEN. That is correct.

Chairman SPECTER. What is ubiquitous distribution?

Mr. COHEN. They are available on Cablevision, Time Warner, Comcast, and at least DirecTV. They also have a deal with Verizon, and, by the way, Verizon is an active competitor of Cablevision's, and Cablevision's territory as well. So you have now got at least five and maybe six multi-channel video distributors that are carrying the YES Network.

Chairman SPECTER. Well, wait a minute. The question in my mind is: Where does all this leave the consumer? Where does this leave the consumer now? And where does this leave the consumer down the road? These are only partial steps in what is being undertaken. We are going to come to that in just a minute going to the NFL issue. But I am trying to understand what is happening here. A chart has been provided which shows at the top George Steinbrenner, principal owner, and minority partners, and that leads down into the Yankee Global Enterprises. And that branches off into two lines. One is the New York Yankees, and the other is the YES Network.

Now, it has been public knowledge for a long time that the YES Network was more valuable than the New York Yankees, and you say, Mr. Cohen, that they are going to rearrange with the conglomerate, it is going to be worth $3 billion, which is three times the value of the Yankees.

This is an extraordinarily complex structuring which I am concerned places the consumer at considerable risk.

You had a comment, Dr. Cooper. Then I want to move on.

Mr. COOPER. Of the six entities that Mr. Cohen mentioned, at least three of them do not compete with each other because the cable operators have chosen never to overbuild and compete. And

so you are left with the satellite, which involves significant switching costs, short-term promotion, as he pointed out, as part of this commercial dispute. And, of course, those are the competitors who he denies his programming to. And he knows that the other major cable operators are not going to overbuild him. So that list of places, what YES did was they secured distribution throughout the region because that region is splintered between a number of cable systems. Many of Comcast's regions are not. They are the dominant provider throughout the region, and, again, he has chosen not to allow that key marquee programming to be available to the one entity that actually could compete throughout the service territory.

Chairman SPECTER. Mr. Cohen, you testified earlier with considerable fervor about the Sunday Ticket. Do you believe that that arrangement between the NFL and DirecTV is a violation of the antitrust laws?

Mr. COHEN. Building on Mr. Salinger's comment about the need to look at particular sports programming in particular markets, I think if there is any sports programming about which you could make a case that it is an essential facility, it would be NFL programming. And so I am not prepared to say that I think the NFL Sunday Ticket is an antitrust violation. You are aware of the Shaw litigation in the Third Circuit, which, again, the litigation never reached the ultimate question whether the NFL Sunday Ticket was an antitrust violation, the Third Circuit only finding that the Sunday Ticket was not entitled to the antitrust immunity that was provided under the Sports Broadcasting Act. I would note, though, that before that case went to trial, it was settled. So there was at least some risk perceived by the NFL and presumably DirecTV that the Sunday Ticket could be found to be an antitrust violation.

Chairman SPECTER. Well, I know that it has not been resolved, but I was asking one astute lawyer's opinion as to whether he thought it was an antitrust violation. But I will accept your answer.

The activities of the NFL are very extensive and definitely ongoing in what they are undertaking to do. And a big question is posed by what they have done as to whether it is a violation of the antitrust laws and what is coming next. We now have the NFL Channel, and we have this year, last month, the expansion to the Thursday-Saturday Ticket, and we can expect more.

We have had the change from Monday Night Football from ABC-TV to ESPN, which is an interesting transaction, raises a lot of questions, especially since ESPN is owned by ABC- TV. And on inquiry, we find that ESPN can pay the NFL more money because ESPN has two revenue streams: one, the advertising, which is somewhat less—how much less I do not know, but I am advised not appreciably less—than over-the- air transmission by ABC; but ESPN also has the revenue stream from subscriptions from the subscribers. I am advised that it is $500 million more a year, and what it appears to be is that the NFL makes an evaluation as to how much they can extract, how much can they extract from ESPN, a subsidiary of ABC, to carry the Monday night games on ESPN. And ABC-TV on Monday night games, an enormous demand. You would think if anybody could survive and afford the

programming, ABC-TV could. But they could not when the NFL decided to raise the prices.

Now, the NFL enjoys all of this maneuvering room because they have the antitrust exemption. The teams are not guilty of conspiracy and restraint of trade because they got the antitrust exemption. But if they did not have the antitrust exemption, then the San Diego Chargers could negotiate, and if you could not get them, you could get the Seattle Seahawks, or you might get some other team. But the variety of distribution chains are not free to negotiate because the NFL has it all.

What good reason, Mr. Salinger, is there for leaving that antitrust exemption in place?

Mr. SALINGER. Senator, as a general principle, I think that special antitrust laws for particular industries are a mistake, that we should use the same antitrust principles across different industries.

As to whether it should be illegal for the NFL to negotiate television rights, as a single entity—

Chairman SPECTER. Well, wouldn't the consumer be better off if the sports teams were negotiating on their own so that there would be competition as to what football team would be shown on what network and what channel as opposed to having all the bargaining rights in the NFL, which they can have because they have an exemption under the antitrust laws? There is no doubt that it is collusion if it is an agreement of two or more parties, which has the impact of restraining trade. What is the justification for that in this day and age with what the NFL is doing?

Mr. SALINGER. Well, it is two or more parties that are engaged in a joint venture, and so that complicates the analysis substantially.

Chairman SPECTER. Well, it is a joint venture.

Mr. SALINGER. I don't know whether legally the NFL is a joint venture, but the product that they are providing requires the existence of the league. One team cannot provide that product.

Chairman SPECTER. Well, they cannot provide the entire product, but one team can provide rights to televise their games.

Mr. SALINGER. That is correct. But the league needs to make joint decisions and joint investments, and that—

Chairman SPECTER. I know, and that stops individual cable companies or individual distributors from negotiating with teams.

Mr. Goodman, any reason to keep that antitrust exemption in place?

Mr. GOODMAN. I am going to defer to the lawyers.

Chairman SPECTER. Why are you doing that? You represent the consumers. I am not going to put you on the next panel, Mr. Goodman. You represent the consumers.

Mr. GOODMAN. The NFL and the process of those negotiations gets to prices that a lot of consumers do not want to bear, and I think that is more the consumer issue than the antitrust issue. You have in the current carriage deals today a structure—

Chairman SPECTER. Is your microphone on?

Mr. GOODMAN. I am sorry. You have in the current structure today bundling and carriage deals that cause professional sports, NFL, et cetera, to be packaged in with what is called the Expanded Basic. In that Expanded Basic, you have someplace between 40 to

60 percent of the customers paying for that that do not want that particular content, they do not particularly want to pay for it. You have—

Chairman SPECTER. That is the whole basis of the controversy that Comcast is having now with the NFL.

Mr. GOODMAN. Correct.

Chairman SPECTER. NFL wants it on the basic line. Comcast wants to put it on the sports line for the people who want it who can see it.

Mr. GOODMAN. Correct.

Chairman SPECTER. And this is the NFL exerting its power right down to the last nub, right down to the last nickel. Go ahead.

Mr. GOODMAN. Correct. I mean, it is interesting that they are taking that position on that particular set of content when they are involved in all sorts of other bundling arrangements.

One of the things I would encourage everybody to look at long term is what happens to these kinds of contracts and structures as we move to digital carriage. When we move to digital carriage, then a lot of the technical and business issues that have led to the bundling and packaging that we have got today are not going to be as relevant. And hopefully we will get to a different structure.

Chairman SPECTER. Dr. Cooper, I noticed you would like recognition. On what issue?

Mr. COOPER. On this issue.

Chairman SPECTER. Good. Proceed.

Mr. COOPER. I mean, two of my four recommendations address this fundamental problem. Disney maximizes the extraction of rent because of two practices we think are anticompetitive and anticonsumer in this case—that is, ABC ties its programming together in big bundles, demanding carriage for a set of programs, not negotiating individually for each, and then the cable operators bundle those together and do not give the consumer the choice.

If you break those two links, the study we saw is that 75 percent of the people would not pay the $2 a month or plus that ESPN gets to be put into the Expanded Basic bundle. That is why we believe breaking these ties would, in fact, begin to exert consumer demand genuinely at the point of sale.

Chairman SPECTER. Breaking what ties?

Mr. COOPER. The ability of ABC to insist that their bundle of programs be carried using the leverage of their must-carry and retransmission rights. Remember, Congress gave them rights to carriage. And, two, that cable operators be required to offer consumers a choice to buy the individual programs that they also offer in the bundle.

Imagine if consumers could choose not to pay for ESPN, just as Comcast is saying maybe they should be allowed to choose not to pay for MASN, right? The consumer would then be sovereign, which is the objective here. In this current environment, consumer elasticity of demand has been dulled dramatically by these massive bundles—

Chairman SPECTER. How about the antitrust exemption? Should that remain?

Mr. COOPER. The antitrust exemption would be one way to diminish the market power of the league.

Chairman SPECTER. Should we eliminate the antitrust exemption?

Mr. COOPER. I believe CFA has supported the elimination of those antitrust exemptions across the major league sports.

Chairman SPECTER. Mr. Baller, should we eliminate the- -revise the 1961 antitrust exemption for the NFL?

Mr. BALLER. For all major sports. We have had problems with Major League Baseball as well, and I think that it would be in the consumers' interest to eliminate the exemption across the board, if possible.

Chairman SPECTER. Well, is baseball engaging in the same kinds of practices that the NFL is?

Mr. BALLER. I cannot say for sure. My experience is limited to a town named Bristol, Virginia, on the border of Tennessee, not—

Chairman SPECTER. Is hockey doing what the NFL is doing?

Mr. BALLER. I don't—

Chairman SPECTER. Is the NBA doing what the NFL is doing?

Mr. BALLER. I have no experience.

Chairman SPECTER. Well, I would be reluctant to use too broad a swath here unless we see what they are doing, unless we see that they are anticonsumer. But what we are getting with the NFL, the raising of pay television through the add-ons and extracting—not allowing the sports channel to carry it where they could get a substantial amount of money.

Mr. Cohen, should we legislatively change the antitrust exemption that the NFL has?

Mr. COHEN. I noticed you changed the form of the question for me, which I appreciate, because I think the answer to that question is yes. I think the answer to the question you asked everyone else, which is should we eliminate the antitrust exemption for—it is in the Sports Broadcasting Act of 1961 for the NFL. I think that answer is no, and I think it goes in part, again, to what Mr. Salinger said.

I do think that there is a proconsumer justification for leagues negotiating certain television rights on behalf of all of the teams. I think, however, in granting that type of an exemption from antitrust scrutiny, it would be appropriate for Congress in the NFL's case, which, unlike all the other sports, negotiates 100 percent of the television rights in the league on behalf of all of the teams. In all the other sports, there are national rights, but there is a substantial chunk of rights that are retained by the individual teams to be able to market and negotiate over. So the NFL is a distinct case because, No. 1, it controls all of the rights of its teams, and, No. 2, because of the market power that I believe the NFL has in television rights, sports television rights, as compared to the rest of the teams. And I believe it would be appropriate for this Committee and this Congress to look at appropriate conditions to be put on a continuing exemption—on a continuing immunity from the antitrust laws as opposed to the blanket immunity that exists in the current legislation

Chairman SPECTER. Well, Mr. Cohen, this Committee and this Senator has considered conditioning the antitrust exemption on a variety of factors. It is very difficult for the Congress to anticipate and understand all the potential ramifications as to when we start

to deal with part of it and not all of it. If we take away the antitrust exemption for the NFL to deal jointly, then the market comes in. And there are very powerful reasons to allow the market to govern, which we do not anticipate. Nobody since Adam Smith has been as smart as the market. So if we take away the antitrust exemption, you have the market coming in.

I introduced legislation in the 1980's to condition the antitrust exemption of the NFL on limitations of franchise moves. When they wanted to move the Philadelphia Eagles to Phoenix, I introduced that legislation. We had a very spirited debate at that table in about 1982 between Pete Rozelle, the Commissioner of Football, and Al Davis when they moved the Oakland Raiders to Los Angeles, and they had antitrust litigation that Mr. Davis won. And then the NFL has permitted franchise moves with the Colts, in the middle of the night Irsay going to Indianapolis, the Browns coming from Cleveland, disrupting fan loyalties in a major way.

Of course, baseball is not immune either, taking the Dodgers from Brooklyn in 1958 because Walter O'Malley got a lot of prime real estate in Los Angeles, and the Giants joined. The fans be damned. And now it is the consumers be damned with what is happening.

But as I look at what the NFL is doing today, with the NFL Channel, with the DirecTV, which you spoke about passionately and eloquently, in terms of limiting—a lot of people, including myself, would like to be able to have that ticket. But I have got to have a dual system. I have got to go to satellite. And what is coming next?

When you look at ESPN taking over Monday Night Football, the NFL decides how much they can extract. And then the structure is reworked between ABC-TV and ESPN.

I am going to introduce legislation in the next session to take away the antitrust exemption from the NFL, and I think that they are building a very, very strong case—the NFL is building a very, very strong case to have Congress take away the exemption that was granted in the 1961 legislation. If someone is wise enough to tell us how to condition it, we would certainly be interested in considering that. But the market is—you do not have to be very smart to be smarter than the Congress. But the market has demonstrated its wisdom, and that is where my inclination is.

But as I take a look at what is happening here, I like the competition that is coming in with Verizon and the competition that is coming in, and satellite competition is good. But I am not sure we do not have to make some changes legislatively on integration, but before we do, we have to understand it. We are a good ways away from that. I know there are a lot of charts a lot more complicated than this one in the offing.

I will give each of you a chance to make a closing statement. Mr. Baller, you have your hand up. You are first.

Mr. BALLER. Okay. Thank you very much. As I heard you say that you are considering introducing legislation, I had—

Chairman SPECTER. I am not considering it. I am going to do it.

Mr. BALLER. All right. I had a flashback to the hearing that I mentioned at the outset of my testimony that occurred in this room in February of 2004. At that hearing Senators Kohl and DeWine

announced that they were going to introduce legislation to eliminate the terrestrial loophole. And after that hearing, Comcast announced that it was going to fix this problem everywhere. It was only then that some of our clients, including the Borough of Kutztown, Pennsylvania, were able to get Comcast programming—sports programs in that case.

Now, Kutztown could not have brought an antitrust action. It has a population of only 5,000. That kind of litigation would have been impractical. And it seems to me that having rights of that kind cannot be left to coming to the Senate and having a Senator or two Senators say they are going to introduce legislation. If it is a good idea—and I believe it is—it ought to be put into a statute so that everyone understands it and everyone can live by it. And I think that it is solutions of that kind that we need and not solely reliance on antitrust remedies. That may work for Verizon, but it does not work for the small to medium-sized competitors who we want to succeed.

Chairman SPECTER. Mr. Salinger, do you have a closing statement you would like to make?

Mr. SALINGER. Senator, no, I do not.

Chairman SPECTER. Dr. Cooper?

Mr. COOPER. I think you have heard a number of reasons why consumers continue to be very upset about their cable bills. There are sources of market power in this industry in both distribution, in carriage rights, and I honestly believe that the NFL would not be able to extract those rents if this structure were not set up the way it is.

You have identified the antitrust exemption underlying the franchises and the leagues. We also have a terrible problem of market power in the distribution and the rules that were set up about the bargaining power that programmers and cable operators have, all of which is being used and has been used for a couple decades to the detriment of the consumer. And the competition we see is not sufficient to alleviate the problem.

Chairman SPECTER. Mr. Goodman, a concluding statement?

No, Mr. Goodman, I am the Chairman. Mr. Goodman, a concluding statement? Senator Kennedy made that mistake.

Mr. GOODMAN. I think that Mr. Cohen has put the context of what is going on, on the table. Their specific goal is to get the current laws repealed. The goal of the group that I represent is to highlight the fact that the current vertical integration, as we submitted, is actually more powerful and has the ability to affect the market as much today as it did in 1992.

The access that we have has only come through very constant confrontation, and as Jim Baller mentioned, we can give you a list of specific moments in time related to mergers and acquisitions or hearings here or other activities that resulted in our finally getting access to content. It has not come because of just willing give it to us.

When we look forward and we look at the new structure and we look at the level of vertical integration, we believe that you just are going to have to maintain these rules of access to content with some expansion and clarification, or you are not going to have the competition you want.

Chairman SPECTER. Mr. Cohen?

Mr. COHEN. Thank you very much, Mr. Chairman. Three quick points.

Number one, the market is working. The video distribution market is vigorously competitive. I controlled myself until the very end, but I hold up today's Wall Street Journal with the headline, "Cable rate increases are smallest in years," and making the case that consumers have more choice today than they have had at any time in the—

Chairman SPECTER. Is 3.2 percent that I saw in the Philadelphia headlines for Comcast the smallest in recent years?

Mr. COHEN. It is the smallest in that market. But in many of our markets, the increases are even lower. And, in fairness, Mr. Chairman, you have to look at our entire package of services. For the fifth consecutive year, we are not raising the price on our high-speed data service. We are all around the country offering a triple-play bundle of telephone, high-speed data, and digital cable service for $99 a month. This market is vigorously competitive and working.

Number two, the current program access regulations are based on a 1992 model of the world. That model has changed. Notwithstanding any general statements that can be made here today, the indisputable statistical evidence is that vertical integration in our space is dramatically reduced today—57 percent in 1992 to less than 20 percent in the world today.

And, No. 3, trust the antitrust laws. There is no reason why this particular industry needs special regulation. Any abuses that could arise can be handled through the antitrust laws, and if they cannot be handled by individual plaintiffs, the FTC and the Department of Justice and this Committee and the House Judiciary Committee have plenty of capacity to be able to influence behavior in the market where it is necessary to do so.

Chairman SPECTER. So let the market govern without the antitrust exemption.

Mr. COHEN. There is no antitrust exemption that applies to us, so I think I gave my view on the antitrust exemption.

Chairman SPECTER. Mr. Cohen, staff has just handed me a listing from Bernstein Research dated November 30, 2006, which has a listing of Comcast in about a dozen markets, showing an average of 5.4 percent. I would like you to take a look at that and see if that is accurate.

Mr. COHEN. I have seen the Bernstein report, but I will note that that report references our basic cable rate increases. It does not reference what happens with our digital packages, with our premium services, with our set-top boxes, with our high-speed data, or with our Comcast Digital Voice product.

The overall rate of increase that an average Comcast customer will pay this year will be approximately 3 percent.

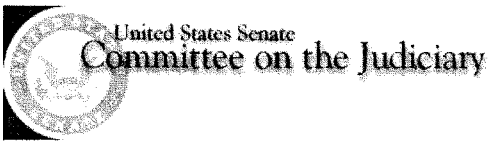
Chairman SPECTER. Gentlemen, thank you very much. It has been a very illuminating hearing.

That concludes our hearing.

[Whereupon, at 12:15 p.m., the Committee was adjourned.]

[Questions and answers and submissions for the record follow.]

SUBMISSIONS FOR THE RECORD



December 7, 2006

Testimony of
James Baller
Senior Principal
The Baller Herbst Law Group, PC
Washington, DC

"Vertically Integrated Sports Programming: Are Cable Companies Excluding Competition?"

Good morning Chairman Specter and members of the Judiciary Committee. I appreciate your invitation to testify, and I am honored to be here today.

Since 1992, I have provided legal services to dozens of public and private providers of competitive communications services. I have also assisted several national and state associations that support such endeavors, including the American Public Power Association, the National Association of Telecommunications Officers and Advisers (NATOA), and the Fiber to the Home Council.

Over the years, I have seen at first hand a wide range of practices through which incumbent cable operators have sought to thwart competition from my clients and similarly-situated entities. At a hearing in this room held on February 11, 2004, NATOA presented to this Committee an extensive report documenting dozens of examples of such practices.[1] Many of these anticompetitive practices are still occurring today, and they need to be curbed, once and for all. I applaud Chairman Specter for focusing on programming access in this hearing, and I hope that the Committee will address the other problems next year.

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[1] The report is available online at http://www.baller.com/pdfs/bh_anticomp_report.pdf.

In my testimony today, I would like to make three main points. The first point is that it is critically important not to treat programming access as just a cable entertainment issue, but to treat it as well as an infrastructure issue that is essential to America's local, regional, and global competitiveness.

As the Committee is aware, America's international ranking in broadband deployment has fallen precipitously in the last decade, from 1st in the world in the mid-1990s to as low as 21st today in some studies. The United States is also falling increasing behind the leading nations in access to high-capacity Next Generation Networks and in cost-per-unit of bandwidth, in which we now rank 6th, according the International Telecommunications Union. These are alarming trends, because virtually everything that we do at home, at work, and at play will increasing be done through broadband platforms. As a result, the nations that lead the way in developing Next Generation Networks will be the ones that are most successful in the emerging knowledge-based global economy. Please see my first handout for much more information on this.

A century ago, when electricity was the must-have technology of the day, the private sector could not alone electrify America fast enough to meet demand, particularly in rural areas. Recognizing that electrification would significantly enhance economic development and quality of life, thousands of unserved or underserved communities stepped forward to form their own electric utilities. Most of those that did thrived, while many that waited for the private sector to serve them did not.

Today, the history of electrification is repeating itself in the communications area, and many communities across the United States, are ready, willing, and able to do their part to help America develop high-bandwidth Next Generation Networks as rapidly as possible. In this, they want to stay abreast of the most progressive municipalities in the leading nations, as you will observe from my second handout.

If we are to succeed as a Nation in developing Next Generations Networks as rapidly as possible, we must ensure that they can be economically viable. Such networks are highly capital intensive, and they are affordable only if used to provide all major products and services, including voice, video and broadband data. Denial of access to critical video programming, particularly sports programming, is thus not just harmful to competition in the market for cable television, but it can destroy the economics of Next Generation Networks and impair America's ability to stay competitive in the global marketplace.

Second, as the Federal Communications Commission has repeatedly found since Congress included programming access safeguards in the Cable Act Amendments of 1992, these safeguards have played an essential role in creating and maintaining a competitive environment in the cable industry. If Congress is serious about preserving this competitive environment, it must update the programming access provisions to keep pace with the significant technological and other changes that have occurred in the marketplace since 1992.

Specifically, it its crucial for Congress to remove the so-called "terrestrial loophole" that allows cable operators, by delivering video content through fiber optic cables, to escape the Cable Act's current satellite-oriented programming access requirements. I do not agree with the testimony claiming that this is a solution in search of a problem. I can cite many examples of public communications utilities that have encountered programming access problems, including several in just the last three years – e.g., Braintree, Massachusetts; Kutztown, Pennsylvania; Wadsworth, Ohio. This is not a problem that Congress should allow incumbent cable operators to create or remove at will. Given the huge capital investments that Next Generation Networks require, current and potential providers, investors, and the public need, and are entitled to, certainty about access to critical video programming.

Third, when faced with anticompetitive practices by incumbent cable operators, small to medium-sized entities, such as my clients, can take little, if any comfort, from the antitrust laws.

For such entities, the time, cost, burden, and uncertainty of pursuing antitrust remedies render such remedies all but worthless. What we need are clear and objective statutory safeguards that are easy to understand, that lend themselves to prompt and effective enforcement, and that provide sufficiently onerous multiple damages, penalties, and attorneys fees to deter non-compliance. Congress should also ensure that the Department of Justice, the Federal Trade Commission, and the Federal Communications Commission have clear jurisdiction and a mandate to protect small competitors from anticompetitive practices, including denial of access to critical content.

Thank you very much. I would be glad to answer any questions that you may have.

TESTIMONY OF
DAVID L. COHEN
EXECUTIVE VICE PRESIDENT
COMCAST CORPORATION

BEFORE THE
U.S. SENATE
COMMITTEE ON THE JUDICIARY

HEARING ON
"VERTICALLY INTEGRATED SPORTS PROGRAMMING:
ARE CABLE COMPANIES EXCLUDING COMPETITION?"

DECEMBER 7, 2006

Mr. Chairman and Members of the Committee:

Thank you for inviting me to testify today. I welcome the opportunity to continue a dialogue with you about the intensely competitive marketplace for communications and video services. In particular, I appreciate the privilege of sharing with you Comcast's experience and insight into issues related to vertical integration in the creation, aggregation, and distribution of video programming, including sports programming.

Consistent with my testimony at the hearing you held six months ago, I want to emphasize again today that video businesses are intensely and increasingly rivalrous and that American consumers enjoy access to a greater abundance and diversity of programming, delivered in more different ways, than at any point in history. But, focusing specifically on the subject of this hearing, I want to make three main points about vertical integration and how it impacts the video marketplace.

First, as a matter of policy, vertical integration is generally good for competition and consumers. This is true in many different sectors of the economy, and it is true in video businesses as well. Many of the cable programming networks that American consumers take for granted today came into existence only because cable operators were willing to invest in the creation of new programming.

Second, as a matter of fact, vertical integration in the cable industry has declined enormously over the past decade. It wasn't all that long ago that over 50% of the networks that cable operators carried were owned or controlled by cable operators, and the percentage of affiliated networks was steadily rising. But, in this new century, vertical integration has steadily declined year after year and we believe it is now approximately 12%. At Comcast, we have an ownership interest in less than 7% of the networks that we carry in a typical cable system.

Of course, many of the networks that we carry are vertically integrated with other companies -- especially the four major broadcast television networks. News Corp., for example, is the most vertically and horizontally integrated media company in the world.

Third, in light of the intense competition that now pervades the video marketplace, and the benefits that can flow from vertical integration, it is my opinion that the solution to any problems caused by vertical integration lies in the antitrust laws. In particular, I will explain why I believe that the antitrust laws are far superior to sector-specific regulation in addressing concerns about the potential for anticompetitive behavior. I will also touch on ways in which antitrust exemptions can create competitive distortions and injure consumers.

I. THE VIDEO MARKETPLACE IS INTENSELY COMPETITIVE AND TODAY CONSUMERS CAN RECEIVE MORE PROGRAMMING FROM MORE SOURCES VIA MORE MEANS THAN EVER BEFORE.

Any analysis of existing laws or of proposals to change the laws should begin with an analysis of the relevant marketplace. In the video marketplace, two segments of the marketplace are particularly relevant to this hearing: programming supply and programming distribution. Because market power is a prerequisite to any antitrust concern, let me first clear up any misconception about competition in these segments.

Two years ago, the Federal Communications Commission ("FCC") concluded that: *"[T]he vast majority of Americans enjoy more choice, more programming and more services than any time in history."*[1] Yet the competition that exists today is far greater than existed then. This competition has driven our company, and the entire cable industry, to improve. More importantly, it has given the American consumer the richest cornucopia of video programming in the world, with extraordinary diversity of voices and content, meeting almost every conceivable need and interest.

In the past, when Congress and the FCC assessed competition in video distribution, the analysis was often confined to a subset of the video marketplace, that is, to what they call the "multichannel video programming distributors," or "MVPDs." Today, even if one adheres to this artificially narrow focus, which ignores a profusion of new video distribution mechanisms, the marketplace is intensely and increasingly competitive. MVPDs include not just traditional cable television operators but also "broadband service providers" like RCN, WOW, and Knology; direct broadcast satellite ("DBS") providers like DIRECTV and EchoStar's Dish Network; local exchange carriers like Verizon and AT&T; providers of Multichannel Multipoint Distribution Service; electric utilities; and satellite master antenna TV systems.

Taken as a whole, the growth of these competitors has been extraordinary since Congress passed the Cable Television Consumer Protection and Competition Act of 1992 ("1992 Cable Act").[2] At that time, Congress foresaw the possibility of significant *potential* competition from these providers of multichannel video services, and it took measures to promote that competition. Today, that competition is real, robust, and thriving, as the most recent data from the FCC and other sources affirm.

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[1] *In re Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, 10th Annual Report, 19 FCC Rcd. 1606 ¶ 4 (2004).

[2] Pub. L. No. 102-385, 106 Stat. 1460 ("*1992 Cable Act*") (codified at 47 U.S.C. §§ 521-555a).

Given the seismic changes that are occurring in the video marketplace, to focus exclusively or even primarily on MVPDs is myopic and misleading. Today, American consumers enjoy an unprecedented array of other means for how, where, and when they can obtain video programming. Increasingly, they consume what they want, when they want it. The source may be an over-the-air broadcast, a digital video recorder ("DVR"), an Internet download, or a video-on-demand ("VOD") server. The content may be a full-length movie or a 30-second video clip. The viewing device may be a 60-inch high-definition television ("HDTV"), a mobile device with a three-inch screen, or a PC with a 20-inch screen. Consumers, not programmers or distribution companies, are now sovereign.

A. Video Distribution Is Highly Competitive.

Viewed over the period of time since Congress enacted the 1992 Cable Act, the growth of DBS has been remarkable. DIRECTV and EchoStar each offer their services to almost every household in the United States, and between them they have captured over 28.5 million customers -- more than any single cable company. Each year for the past five years, the DBS companies have added two to three million new customers, while the cable industry in the aggregate has added approximately zero. The two major DBS companies now serve 30% of all MVPD subscribers, and they are the second and fourth largest MVPDs in America.

Local exchange carriers like Verizon and AT&T (both Bell Operating Companies that continue to provide telephone service to over 90% of all the households in their service areas and have resources far beyond those of any traditional cable company) are also making a large-scale entry into the multichannel video marketplace and are poised to become formidable competitors. For example, in the last year alone, Verizon has deployed its cable services to consumers in California, Florida, Maryland, Massachusetts, Pennsylvania, New York, Texas, and Virginia. As of September 30, 2006, it offered cable service to over 1.2 million households. Verizon expects that number to rise to 18 million households by the end of 2010.[3] Just this past Monday, Verizon announced that its cable service "is available now to 80,000 households in parts of 35 communities" in the greater Philadelphia area.[4]

AT&T is moving a little more slowly, but it plans to offer its cable service to about 90% of what it regards as "high value" customers and 70% of "medium-value" customers in the areas where it currently provides telephone service (while bypassing all but a few "low-value" customers).[5]

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[3] *See* Press Release, Verizon Communications Inc., *Verizon Provides New Financial and Operational Details on its Fiber Network as Deployment Gains Momentum* (Sept. 27, 2006), *available at* http://investor.verizon.com/news/view.aspx?NewsID=773; *see also* Tilde Herrera, *Verizon Expands FiOS TV Service*, Bradenton Herald, Oct. 4, 2006, at 1.

[4] Press Release, Verizon Communications Inc., *TV as You've Never Seen It Before: Verizon Launches FiOS TV in Greater Philadelphia Area* (Dec. 4, 2006), *available at* http://newscenter.verizon.com/press-releases/verizon/2006/tv-as-youve-never-seen-it.html.

[5] *See Project Lightspeed*, SBC Communications Conference Call 14 (Nov. 11, 2004).

Meanwhile, both Verizon and AT&T, as well as BellSouth and Qwest, are successfully partnering with the DBS providers to provide video options to consumers today in areas where they have not yet deployed their own cable services.

MVPDs, however, are not now, nor have they ever been, the only source of video programming. Anywhere from 15-20 million households prefer to rely on over-the-air television. Tens of millions of Americans also supplement their viewing with DVD and videotape rentals and purchases, and Netflix has become a national phenomenon. Additional video options, which are becoming more popular every day, include iPods, mobile phones, and broadband Internet.

Probably the most significant developments of the past year have taken place in video available through either Internet streaming or downloads. As Comcast recently pointed out in the FCC's annual inquiry on the status of competition in the video marketplace, in July 2006 alone, 107 million Americans, or three out of every five Internet users, viewed video online.[6] According to *The Wall Street Journal*, "video Web sites now draw users in numbers that rival those of cable and satellite companies."[7] It is unlikely that anyone would have imagined that, when YouTube launched last December, it would be acquired by Google less than a year later for $1.65 billion. Nor was it foreseeable, just a year or two ago, that every major broadcast network would be offering a selection of its most popular shows over the Internet.

And consumers are increasingly freed from the boundaries of time and space. DVRs, VOD, Internet streaming and downloads, and new mobile devices make it possible to watch video at a time and place of the user's choosing, rather than being constrained to view it only when it appears on a linear network and only if one is home and available at the appointed hour.

In this unbelievably dynamic marketplace, neither Comcast nor anyone else can rest for even a moment. Each and every day, we compete to attract new customers and to keep our existing customers happy. This is why Comcast alone has spent over $45 billion since 1996 to add the channel capacity that allows us to deliver 200 or more video channels to almost every home we pass... and added dozens of international and foreign-language channels... and added a dozen or more HDTV channels in every market... and become the industry leader in providing VOD, offering our digital homes over 8000 different programming choices any time, day or night, in every conceivable niche, including more local programming and -- now -- high-definition VOD as well. We have to work extremely hard to remain our customers' first choice. The way that we do that is

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[6] *See Study: 107 Million People Viewed Online Video in July*, USA Today, Sept. 28, 2006 (noting that "107 million people streamed or downloaded nearly 7.2 billion video clips -- an average of 67 apiece"), *available at* http://www.usatoday.com/tech/news/2006-09-28-online-video-study_x.htm; *see also* Kimberly S. Johnson, *Web TV Network Makes New Waves*, Denv. Post, Nov. 2, 2006 ("Internet-based videos and television shows are soaring in popularity among viewers, investors, and advertisers."), *available at* http://www.denverpost.com/business/ci_4588024.

[7] Ellen Sheng, *As Internet TV Gains Popularity, Cable Firms Bulk Up Offerings*, Wall St. J., Sept. 27, 2006, at B4.

by constantly investing in more capacity so that we can add new programming, new channels, and new features.

Comcast offers consumers the highest quality programming and, we think, the highest quality video services available in the marketplace. This is a direct result of the investments we made in response to intense competition. The claim that competition is not robust because cable prices have not decreased is false. In fact, according to some economists, DBS competition has constrained cable prices substantially and "without DBS entry[,] cable prices would be about 15 percent higher and cable quality would fall."[8] Moreover, modern economic theory recognizes that lower prices are not the only manifestation of vibrant competition: improved quality and service also are natural competitive responses to increased competition.[9] It is not unusual for prices not to drop in intensely competitive markets, especially where significant costs are created at different layers in the distribution chain. In the video marketplace, competition has manifested itself in substantial service and quality enhancements.

In short, the video distribution marketplace is more competitive and diverse than ever. As Congress looks to the future, it is wrong to view television as it was viewed in 1992, or 1996, or even 2000. It is an entirely different marketplace, and is fundamentally and irreversibly competitive.

B. Video Content Choices Are Abundant.

The explosion of distribution capacity and outlets has launched a corresponding explosion in content. When the 1992 Cable Act was passed, there were approximately 68 national programming networks (and only a dozen or so regional networks) in operation in the United States.[10] The majority of them were owned by cable companies (largely because independent programmers, the broadcast networks, and the Hollywood studios were not willing to invest in cable programming at the time). In fact, 57% of cable networks had "some ownership affiliation with the operating side of the cable industry."[11]

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[8] Austan Goolsbee & Amil Petrin, *The Consumer Gains from Direct Broadcast Satellites and the Competition with Cable TV*, 72 Econometrica 351, 351 (2004). Goolsbee & Petrin find that

> For cable subscribers, our results suggest that cable prices are at least $4 per month lower than they would have been [without DBS entry]. In the aggregate, given 70 million cable subscribers, the price effect yields a total welfare gain of about $3.3 billion for the consumers that stay with cable. The quality improvements to cable characteristics are worth approximately another $1 per month of surplus, which adds another $800-900 million to the welfare change.

Id. at 377.

[9] *See, e.g.*, *id.* at 370 ("In most empirical work [the incumbent firm's response to entry] is ignored, even though it can substantially impact consumer welfare. In the cases where it is recognized . . . , incumbents are assumed to respond only by changing prices. Because of the rapid rise of DBS and the fact that it [was] a higher quality alternative [in 2001] on many dimensions, we examine the response of both cable prices and cable characteristics to entry.").

[10] H.R. Rep. No. 102-628, at 41 (1992) (noting that there were "68 nationally delivered cable video networks").

[11] *Id.* (noting that "39 [of the 68], or 57 percent, have some ownership affiliation with the operating side of the cable industry").

The average household did not have cable at all, and those that did normally had access to 36 or fewer channels of programming (all analog).

Fast forward to 2006. Incredibly, today, of the 531 national networks, the FCC reports that cable operators have an interest in approximately 20 percent of them, although our data shows that the number is closer to 12%.[12] On a typical Comcast system, we have a financial interest in less than 7% of the networks that we carry. Meanwhile, the number of national programming networks affiliated with broadcast networks or broadcast stations has increased dramatically -- as of the FCC's latest report, 26.6% of the 531 total networks were owned by a media entity, such as a broadcast network or station, but not by a cable operator.[13] For example, News Corp. has a financial interest in over 54 programming networks worldwide, of which more than 19 are national programming networks distributed in the United States.[14] Approximately 85% of all American TV households take service from an MVPD, and a typical MVPD household enjoys access to over 200 video channels. In addition, many producers -- both majors and independents -- are creating programming for VOD, and some have used VOD exposure as a springboard for the creation of new full-time channels.

Meanwhile, the Internet has made it easy for anyone with a video camera and an Internet connection to become a programmer. Anyone can instantly make one's content available to hundreds of millions of broadband-empowered viewers around the world. Millions of videos have been posted to the Internet, where they can be accessed by anyone with a broadband connection. "YouTube, the country's No. 1 online-video site, had more than 34 million unique visitors in August, according to Nielsen.Net Ratings."[15]

Four important developments contributed to this proliferation of programming choices:

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[12] *See In re Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming,* Twelfth Annual Report, 21 FCC Rcd. 2503, ¶ 157 (2006) ("*12th Annual Report*"). In the *12th Annual Report*, based on data as of June 30, 2005, the FCC found that 21.8% of national programming networks were vertically integrated with cable operators, but this finding was based on a computation that counted a single network, iN DEMAND, as if it were 60 separate networks. *See id.* ¶ 157 & n.568. The FCC noted that, "[i]f we count iN DEMAND as one network, 57 satellite-delivered national programming networks are vertically integrated with one or more . . . cable operator[]," *id.* ¶ 159, which would mean 57 out of the total 472 (or approximately 12.1%) national programming networks are vertically integrated with a cable operator.

[13] *See id.* ¶¶ 160-161.

[14] *See generally* News Corp., *Form 10-K* (Aug. 23, 2006), *available at* http://ccbn.10kwizard.com/download.php?repo=tenk&ipage=4350417&format=PDF&cik=0001308161; *12th Annual Report* app. C-1; News Corp. Web Site, *at* http://www.newscorp.com; Star Group Ltd., *Star Brands, at* http://www.startv.com/corporate/about/starbrands.htm. Of the 54 worldwide programming networks, DIRECTV, which is owned by News Corp., carriers over 30 networks -- 26 of those are sports networks, including 21 regional sports networks. The number of affiliated networks DIRECTV carries is almost twice as many as Comcast carries.

[15] Sheng, *supra* note 7, at B4 ("MySpace was second with 17.9 million unique visitors. In comparison, Comcast, the country's largest cable company, has 24 million subscribers and DIRECTV, the largest satellite-TV provider[ ], has 15.5 million U.S. subscribers.").

- First, the cable industry invested over $100 billion to expand the capacity of our distribution networks and tens of billions more to improve the quality and diversity of our programming offerings.

- Second, DBS and other distribution media have emerged to provide additional outlets for programming.

- Third, cable operators and other distributors enjoy the freedom to package and price this programming as required by the marketplace, not regulation, and to create tiers and packages that respond to consumer demand, make economic sense for our industry, and respond to competition from other providers.[16]

- Fourth, cable's infrastructure investment created a market for residential broadband, which stimulated competitors to invest in DSL, wireless broadband, satellite broadband, and broadband over powerlines -- and companies and individuals have used these new media to make their content available to tens of millions of consumers.

Much of this progress resulted from a conscious congressional decision to get the government out of the marketplace and to promote competition instead of regulation.

For example, before 1996, all of cable operators' programming tiers were subject to rate regulation, which created a disincentive for anyone to invest in new programming networks. After Congress deregulated cable operators' programming tiers (except for the basic tier), investment in cable systems and programming increased drastically and the number of national programming networks exploded. National programming networks totaled 129 in 1995, of which approximately 51% were affiliated with a cable operator; with the investment explosion fueled by the 1996 Act, that number grew to 531 by 2006, of which (according to the FCC) only 21.8% are affiliated with a cable operator.[17] This represents a 300% growth in the number of networks in the last decade, while at the same time vertical integration declined 60%.

In light of this significant competition in the programming supply and distribution segments of the video marketplace, Congress should be working to eliminate unnecessary regulations. Too many remnants of an antiquated statutory regime crafted for the marketplace of 1992 remain in place. In a robustly competitive and rapidly evolving marketplace, such regulations simply do not make sense.

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[16] As I noted in my prior testimony before this Committee, program tiers *lower transaction costs, reduce marketing costs, lower distribution costs, increase the value of advertising*, and *reduce equipment costs*. The benefits of tiering in this fashion are widely understood and appreciated by both network programmers and would-be programmers. That is why so many of them have so vigorously opposed calls to require distributors to sell programming a la carte.

[17] *Compare In re Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, Third Annual Report, 12 FCC Rcd. 4358 ¶ 142 (1996), *with 12th Annual Report* ¶ 157 & n.568. As noted above, the FCC's calculation overstates vertical integration greatly by counting one network multiple times. *See supra* note 12.

II. VERTICAL INTEGRATION, EXCLUSIVE ARRANGEMENTS, AND ANTITRUST.

One of the characteristics of the antitrust laws is that, with few exceptions, they are laws of general applicability and apply across the economy. Although the competitive characteristics of industries may vary a great deal from one sector to the next, the essential laws and analytical tools remain the same. And thus the core precepts of the Sherman Act and the Clayton Act remain equally applicable whether the industry is barbed wire or fiber optics, chalkboards or laser printers, baby buggies or supersonic transports. Between them, the Antitrust Division of the U.S. Department of Justice and the Federal Trade Commission apply these laws to industries as diverse as trash hauling, semiconductor fabrication, and credit card services.

Yet, in parts of the communications industry, there are provisions of the Communications Act that address vertical integration and exclusive arrangements in ways that constrain business dealings well beyond what the antitrust laws require. This is an anachronism that is no longer necessary.

A. What Does Antitrust Law Tell Us About Vertical Integration and Exclusive Agreements?

One of the issues I think it is important to address today is vertical integration in the video marketplace. Another, sometimes related and often controversial, issue is the use of exclusive arrangements between programming networks and MVPDs. Although vertical integration and exclusive arrangements can go hand-in-hand, the latter being facilitated by the former, neither is a prerequisite for the other and each can exist on its own. More importantly, for the purposes of this hearing, both vertical integration and exclusive arrangements are useful economic tools that can benefit competition and consumers.

At the outset, two key points are worth emphasizing: (1) vertical integration and exclusive arrangements are common throughout the economy and generally benefit consumers and competition; and (2) vertical integration and exclusive arrangements raise competition or policy concerns *only* in the very rare circumstances when they have the effect of seriously impairing a rival's ability to compete, which may thereby reduce consumer choice.

1. Vertical Integration and Exclusive Arrangements Generally Promote Competition and Consumer Welfare.

Vertical integration is something that the antitrust laws know and understand. Vertical integration is not something to be feared; in fact, it often promotes competition and consumer welfare. Where it creates a problem, antitrust creates a remedy.

The classic definition of vertical integration is straightforward: "Vertical integration occurs when a firm provides for itself some input that it might otherwise have purchased on the market. As a result, the input is said to be produced within the firm rather than

purchased from another firm."[18] Vertical integration is common and ubiquitous. It occurs in every industry and region and is "practically infinite in its variety."[19]

As a general matter, vertical integration is widely understood to be procompetitive or competitively neutral, and courts and expert analysts agree that there should be no presumption against vertical integration.[20] There is a long-standing and bipartisan consensus among antitrust enforcers and practitioners that vertical integration is usually beneficial.[21]

Firms typically integrate vertically because they find it cheaper and more efficient to produce an input rather than to purchase it from the marketplace. As a general matter, this type of cost savings is beneficial to the economy and should be encouraged.[22] Vertical integration can also lower costs to consumers by eliminating "double mark ups" -- the ability of an upstream firm to charge a downstream firm a mark-up for an input, which is then passed on to consumers. Economists refer to this as the elimination of "double marginalization."[23]

Vertical integration may also bring together complementary resources or expertise, thereby facilitating investment, innovation, and product development. This helps explain why cable companies have played a leading (but far from unique) role over the years in developing and launching new programming networks.

Similar competitive benefits are associated with exclusive contracts. Allowing the producer of a product or service to limit the channels through which it will be distributed

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[18] 3A Areeda & Hovenkamp, *Antitrust Law* ¶ 755a (2005).

[19] *Id.* For example, a car manufacturer produces its own glass in its own plant rather than purchasing glass from a separate manufacturer; a newspaper company uses employees rather than contractors to distribute its newspapers to newsstands; a university operates its own electrical generation facility rather than purchasing electricity from a local utility; a clothing store manufactures its own branded line of clothes rather than reselling other brands.

[20] *See Nat'l Fuel Gas Supply Corp. v. FERC*, 2006 U.S. App. LEXIS 28504 (D.C. Cir. Nov. 17, 2006) ("We began by emphasizing that vertical integration creates efficiencies for consumers."); DOJ, *Merger Guidelines*, 49 Fed. Reg. 26,823, § 4.23 (noting efficiencies associated with vertical integration) (1984); Areeda & Hovenkamp, *supra* note 18, ¶ 755a ("In the majority of cases no anticompetitive consequences can be attached to [vertical integration], and injury to competition should never be inferred from the mere fact of vertical integration. Every firm -- from the largest monopolist to the tiniest competitor -- is vertically integrated to one degree or another.").

[21] *See* Christine A. Varney, Commissioner, Federal Trade Commission, *Vertical Merger Enforcement Challenges at the FTC* (July 17, 1995) ("Vertical integration can lower transaction costs, lead to synergistic improvements in design, production and distribution of the final output product and thus enhance competition. Consequently, most vertical arrangements raise few competitive concerns."), *available at* http://www.ftc.gov/speeches/varney/varta.htm.

[22] *See* Areeda & Hovenkamp, *supra* note 18, ¶ 757c ("The extensive literature on vertical integration suggests that the majority of instances of vertical integration produce resource savings.").

[23] *Id.* ¶ 758a2 ("*Consumers are better off for each instance of double marginalization eliminated.* By precisely the same token, the market price comes down each time a firm with market power is eliminated from the production and distribution chain.").

or allowing a distributor to distribute or refuse to distribute a given product or service can foster investment and innovation and increased competition based on product differentiation -- so-called "interbrand" competition.[24] Exclusive arrangements often promote non-price competition and improved quality, as well as eliminate free-riding of one distributor on the marketing efforts of another distributor. A distributor with an exclusive arrangement has more incentive to market the supplier's product for which it has exclusive distribution rights.

We see this when Yahoo! cuts exclusive deals with newspapers so that it can better compete against Google.[25] We see this when XM Radio builds exclusive shows around Bob Dylan, Oprah, and Major League Baseball, and Sirius counters with Howard Stern, Martha Stewart, and the National Football League.[26] We see this when Verizon Wireless announces new Hispanic services for its V-CAST music service, and Cingular responds by saying it has already been providing Spanish-language video services but will announce new services soon.[27] We see this when Microsoft announces a new music player that offers features that are not available on the iPod, while neither device can play music purchased from the other's affiliated music store.[28] None of these examples is an antitrust violation; in fact, all are pro-competitive.

The evidence that vertical integration between video programming producers and distributors has benefited consumers is prevalent throughout the video marketplace. In the cable industry, vertical integration stimulated the flow of capital into the programming marketplace, which resulted in an explosion of programming networks. Absent cable operators' investments in programming networks, consumers would never have been able to watch HBO, Discovery, TV One, C-SPAN, TNT, or CNN. In Comcast's case, we have been an industry leader in developing high quality regional sports networks, and in the past few years our investments and expertise have helped launch Comcast SportsNet West, Comcast SportsNet Chicago, and SportsNet New York. In addition, Comcast has invested in creating innovative networks that are tailored to

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[24] *See generally Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 54-55 (1977) ("Vertical restrictions promote interbrand competition by allowing the manufacturer to achieve certain efficiencies in the distribution of his products. These 'redeeming virtues' are implicit in every decision sustaining vertical restrictions under the rule of reason. Economists have identified a number of ways in which manufacturers can use such restrictions to compete more effectively against other manufacturers.").

[25] Press Release, Yahoo! Inc., *Yahoo! Forms Strategic Partnership with Consortium of More Than 150 Newspapers Across the U.S.* (Nov. 20, 2006), *available at* http://yhoo.client.shareholder.com/press/ReleaseDetail.cfm?ReleaseID=219204.

[26] *See* Corey Deitz, *Radio: A Step by Step Comparison of XM and SIRIUS Satellite Radio Features*, About.com, *at* http://radio.about.com/od/satelliteradio/ss/blsatstepbystep.htm (last visited Nov. 30, 2006).

[27] *See* Ian Martinez, *New Mobile Services Reflect Major Hispanic Market Power*, Communications Daily, Nov. 16, 2006, at 5 (describing Verizon Wireless's new services for Hispanics and stating that "Cingular, which has major announcements 'in the pipeline,' according to a spokeswoman, has engaged in a nationwide 'bilingual concept' conversion of over 500 stores in heavily Hispanic areas").

[28] *See* Ethan Smith, *Can Anybody Catch iTunes?*, Wall St. J., Nov. 27, 2006, at R1 ("Microsoft is currently mounting the most ambitious assault on iTunes with Zune -- a software and hardware 'ecosystem' that tries to mimic the successful synergy between iTunes software and iPod gadgets.").

niche audiences, for example, PBS KIDS Sprout, G4, TV One, and AZN. Without these investments, it is likely that many programming networks would never have progressed beyond the idea phase.

2. Vertical Integration and Exclusive Arrangements Implicate Antitrust Laws Only When a Competitor with Market Power Engages in Unfair Competition.

Of course, in some cases vertical integration and exclusive arrangements can cause competitive harm. For example, in some instances, vertical integration or exclusive arrangements can create entry barriers and can foreclose access to important upstream inputs or downstream markets.[29] Such anticompetitive effects are unlikely, however, if a firm (even a monopolist) vertically integrates into a competitive market.[30] Even if the subject market is not competitive, there is no basis for a flat presumption against vertical integration.[31]

For these reasons, antitrust enforcement agencies and the federal courts analyze the costs and benefits of vertical integration on a *case-by-case basis*, based upon the particular real-world facts and circumstances of the affected markets.[32] This is the correct approach. It ensures that the economy is able to benefit from the many instances of procompetitive vertical integration, while ensuring that potentially harmful instances of vertical integration are identified and remedied.[33] Only in limited cases where vertical integration and exclusive arrangements are accompanied by anticompetitive conduct exerted by a competitor with market power does such conduct implicate the antitrust laws.[34]

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[29] *See, e.g.*, *Jefferson Parish Hosp. Dist. No. 2 v. Hyde*, 466 U.S. 2, 45 (1984) (O'Connor, J., concurring) ("Exclusive-dealing arrangements may, in some circumstances, create or extend market power of a supplier or the purchaser party to the exclusive-dealing arrangement, and may thus restrain horizontal competition. Exclusive dealing can have adverse economic consequences by allowing one supplier of goods or services unreasonably to deprive other suppliers of a market for their goods, or by allowing one buyer of goods unreasonably to deprive other buyers of a needed source of supply.").

[30] *See* Areeda & Hovenkamp, *supra* note 18 ¶ 755c.

[31] *See id.*

[32] *See Jefferson Parish*, 466 U.S. at 45 ("In determining whether an exclusive-dealing contract is unreasonable, the proper focus is on the structure of the market for the products or services in question -- the number of sellers and buyers in the market, the volume of their business, and the ease with which buyers and sellers can redirect their purchases or sales to others.").

[33] *See* Vareny, *supra* note 21 ("As a part of the FTC's case-by-case analysis, antitrust enforcers must take great care when considering the nature and extent of the remedy in vertical merger cases. Since many vertical mergers result in procompetitive efficiencies, we must craft relief narrowly to permit procompetitive efficiencies to come to fruition whenever possible.").

[34] *See Verizon v. Trinko*, 540 U.S. 398, 407 (2004) ("The mere possession of monopoly power, and the concomitant charging of monopoly prices, is not only not unlawful; it is an important element of the free-market system. The opportunity to charge monopoly prices -- at least for a short period -- is what attracts 'business acumen' in the first place; it induces risk taking that produces innovation and economic

"Absolute" or "per se" prohibitions on vertical integration and exclusive arrangements are undesirable. As noted, there are numerous benefits to vertical integration -- even by monopolists -- and the competitive harms associated with vertical integration are rare. The antitrust laws have addressed such harms for over a hundred years, and have proven well-suited to enforcing the pro-consumer and pro-competition goals of Congress. In virtually every industry, arrangements perceived by someone as anticompetitive can be subjected to antitrust scrutiny, and absent some showing of market power and likely consumer injury, antitrust will shrug the complaint off and leave the marketplace to work its magic. Thus, Congress should be skeptical of efforts to supplement or supplant antitrust enforcement with inflexible and absolutist approaches. The danger of such approaches is that they will undermine economic efficiencies and increase prices to consumers.

This is probably the case with the cable industry. With content of all kinds being increasingly consumed by consumers whenever and however they want it, the time is long since past when one subset of players in the multiplatform content distribution business is subject to uniquely restrictive rules. The antitrust laws provide adequate protection against anticompetitive conduct, but without skewing incentives, stifling investment, or unfairly burdening one competitor as against another.

B. Antitrust Laws Are Better Suited To Protect Consumers and Competition Than Is Cable-Specific Video Regulation.

Independent of the antitrust laws, Congress has enacted legislation applicable to particular industry sectors. But sometimes this sector-specific legislation addresses what are perceived to be deficiencies in competition, and this can lead to duplication, inefficiency, and even conflicts with antitrust laws.

As you know, in 1992, Congress felt it necessary to address a variety of perceived competitive deficiencies in the video marketplace as it then existed by enacting a uniquely detailed and regulatory regime to govern cable operators.[35] Rules were established to require cable operators to carry broadcast channels;[36] to allow local franchising authorities to require the carriage of public, educational, and governmental channels;[37] to allow the FCC to establish requirements for commercial leasing of channels;[38] to allow the FCC to review certain commercial carriage decisions of cable operators;[39] to prescribe rules governing the sale of certain cable-affiliated programming networks to competing MVPDs;[40] and -- of particular relevance here -- to prohibit (for

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growth. To safeguard the incentive to innovate, the possession of monopoly power will not be found unlawful unless it is accompanied by an element of anticompetitive *conduct*.").

[35] *See generally 1992 Cable Act*, Pub. L. No. 102-385, 106 Stat. 1460.

[36] 47 U.S.C. §§ 534-535.

[37] *See id.* § 531.

[38] *See id.* § 532.

[39] *See id.* § 536.

[40] *See id.* § 548(c)(2)(A)-(C).

ten years) any exclusive arrangements between cable operators and their affiliated programming networks.[41]

Whatever the merits behind the enactment of all these sector-specific statutory provisions at that point in time, it is clear that -- today -- they have long since outlived their usefulness. Of the 531 national programming networks identified in the FCC's latest report,[42] Comcast has a financial interest in only ten.[43] And of the 100 or so regional networks, Comcast has a financial interest in only twelve.[44] Focusing more specifically on sports programming, Comcast has a financial interest in only three national programming networks and eight regional programming networks that could be considered sports networks.[45] And in every case except one, which I will discuss below, Comcast has made its programming available to every other competitor. Comcast has not used its affiliation with sports programming networks in any manner that could be viewed as anticompetitive. Quite the opposite is true, and our investments have produced better programming for consumers and fostered fierce competition with other MVPDs.

As I explained above, the intense competition that now pervades every aspect of the video marketplace makes these cable-specific market-conduct rules an anachronism. These rules address problems that no longer exist. And, to the extent that there remain any bases for concern about anticompetitive conduct, the current cable-specific rules represent artificial and clumsy solutions to problems that can better be addressed through the mechanism of antitrust.

Remember, cable operators and other communications companies are fully subject to the antitrust laws,[46] and the antitrust laws already address vertical relationships. They already provide the tools to evaluate whether a contract that enables a single MVPD to

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[41] *See id.* §§ 548(c)(2)(D), 548(c)(5). The FCC later interpreted this provision to prohibit any exclusive arrangement between a cable operator and any programming network affiliated with that cable operator or any other cable operator. *See* 47 C.F.R. § 76.1002(c) (2005).

[42] *See supra* note 12 and accompanying text (noting that the FCC's 531 networks counts iN DEMAND as 60 different networks).

[43] The national programming networks are: E!, G4, AZN, VERSUS, style, Golf Channel, iN DEMAND, TV One, PBS KIDS Sprout, and The mtn.

[44] Comcast's regional programming networks are: CN8, Cable Sports Southeast, Comcast SportsNet Philadelphia, Comcast SportsNet Mid-Atlantic, Comcast SportsNet Chicago, Comcast SportsNet West, SportsNet New York, Fox Sports New England, New England Cable News, and Pittsburgh Cable News Channel, Comcast Local (Detroit), and Comcast Entertainment TV (Denver).

[45] These networks are: VERSUS, Golf Channel, The mtn., Cable Sports Southeast, Comcast SportsNet Philadelphia, Comcast SportsNet Mid-Atlantic, Comcast SportsNet Chicago, Comcast SportsNet West, SportsNet New York, Fox Sports New England, and Comcast Local (Detroit).

[46] *See 1992 Cable Act* § 27 (codified at 47 U.S.C. § 521 note) ("Nothing in this Act or the amendments made by this Act shall be construed to alter or restrict in any manner the applicability of any Federal or State antitrust law."); *United States v. AT&T*, 552 F. Supp. 131, 157 (D.D.C. 1982) (explaining that the court repeatedly rejected the pre-divestiture Bell System's claim that it was immune from the antitrust laws because those laws had been preempted by "pervasive regulation" under the Communications Act); *United States v. AT&T*, 524 F. Supp. 1336, 1345 (D.D.C. 1981); *United States v. AT&T*, 461 F. Supp. 1314, 1320-30 (D.D.C. 1978).

carry a given network is procompetitive or anticompetitive. They already provide a mechanism for judging the reasonableness of a given distributor's decision not to carry a particular network. The real question is whether those types of arrangements need to be subject to two different sets of federal laws. I submit that the answer is an emphatic *no*.

In my judgment, the antitrust laws are superior to sector-specific regulation in a number of respects. One important difference is that antitrust is driven by *facts and analytical rigor*, not by speculation. Antitrust is informed by evolution in the science of economics, not preconceived theories that have long since been disproved by real-world experience in the marketplace. Antitrust generally leaves market participants free to create, innovate, and alter business arrangements without pre-ordained and highly artificial boundaries, and it intrudes only to the extent needed to remedy market failures.

In contrast, laws and regulations applied specifically to cable companies under the Communications Act impose arbitrary restrictions on certain competitors' abilities to innovate and structure their businesses in the ways that make the most economic sense. In fact, those laws and regulations discriminate between competitors and create an uneven playing field. While cable operators are subject to an expansive regulatory regime that includes regulation of their vertically integrated programming networks and prohibitions on entering into exclusive contracts, no such regulation and restrictions are imposed on cable operators' competitors. How can News Corp.'s vertical integration and exclusive arrangements be beneficial for consumers but Comcast's and Time Warner's not be? As I explain below, it is past time for Congress and the FCC to transition communications regulation from sector-specific regulation to the antitrust laws.

III. VERTICAL INTEGRATION, EXCLUSIVE ARRANGEMENTS, AND THE COMMUNICATIONS LAWS.

Policymakers have generally understood that market forces are superior to government regulation in enhancing consumer welfare; that is no less true in the area of video content. But, despite dramatically increased competition, cable operators remain subject to unnecessary regulations that address concerns which, in this day and age, are fully addressed by antitrust laws.

Back in 1992, when DBS had yet to launch its first satellite or sign up its first customer, the cable industry faced little direct multichannel competition. In response to consumer complaints, and in the absence of meaningful alternative sources of programming, Congress passed strict regulations governing the cable industry. Even then, Congress expressed a strong preference for competition over regulation, and its intention to reduce regulation as competition took hold.[47] Congress even went so far as to acknowledge that, at some point in the future, it expected competition to displace regulation.[48]

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[47] *See* 47 U.S.C. § 521(6).

[48] *See, e.g.*, 47 U.S.C. §§ 543(a)(2), 548(c)(5).

In the years since, video competition has taken deep root. Many of the regulations that currently govern the cable industry were intended to address less competitive market conditions that have long since changed. The regulations, however, have not.

Two of those regulations that are relevant to this hearing are the so-called "program access" provisions of the 1992 Cable Act,[49] and the "program carriage" provisions of that Act.[50]

A. Program Access Regulation Is a Remnant of a Bygone Marketplace.

Congress adopted the program access provisions to ensure that national satellite-delivered cable programming services in which cable operators had an attributable financial interest would be made available to the industry's competitors on rates, terms, and conditions comparable to those available to cable companies. Moreover, the program access provisions, implemented into rules by the FCC,[51] prohibited exclusive arrangements between cable operators and cable-affiliated programming networks in order to ensure that fledgling satellite providers and other competitors would have access to programming perceived as critical to their success.

These provisions represented a major departure from normal competition policy, which would encourage investment and innovation in exclusive programming.[52] In appropriate situations, exclusive programming arrangements may permit competitors to distinguish themselves from one another and thereby *intensify* competition and benefit consumers.

In adopting program access requirements, Congress clearly did not intend to commoditize all video programming. The statute does not apply to any programming in which a cable operator does not have an attributable financial interest, nor does it apply to terrestrially distributed cable networks (of which there were more than a dozen in operation when the 1992 Cable Act was passed). Nor does the statute require that all programming be sold to everyone or sold at the same price to all distributors. Thus, in adopting this striking exception to freedom of commerce, Congress specifically limited its marketplace intrusion.

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[49] *1992 Cable Act* § 12 (codified at 47 U.S.C. § 548).

[50] *Id.* § 19 (codified at 47 U.S.C. § 536).

[51] *See In re Implementation of Sections 12 and 19 of the Cable Television Consumer Protection and Competition Act of 1992: Development of Competition and Diversity in Video Programming Distribution and Carriage*, First Report & Order, 8 FCC Rcd. 3359 (1993).

[52] Congress even recognized the importance of exclusive arrangements in promoting investment by permitting cable operators to petition the FCC for a waiver from the exclusivity prohibition. *See* 47 U.S.C. § 548(c)(4). However, the regulatory process for and delays associated with obtaining such waivers has made this a burdensome means by which to obtain exclusivity.

Congress also intended that the exclusivity prohibition be temporary. It was scheduled to sunset in ten years.[53] Unfortunately, the FCC saw fit to exercise its authority to extend it for another five years,[54] and the matter will be debated anew in 2007.

Although it could be said that (given the successful growth of DBS, in particular) the program access rules are working, it would probably be more accurate to say that *the marketplace* is working. In the 14 years since Congress enacted these provisions, there have been far fewer program access complaints filed with the FCC than either the FCC or Congress envisioned (approximately 45 in total), and only six of these complaints have resulted in rulings adverse to the programmer -- in fact, most have been settled. Importantly, as competition has grown, the number of program access complaints has dwindled, not increased. What is clear in today's marketplace is that national programming networks, whether or not affiliated with a cable operator, desire broad distribution of their services and have every incentive to ensure that as many consumers as possible can see their programming, including the 28.5 million DBS subscribers, the customers of other MVPD competitors, the millions of broadband Internet enthusiasts, and the growing hordes of mobile phone and portable media device users.

Perhaps the best known complaint pertaining to program access concerns Comcast SportsNet Philadelphia. The FCC (twice) and the courts (once) have thoroughly considered and rejected complaints by DIRECTV and EchoStar that Comcast's creation and distribution of this high-quality regional sports network violated the program access rules. All have concluded that Comcast was within its rights to make the economically sound decision to distribute this network terrestrially using a pre-existing distribution system and to license it to some, but not all, of Comcast's direct competitors.[55]

DIRECTV and EchoStar both claim that Philadelphia professional sports programming is "must-have" programming and that they cannot compete in that region without it. The facts, however, do not support that claim.

Since the mid-Nineties, nearly a hundred local Philadelphia professional sports events have been available on local broadcast stations, but when the DBS companies were authorized to carry these signals (which were available to them free of charge), they did not do so until they were required to by federal law. It is difficult to understand why, if the games of Philadelphia sports teams are "must-have" programming, they would not

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[53] *See* 47 U.S.C. § 548(c)(5).

[54] *See In re Implementation of the Cable Television Consumer Protection & Competition Act of 1992, Development of Competition and Diversity in Video Programming Distribution: Section 628(c)(5) of the Communications Act Sunset of Exclusive Contract Prohibition*, Report & Order, 17 FCC Rcd. 12124 (2002).

[55] Both Verizon and RCN have carriage agreements for Comcast SportsNet Philadelphia. While the DBS companies and others have cried wolf for nearly a decade, claiming that the FCC's decision would encourage companies to move their most valuable programming off of satellite (and therefore beyond the reach of the program access rules), the fact of the matter is that that has not happened. In fact, Comcast's other regional sports networks -- including those launched since Comcast created the Philadelphia network -- are all satellite-delivered, again for sound economic reasons, and all are made available to competing MVPDs.

bother to carry them for free. Moreover, based on data from Media Business Corp. (as of September 30, 2005), it is clear that DBS penetration in Philadelphia is higher than or comparable to that in many other urban markets.[56] And between 2000 and 2005, the DBS companies *tripled* their market share in Philadelphia.[57] Clearly consumers are considering a wide variety of factors -- prices, programming choices, technology options, customer service, etc. -- when choosing among MVPDs, and not just the presence or absence of one particular network.

As I noted earlier, most programmers -- including cable companies that own programming -- want maximum distribution for most of their products. But that should not mean that cable companies, DBS companies, and others should not have the freedom to create and invest in some original and exclusive programming as well, in order to distinguish themselves from one another in the marketplace. Thanks in part to Comcast's freedom to use Comcast SportsNet Philadelphia as a point of competitive differentiation against its satellite competitors, Comcast has invested over $456 million in making this an exceptionally high-quality network. As a result, the network has been nominated for over 150 Emmys and has won 56 times; provides over five hours of live sports news programming seven days a week; broadcasts over 300 games per year including 72 Sixers games and 61 Flyers games this season; and produces all home games in HD in its own HD Studio, live postgame shows after every Flyers, Sixers, and Phillies game on Comcast SportsNet Philadelphia and after every Eagles game, and over 40 prime time specials involving all of our teams in the city from college to high school.

Given these facts, Congress and the FCC should consider that the program access rules (and the corresponding restrictions that now apply to DIRECTV as a consequence of its merger with News Corp.) may now be having the perverse effect of *reducing investment* in original programming. After all, why should competitors invest and create if they are guaranteed access to someone else's work on the cheap? Reliance on antitrust laws to police any potential harms caused by exclusive arrangements would reverse this course.

B. Program Carriage Decisions Should Be Left to the Marketplace.

The program carriage provisions of the 1992 Cable Act were intended to ensure that, 14 years ago when cable companies were perceived to be the sole providers of multichannel services, those companies could not play a "gatekeeper" role through actions that unfairly barred or handicapped independent programming networks from gaining distribution. These rules have almost never been invoked, again largely because the marketplace works. Anyone who has an attractive programming idea, a sensible business plan, and a willingness to negotiate carriage terms that make sense for both the programmer and the distributor, has had the opportunity to build a business.

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[56] As of September 30, 2005, DBS penetration in Philadelphia was 12.04%, which was higher than Hartford, Springfield-Holyoke, Laredo, Providence, or San Diego; and was comparable to Boston, Las Vegas, El Paso, and Palm Springs. Other major cities such as New York, Tampa, Baltimore, and Milwaukee were only slightly higher.

[57] DBS penetration in Philadelphia rose from 4% in September 2000 to 12.04% in September 2005.

But, what if a company feels that it has unreasonably been refused carriage? Should such a matter be addressed by the FCC, under its program carriage rules, or are such matters better left to antitrust enforcement? Just as with "program access," I believe antitrust is the better way to go.

This was borne out by our recent experience with the Mid-Atlantic Sports Network ("MASN"). We believe that the network came into being as a result of a breach of the contractual rights of Comcast SportsNet Mid-Atlantic, and Comcast declined to carry it. While this dispute was pending in the Maryland courts, and while the FCC was considering Comcast's and Time Warner's requests for approval of their acquisition of the Adelphia cable systems out of bankruptcy, MASN used print and online ads to generate political pressure on the FCC. The agency, in turn, decided to impose a condition on Comcast under which owners of regional sports channels, uniquely among all programming categories, may now demand that cable companies submit to binding arbitration if the channel owner and the cable operator cannot agree on terms and conditions of carriage. They did this even though Comcast already carries a great deal of unaffiliated regional sports networks -- even where we also carry affiliated regional sports networks-- because this is what is required by competitive market forces.[58]

Shortly after this condition was adopted, Comcast and MASN reached a carriage agreement and settled their pending litigation. One immediate (and inevitable) result was that customer prices rose by $2 per month. One should rightfully question whether the FCC truly achieved any consumer benefit by effectively mandating a significant price increase for 1.5 million customers, only a fraction of whom will even watch MASN.

Although it is not the beneficiary of that merger condition, The America Channel ("TAC") is trying to achieve a similar result. Since April 2004, it has filed more than 66 pleadings (over 22 in the past 12 months) seeking FCC pressure to force carriage deals with Comcast and other cable operators. Although TAC has not demonstrated that it has produced a single hour of video programming, TAC claims that: (1) independent programming networks cannot succeed without a carriage agreement from Comcast and Time Warner; and (2) those companies will not work with independent programming networks.

In response to TAC's first claim, I would refer you to the article by C. Michael Cooley of The Sportsman Channel, entitled "How I Started a Network Without Comcast."[59] Moreover, there are many networks that have become viable *before* they obtained cable carriage,[60] reinforcing the point that there are a sufficient number of U.S. MVPD households served by competitors to support such programming.

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[58] This is the situation in Atlanta, Boston, Detroit, Miami/Orlando/Tampa Bay, New York, and San Francisco/Sacramento.

[59] C. Michael Cooley, *How I Started a Network – Without Comcast*, Multichannel News (Oct. 3, 2005). I attached a copy of this article to my testimony before this Committee this past summer.

[60] *See* Comcast Reply Comments, filed in MB Docket No. 05-255, at 34 n.138 (Oct. 11, 2005) (noting that BBC America, CNBC World, Bloomberg Television, ESPNU, Classic Sports/ESPN Classic,

In response to the second claim, marketplace facts refute TAC's assertion. Comcast carries dozens and dozens of independent networks. In fact, we have no choice but to carry a significant number of independent programmers. Not only do our customers demand independent programming, but there aren't anywhere nearly enough affiliated programming networks to fill out our channel lineups.

In fact, 13 out of every 14 channels carried by Comcast are owned by companies that are completely independent. This should not come as a surprise -- it is our goal, and a competitive necessity, to provide the best programming and the best value for our customers, regardless of who owns or produces the programming.

Nonetheless, TAC has threatened to file a program carriage complaint with the FCC, and it has already filed a private antitrust lawsuit. Fortunately, the antitrust forum is one that will ultimately require TAC to prove its case with facts, not unsupported allegations, and to demonstrate both the existence and abuse of market power. This is a far superior process to having the FCC simply make up the rules as it goes along, interfering in the cable business in ways that it never could with those who compete with us using other platforms.

I respectfully submit to you that the cable-specific rules have outlived their usefulness. To the extent that there remains any potential for anticompetitive abuse, antitrust -- with its focus on facts and its analytical rigor -- is the only remedy needed. (And for anyone who is concerned that today's Antitrust Division may not be sufficiently zealous in bringing antitrust cases, I would remind you that dozens of state attorneys general and hundreds of private plaintiffs' attorneys are all capable of pursuing antitrust remedies.)

IV. ANTITRUST AND SPORTS

With all that as background, I also want to make a few additional comments about antitrust and sports. Just as I think the time has come to eliminate sector-specific statutes that overlap and interfere with antitrust laws, so do I think this Committee should consider revoking sports-related exemptions from antitrust laws.

My earlier comment that the antitrust laws apply across the entire economy was something of an oversimplification. As you know, Major League Baseball is exempt from the antitrust laws under an exception created by the Supreme Court.[61] In addition, Congress has enacted legislation that exempts certain narrowly defined conduct by all four of the major professional sports leagues and their respective teams. Specifically, and of particular relevance to this hearing, in 1961, Congress enacted the Sports Broadcasting Act, which permits teams of the four major sports leagues to pool their individual

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GolTV, DIY, Boomerang, The Independent Film Channel, and NFL Network are just some "examples of networks that obtained most of their initial carriage on DBS").

[61] *See Federal Baseball Club v. National League*, 259 U.S. 200 (1922); *see also* 15 U.S.C. § 26b (removing the league's employment negotiations with players from the scope of the antitrust exemption, while clarifying that the exemption continues to apply to other antitrust issues).

television rights to allow the league to sell "all or any part of the rights of such league's member clubs in the sponsored telecasting of the games."[62]

Many in Congress decry increases in the prices for cable and satellite programming. Yet the biggest cost incurred by MVPDs is for access to programming, and as the Government Accountability Office found a few years ago (when it was still called the General Accounting Office), programming costs are rising faster than cable prices.[63] By far the biggest programming cost increases are those for sports programming.[64] Part of the problem may be attributable to the antitrust exemptions that professional sports leagues enjoy.

Consider the NFL and its ability to extract exorbitant rate increases year after year for its content. The NFL is expected to receive more than $3.7 billion per year from CBS, ESPN, Fox, NBC, and DIRECTV through its television rights deals that extend from the 2006 to 2013 seasons.[65] This represents a 53% increase in annual revenue over the deals that expired at the close of the 2005 season.[66] And this was just the tip of the iceberg -- now the NFL Network is reportedly seeking to raise its license fee for large cable operators to between $.70 and $.90 per subscriber from its previous price of between $.20 and $.25 per subscriber.[67] This rate hike would make the NFL Network the third most expensive national ad-supported cable channel after ESPN (at about $3) and TNT (a little less than $1).[68]

In my view, it is certainly valid to ask whether that antitrust immunity played any role in enabling the NFL to pull its games off of broadcast television and then try to force cable

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[62] Pub. L. No. 87-331, 75 Stat. 732 (codified at 15 U.S.C. §§ 1291-1295). As Chairman Specter noted at the last hearing, the exemption for pooling games in order for the league to sell the rights for "sponsored telecasting" has been interpreted by the U.S. Court of Appeals for the Third Circuit to be limited to selling those rights to "broadcasts which are financed by business enterprises . . . in return for advertising time and are therefore provided free to the general public"; in other words, a broadcast network. *Shaw v. Dallas Cowboys Football Club, Ltd.*, 172 F.3d 299, 301 (1999).

[63] U.S. Gen. Accounting Office, *Telecommunications: Issues Related to Competition and Subscriber Rates in the Cable Television Industry* 22 (Oct. 2003) ("*2003 GAO Report*"), *available at* http://www.gao.gov/new.items/d048.pdf.

[64] *See id.* GAO found that between 1999 and 2002, the average license fee for sports networks (ESPN, ESPN Classic, ESPN2, Fox Sports Net, The Golf Channel, The Outdoor Channel, and Speed Channel) increased by 59%. In that same period, by contrast, the average license fees for the 72 non-sports networks analyzed by GAO increased by only 26%. *See id.*

[65] Mike Reynolds, *Football Kicks Off with Shifts in TV Formation*, Multichannel News, Aug. 14, 2006, at 28.

[66] *See id.* The fees currently being paid for rights to televise NFL games each year are approximately equivalent to the *combined* fees paid annually for rights to televise NASCAR races; Major League Baseball, NBA, NHL, and NCAA basketball games; golf; and the Olympics. *See* Ben Grossman & John M. Higgins, *NFL Goes Long: League's New Network Ignites a Turf War with Cable Operators*, Broad. & Cable, Aug. 14, 2006, at 14.

[67] *See* John Ourand, *Comcast To Pay Surcharge, Carry NFL Net Games*, Sports Bus. J., Aug. 28, 2006.; Reynolds, *supra* note 65, at 28.

[68] *See* Ourand, *supra* note 67.

and satellite companies to buy access to those games at vastly increased prices without antitrust immunity. If antitrust immunity is a factor in allowing the professional sports leagues to substantially increase prices that must be passed along to cable and satellite customers, I urge you to consider revoking that immunity. This doesn't mean that the leagues will be adjudged to have violated the antitrust laws, but I don't see why they should be immune from those laws.

I do recognize that sports programming has characteristics that makes it somewhat different from other types of programming. The passion that some fans bring to sports sometimes exceeds that of even the most intensely loyal viewers of primetime network series. And, as noted, sports programming can be exceptionally expensive. But these particular characteristics are not reasons for special treatment under the communications or antitrust laws. To the contrary, the arguments given above for eliminating program access and program carriage laws -- but leaving the antitrust laws fully in force -- would seem to apply fully.

As our Chairman, Brian Roberts, said to an audience here in Washington a couple of months ago, Comcast is open to a serious public dialogue about the issues that are arising due to the proliferation and escalating costs of sports networks, and I applaud this Committee for holding today's hearing and the one held last month. There are legitimate issues about how the growing number of pricey sports channels should be offered and who should bear the cost. But as this dialogue begins I think it is fair to ask that policymakers exercise regulatory restraint. In particular, I would think we should try to avoid anomalies like requiring Time Warner to carry the NFL Network, apparently under the theory that it is essential that Time Warner have access to that network's grand total of eight out-of-market games, while DIRECTV is permitted to have exclusive access to literally scores of the NFL's other out-of-market games.

V. CONCLUSION.

Mr. Chairman and Members of the committee, the video marketplace is the most competitive it has ever been; virtually every consumer in the United States can choose to receive video programming from at least three different multichannel video providers, in addition to broadcast stations, the Internet, and an ever increasing number of sources, including telephone companies.

Enormous successes have resulted from deregulation and competition in the video marketplace, including massive investments, robust competition, and abundant choice. The time has come to take the next step, eliminating sector-specific regulations that saddle cable with a layer of regulation that is in addition to antitrust and, perhaps, eliminating sector-specific immunities from the antitrust laws as well.

We appreciate your attention to these issues -- in the context of video programming in general and sports programming in particular. I hope my testimony has helped to show that today's problem is not that sports programming might be withheld from competitors. Quite the opposite -- today's problem is that sports teams and leagues can force their way onto cable systems and charge whatever they can convince the FCC or an arbitrator is

"fair." This has the effect of driving up what all consumers are paying, even though many have no particular interest in sports, and even the sports fans are being asked *to pay more* to see the *same number* of games. We will welcome the opportunity to work with you in forging effective solutions to this problem.

Thank you for the opportunity to testify today.

Testimony of

Mark Cooper
Director of Research
Consumer Federation of America

on behalf of

Consumer Federation of America
Free Press
Consumers Union

before the

United States Senate
Committee on the Judiciary

December 7, 2006

MR. CHAIRMAN AND MEMBERS OF THE COMMITTEE,

The Consumer Federation of America,* Free Press**, and Consumers Union*** appreciate the opportunity to testify on the issue of competition and convergence in the telecommunications market. My name is Dr. Mark Cooper. I am Director of Research at the Consumer Federation of America.

OVERVIEW

The continuing market failure and imperfections in the Multi-channel Video Distribution Programming (MVPD) market is evident in rising prices for monthly service, anti-consumer and anticompetitive bundling, discrimination in the carriage of programming by cable operators and refusal to offer critical marquee programming to competing delivery platforms.

Entry into the industry remains extremely difficult from both the content and the distribution sides. Satellite has been unable to discipline cable market power and it appears that the entry of telephone companies is equally ineffective. Monthly prices for basic and expanded service have just about doubled since the passage of the Telecommunications Act of 1996.[1] Just last week the two largest theoretical competitors in the Northeast each upped their rates dramatically, by four to five times the rate of inflation.[2]

This market power stems primarily from a lack of competition at the point of sale. The MVPD market exhibits not only the classic barriers to entry such as high capital costs, specialized inputs and economies of scale, but cable operators have also built barriers to entry with their regional concentration, vertical integration and bundling strategies. The topic of this hearing, the withholding of vital, geographically specific marquee programming from alternative distribution platforms is one of the elements in a tightly woven web of business practices that have dampened competition in the sector.

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*The Consumer Federation of America is the nation's largest consumer advocacy group, composed of over 280 state and local affiliates representing consumer, senior, citizen, low-income, labor, farm, public power and cooperative organizations, with more than 50 million individual members.

**Free Press is a national, nonpartisan organization with over 225,000 members working to increase informed public participation in crucial media and communications policy debates.

***Consumers Union is a nonprofit membership organization chartered in 1936 under the laws of the state of New York to provide consumers with information, education and counsel about good, services, health and personal finance, and to initiate and cooperate with individual and group efforts to maintain and enhance the quality of life for consumers. Consumers Union's income is solely derived from the sale of *Consumer Reports*, its other publications and from noncommercial contributions, grants and fees. In addition to reports on Consumers Union's own product testing, *Consumer Reports* with more than 5 million paid circulation, regularly, carries articles on health, product safety, marketplace economics and legislative, judicial and regulatory actions which affect consumer welfare. Consumers Union's publications carry no advertising and receive no commercial support.

Market power at the point of sale to the public and monopsony power at the point of purchase from programmerd combine to undermine competition. Large MSOs have come to dominate specific regions of the country. They move into regionally specific programming, that is itself a monopoly. They embed this programming in huge bundles, forcing all consumers to pay for programming. They then deny access to this programming to competing distributors.

Their monopsony power, grounded in their market power at the point of sale and the huge regional clusters and concentrated national market created over the past decade, gives them the ability to secure control over the regionally specific marquee programming, like sports channels. Since this programming is regional, it is readily distributed through terrestrial means. Subject to the so-called "terrestrial loophole," the programming can be withheld from competing distribution platforms under the Cable Consumer Protection Act of 1992. The net effect is to add another tool to the cable operators' kit of anticompetitive and anti-consumer practices.

The incessant reduction in the number of cable operators and their increasing size has led to the aggregation of cable systems into large, regional clusters of systems. As cable operators gain control of large, contiguous geographic areas, their ability to withhold programming they own from other operators increases. They are also more able to obtain exclusive rights to programming they do not own. Restricting the flow of programming to alternative distribution platforms blunts competition at the point-of-sale increasing the cable operator's market power over consumers and programmers. The result is that consumers have few or no alternatives for obtaining television service, while programmers alternatives for distributing programming to the public are significantly limited.

Another development that has further restricted consumer choice and programmer access is the cable industry practice of bundling. Cable operators force consumers to buy large bundles of programs in order to obtain the small number of networks that they actually watch. And for independent programmers, carriage in the bundles that will be widely distributed nationally or regionally is a make-or-break threshold. Access to these bundles is under the control of the cable operator. This practice, which has been prevalent for basic and expanded basic tiers in the past, has recently been extended to digital tiers. In addition, anecdotal evidence suggests that cable distributors are beginning to eliminate availability of some channels on analog systems, requiring consumers to pay a hefty monthly rental fee for the digital box, just to get the channel they had previously been receiving in the analog bundle.[3] With rental prices exceeding $5/month in many cases, "migration" of analog channels to digital, represents a hidden rate hike on consumers.

By creating the huge bundles, then controlling which programs are placed in the bundles, cable operators perpetuate their control over consumer pocketbooks and the success or failure of programming. The refusal of cable operators to allow consumers to choose which programs they want to pay for on a program-by-program basis makes it impossible for programmers to market directly to the public. They must sell themselves, literally and figuratively, to the handful of gatekeepers that control access to the big bundles. Advertisers, looking for national and regional audiences are unable to target their messages because every subscriber is forced to pay for all the channels, whether they watch them or not, as a result of cable's bundling strategy. Forced bundling places a premium on carriage on cable systems, in the eyes of the advertisers, rather than actual viewing by the public.

PERSISTENT MARKET POWER IN THE MULTICHANNEL VIDEO PROGRAM DISTRIBUTION MARKET

Not only is the industry becoming more concentrated (as measured by the HHI index) but it is also overcharging consumers (as measured by the Lerner index), and capturing massive monopoly profits (as measured by Tobin's q ratios). Each of these measures indicates that the overall competitive situation has become worse since 1992. Unfortunately, when Congress decided to move media and communications policy toward greater reliance on competition in the Telecommunications Act of 1996, the cable operators headed in the opposite direction. Rather than use their expertise, existing plant and ownership of programming to enter neighboring service territories and compete with monopoly incumbents, the dominant cable companies chose to buy each other instead. Not one major incumbent has ever sought to overbuild a neighbor to compete against another incumbent. The monopolies they had gained through franchise awards in the 1970s and defended through anticompetitive behavior in the 1980s were merged into ever-larger MSOs and clusters in the 1990s. The result has been a dramatic increase in concentration and clustering of systems. Thus, we should not be surprised to find that in the late 1990s, the Assistant U.S. Attorney General for Antitrust called the cable industry "the most persistent monopoly in the American economy."[4]

Since that statement was made, mergers have been executed between the first, second, third, fourth and sixth largest companies, creating two giants that tower over the industry. Regional markets have been drawn into huge clusters of systems. Cable's dominance as the multichannel medium is overwhelming, with a subscribership of approximately two-thirds of all TV households. Its penetration is about three times as high as the next multichannel technology—satellite. Because a large number of satellite subscribers live in areas that are not served by cable, competition in geographic markets is less vigorous than the national totals suggest. Cable has about four times the market share of satellite in markets where both are available.

This suggests that cable retains a market share at the point of sale of above 80 percent. The HHI index at the local level is above 6400, at best a duopoly. These market shares and levels of concentration make cable operators virtual monopolies.

CLUSTERING

This market power at the point of sale is reinforced by a strong trend toward regionalization in which one company gains ownership of many firms in a region. Clustering has increased sharply since 1994, when less than one-third of cable subscribers were in clusters.[5] Just over one-half of all cable subscribers were clustered in 1997, but by 2000, three-quarters were. Today, the figure is over 80 percent.[6] The Adelphia-Comcast-Time Warner transaction will push it into the 85-90 percent range.[7]

Econometric analysis by several agencies shows that **bigger monopolies are worse when it comes to consumer prices.** In the GAO analysis, if a cable system is part of a large national operator, its prices are 5.4 percent higher than if it is not.[8] The GAO called this horizontal concentration. Federal Communications Commission (FCC) econometric models

have been finding this to be the case for several years, with even larger effects of being part of a multiple system operator (MSO).[9] When the FCC models add in a specific variable for regional clustering, they find that clustering has an added effect of further raising price.[10] Consumers served by one of the mega-MSOs, which have been expanding their grip on the industry through mergers and clustering, suffer higher prices by more than 5 percent and perhaps as much as 8 percent. Thus, there could be as much as an additional $1.5 billion in consumer savings that could be wrung out of the cable market if it were de-concentrated.

The important implication is that the theory used to allow large cable operators to become larger is not supported by the empirical evidence. That theory claimed that the combination of larger, clustered systems would create efficiency-based cost savings that would be passed on to the public because one big monopolist is no worse that two, contiguous smaller ones. Since large incumbents never overbuild one-another and compete, the claim is that there was little to be lost. The econometric evidence suggests that there is, in fact, considerable harm. It turns out that large operators and clustered systems have more muscle to thwart competition and impose price increases. They can distribute programming terrestrially and extract exclusivity deals from independent programmers, thereby denying programming to competing distribution media (overbuilders and satellite). They have more leverage over local governments to obstruct the entry of overbuilders. But if they knew they could not grow through mergers, they might compete by overbuilding one anothers' networks.[11]

The importance of regional programming is highlighted in FCC's Eleventh Annual Report on the cable industry. Regional sports networks represent about 40% of total regional networks, while regional news networks represent another 40%.[12]

A recent FCC staff white paper on DBS-cable substitution found, "firm-specific attributes and demographic variables that influence consumer choice and switching costs that appear to affect consumers' desire to switch from one service to another." Notably, the control of regional programming decreased consumers' desire to switch from cable to DBS:

> We also find that DBS penetration is lower where cable operators carry regional sports channels.
>
> This is likely due to a combination of factors discussed above. Two of the factors may involve cable operators limiting DBS operator access to regional sports networks. If this is true, cable operators may be able to offset competitive pressures from DBS, and thus may be able to impose larger price increases without losing subscribers to DBS where they are able to transmit vertically-integrated regional sports networks terrestrially, or are able to reach exclusive carriage agreements with non-vertically-integrated regional sports networks.[13]

As shown in the Eleventh Annual Report, cable operators continue to concentrate their systems regionally in "clusters" through the purchase and sales of MSOs or through "swapping." The Report found that clustering subscribers has increased in recent years.[14]

The Eleventh Annual Report also shows that distributors serving small communities and rural areas represent distinct markets that are at a competitive disadvantage in acquiring programming. Operators of small systems report that they have difficulty obtaining programming due to higher costs (programming is not available on terms similar to those received by large MSOs) and because of contractual tying requirements imposed by dominant media programmers.[15] Tying involves programmer requirements that distributors buy all or most of the programmer's channels and offer them all in the expanded basic tier, just to get the channels the distributor's customers want. The practice prevents distributors from meeting customer demands and imposes additional costs on customers.

A second aspect of clustering that plays an important role is the special role of large urban markets in the industry. The reasons offered for the importance of the large designated market areas (DMAs) include the attractiveness to advertisers of a high-income, trend-setting population, as well as the presence of the major media.

> In addition to the number of viewers, advertisers consider the markets to be important (indeed even disproportionately to their subscriber numbers) for a number of reasons including product trend-setting, higher per capita disposable income, and the presence of major press. Networks that do not substantially penetrate the top markets are at a severe disadvantage in the competition for advertising dollars relative to similar networks which do.[16]

While there are many intangible elements to this characteristic of the industry, there is one area in which it should be visible. Advertising revenue should be higher in the more highly valued markets. To assess the importance of this phenomenon, we have calculated the ratio of revenue to population – essentially the market-wide power ratio. The top eleven markets all have a substantial premium of ad revenues above TV households. These markets account for 31 percent of the TV households, but 41 percent TV ad revenue, a premium of over 33 percent. Six of the next 14 markets have a premium, but the overall premium is about the same. That is, the top 25 markets have 49 percent of TV households and 59 percent of the ad revenue.

The dominance of the MSOs in large, urban markets exacerbates their market power over consumers and independent programmers. For example, the importance of large urban markets and the weakness of satellite as a competitor, both at the point of sale and as a means of distribution for independent programming, converge in the case of Comcast. These two factors are extremely important in evaluating the market power of Comcast.

Comcast, the largest cable operator, has clustered its systems in the dominant urban designated market areas. About 60 percent of its subscribers reside in the top 11 DMAs. Eighty percent of its subscribers reside in the top 25 DMAs. Thus, it has a heavy premium in terms of advertising clout. This gives it greater leverage over programmers than its subscriber count would indicate.

Moreover, approximately 85% of the major league franchises for baseball, football and basketball are located in the top 25 DMAs and approximately 90% of those franchises are monopolies – that is, the franchise is the only team in the sport in the DMA. MSO's that

dominate large urban DMA's have greater ability to own and control must-have sports programming.

VERTICAL INTEGRATION AND MUST CARRY RIGHTS

Vertical issues must also be a factor in this hearing. In economics, vertical integration is a potential concern, especially when dominant firms become integrated across markets for critical inputs. The anticompetitive conduct and negative market performance result from weakened markets due to vertical concentration.

Vertical integration can create barriers to entry. By integrating across stages of production, incumbents may force potential competitors to enter at both stages, making competition much less likely.[17] Vertical mergers can also foreclose input or output markets to competitors.[18] Exclusive and preferential deals for the use of facilities and products compound the problem.[19] Cross-subsidization is more readily accomplished.[20] Vertical integration facilitates price squeezes and enhances price discrimination.[21]

Concerns arise that not only will the dominant firm in the industry gain leverage across input and output markets to profitably engage in anti-competitive conduct,[22] but also the dynamic processes in the industry will clearly shift toward cooperation and coordination rather than competition. Mutual forbearance and reciprocity can occur as spheres of influence are recognized and honored between and among the small number of interrelated entities in the industry.[23] The final behavioral effect is to trigger a rush to integrate and concentrate. Being a small independent firm at any stage renders a company extremely vulnerable to a variety of attacks.[24]

The vertical problem is readily identifiable in the market for video programming. A small number of firms that control distribution are integrated into the production of programming. As a smaller number of owners control a larger share of the distribution market, they gain greater bargaining leverage over independent producers. Indeed, a decision by a large MSO to carry or deny carriage to an independent programmer can determine the economic viability of an independent network. Thus, MSOs have the ability to squelch competition in programming simply by denying carriage.

It is also important to recognize that complete foreclosure is not the only concern. The terms and conditions of carriage are at least as important. Vertically integrated firms defend the marquee programming in which they have a direct interest by frustrating entry and extracting rents from others.

> The power to foreclose also implies the ability to force down the license fees that an MSO pays to networks. Some anecdotal evidence suggests the possibility that larger MSOs hold significant monopsony power in the programming market.[25]
>
> Carriage data provide an incomplete picture of vertical integration's effects on premium networks. In particular, even if both affiliated and unaffiliated networks are carried, an integrated system might price them differently to subscribers. Personal selling and other marketing tactics offer other opportunities for system

> operators to favor one available network over another... For the most part, those subscribership results suggest that integrated systems also tend to favor their affiliated premium networks in pricing and promotion behavior.[26]

By forcing consumers to take large bundles and controlling the content of the bundles, cable operators control the flow of content and the access of programmers to the public. By leveraging their control of distribution, they ensure favorable treatment for their own shows.

DISCRIMINATION IN CARRIAGE IS MORE WIDESPREAD AND PERNICIOUS THAN PREVIOUSLY BELIEVED

Vertical integration leads to discrimination in access to carriage. In a rigorous econometric analysis, the GAO found that cable operators were 64 percent more likely to carry their own programming.[27] They were 46 percent more likely to carry cable channels developed or owned by broadcast networks. These are, of course, the two entities that have carriage rights on cable systems. Given how severely tilted access is against independent programmers, it is hard to imagine how they can possibly succeed.

The GAO findings are consistent with the published econometric analysis that was provided in comments filed in FCC's horizontal and vertical ownership cap proceeding. The findings are quite strong on discrimination, providing a detailed understanding of foreclosure motivations and behaviors. Integrated owners of basic programming exclude competitors for their basic package but offer more of their own basic packages and more premium packages.[28] Owners of premium services foreclose competitors and sell more of their own programming, but offer fewer services at higher prices.[29]

The discrimination at the top of the industry, in terms of the most frequently carried networks, starts at the bottom, in terms of carriage for newly launched networks. Not only are affiliated channels nine times as likely to receive carriage as independent programming, they are also more likely to get better carriage on systems owned by the dominant cable operators – Comcast and Time Warner.

Beyond collusion,[30] mutual forbearance and reciprocity can occur, as spheres of influence are recognized and honored between and among the small number of interrelated entities in the industry.[31] The ability of large, dominant firms to look and learn about how others behave and adjust their behavior has been documented across a variety of industries. Even introductory economics texts now contain long discussions of strategic behavior and game theory, and it has become a routine part of applied policy analysis.[32]

This bears directly on the cable industry, since a small number of firms controls access to a large number of TV sets. Indeed, in the cable *a la Carte* proceeding, the fact that programmers only had to market to a handful of cable executives was touted as a huge transaction cost savings. This small number of executives has make or break power over programming, and they have used that power to favor their own programming at the expense of independent production, exactly the situation Congress intended to prevent.

Occasionally, practices within the industry become so bad that collegiality breaks down and even major players became involved in formal protests. Viacom and its affiliates, a group not affiliated significantly with the top two cable operators in the industry, filed an antitrust lawsuit against the largest chain of affiliated competitors in its New York territory.[33] Ultimately, it sold its distribution business to its competitors.

The dispute between Yankee Entertainment Sports (YES) and Cablevision is another example.[34] YES alleges and provides facts to support its claim that Cablevision's refusal to provide nondiscriminatory carriage is part of a scheme to prevent competition in sports programming[35] and preserve Cablevision's local monopoly in distribution.[36] It documents a long history of threats to foreclose markets as a lever against programmers back to the 1980s.[37] The demands of the operator include demands for an equity stake in YES[38] and exclusivity in carriage.[39] Programmers' "bargaining" with a dominant distribution incumbent frequently involves these types of take-it-or-leave-it-threats[40] that offer inferior placement,[41] discriminatory prices,[42] or exclusion from carriage. Programmers have little bargaining power,[43] particularly since denial of access to 40 percent of the market renders new programming unviable.[44]

The market structure that gives distributors leverage is precisely described by the dispute between Cablevision and YES. There is little direct competition in distribution, with Cablevision having a 90 percent market share,[45] which remains insulated behind barriers to entry.[46] Market power has been built and reinforced by acquisition of distribution and programming.[47] Regional market power through clustering plays a critical role[48] particularly for advertising markets.[49] Dominating specific programming categories generates both high profits and provides leverage to undermine competitors.[50] Cable operators have recently added bundling of high speed Internet to their arsenal of anticompetitive practices[51] and reinforced it with anticompetitive contracts.[52] The pattern is being repeated by Cablevision in withholding sports programming in New York[53] and Comcast battling with an independent sports programmer in the Baltimore-Washington area.[54]

Other examples of resistance to entry of programming that might compete with the marquee offerings of the vertically integrated incumbent programming abound, including national[55] and local[56] news programming, home shopping networks,[57] as well as niche programming including educational,[58] arts,[59] and minority[60] programming.

Overbuilders have faced vigorous efforts to prevent competition through exclusion from access to programming and regulatory tactics of incumbent cable operators.[61] Comcast has shifted some sports programming to terrestrial delivery, thereby avoiding the open access requirement of the 1992 statute. As cable operators become larger and more clustered, this strategy will become increasingly attractive to them. Specific areas where such programming has been denied are Phoenix, Kansas, Philadelphia and New York. The denial of access to marquee sports programming can have a devastating effect, with satellite providers in markets where foreclosure has occurred achieving a market penetration only one-quarter of the national average.[62]

Integrated MSOs wield immense power against smaller cable companies, exploiting loopholes in the program access rules.[63] For the smaller entities, the current refusals to deal are

not limited to sports programming. Other services have been denied, such as video-on-demand.[64]

Second, where the large MSOs do not have direct ownership of video services, they have obtained exclusive arrangements, thereby denying competitors and potential competitors access to programming.[65] The exclusionary tactics apply not only to head-to-head cable operators and satellite providers, but also to DSL-based providers seeking to put together a package of voice, video, and data products. Bundling is critical to controlling entry into the emerging digital multimedia market.[66]

Third, because the dominant MSOs are so large, they can influence important programmers not to sell to competitors or potential competitors. Commenters in the horizontal limits proceeding have noted that they are cut off from programming.[67] The list could go on and on.[68]

The problem is not simply one of complete exclusion. Dominant, vertically-integrated MSOs can inflict "discriminatory or excessively burdensome terms and conditions of programming distribution."[69] Recent comments in the program access proceeding point to an even more stark demonstration of the power of cable to engage in content discrimination.[70]

THE ANTI-CONSUMER, ANTI-COMPETITIVE POTENTIAL IN CABLE BUNDLING

The Committee must also not overlook the important role that bundling plays in the web of anticompetitive practices. Over the past two decades, the anticompetitive potential of bundling has been explored and documented in detail. Indeed, almost immediately after the Chicago school of economic analysis tried to conclude that all bundling be deemed, *per se*, benign,[71] the potentially anticompetitive effects of bundling reemerged in the literature. This literature concluded that bundling engenders market efficiency only when the market is characterized by extreme conditions (i.e., permanent monopoly in one product, perfect competition in the other). In the more common situations, firms whose market power is neither total, nor permanent, can use bundling to defend or extend their market power, leading to further inefficiencies in the market. Under a wide range of assumptions, the dynamic[72] ability of bundling to undermine competition has been demonstrated through a number of mechanisms including inducing exit,[73] creating barriers to entry,[74] relaxing price competition,[75] distorting investment,[76] retarding innovation,[77] and extending market power into new markets.[78]

The best that can be said of the current no-alternative bundles imposed on consumers is that, in a static analysis, they may expand total social surplus while reducing consumer surplus.[79] In other words, producer surplus may increase more than consumer surplus declines, increasing total surplus. Even the conclusion to this static analysis is dubious, as it is unclear whether producer surplus has increased more than consumer surplus has fallen.

Under a dynamic analysis, the enrichment of producers is not random. The current system favors a small number of dominant producers and creates barriers to entry for small, independent outlets, resulting in little diversity in ownership. Leveraging their market power through forced bundling, the large operators and dominant programmers not only reduce diversity, but also diminish competition, leading to inefficiencies in the market. Because

bundling reduces competitive pressures, the total surplus is limited. When reality is injected into the theory, the cable industry argument falls apart even faster. There is no reason to believe that prices will skyrocket in an environment where consumers are allowed to choose between bundles and individual programs. In a more competitive, consumer-friendly environment, total surplus might well be higher.

The record is rife with solid evidence from smaller and independent MVPD operators, independent content producers, local cable commissions and independent programmers that discrimination takes place with the largest programmers bundling to force cable operators and consumers to take networks that would not be taken in the absence of leverage.[80]

RECOMMENDATIONS

If the Congress intends to rely on market forces to discipline the market power of cable operators, it will have to break the stranglehold that the handful of vertically integrated, horizontally concentrated firms use to dominate the sector.

Congress should require cable operators to make available to consumers on an unbundled basis all programming that they choose to bundle. This form of "mixed bundling" — where the bundle remains available, but consumers can also pick and choose the channels they want — will allow consumer demand to begin to exercise it influence on programming choices and control skyrocketing prices.

Congress should impose a strict horizontal limit on cable ownership, to diminish cable's monopsony power in the programming market.

Congress should ban the abuse of vertical leverage, both by closing the terrestrial loophole and adopting an effective policy prevent discrimination in carriage.

Congress should prohibit contractual anti-competitive tying arrangements by dominant media programmers that force distributors to carry all of a network's cable channels just to receive the channels their customers want.

ENDNOTES

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[1] "Remarks of FCC Chairman Kevin J. Martin," Georgetwon University McDonough School of Business and Public Policy, November 30, 2006, p. 6.

[2] Craig Moffet and Judah Rifkin, "Comcast: 2007 Expanded Basic Video Price Increases running at 5.4%," BernsteinResearch, November 29, 2006, interprets the price increases for Comcast and Verizon Fios as "a signal that competitive intensity in the pay TV market remains restrained."

[3] See, e.g., Joseph Berger, *Fuming Over the Costs of Classic Movies,* New York Times, November 5, 2006.

[4] U.S. Department of Justice, 1998. The Department of Justice press release refers to the "cable monopoly." In remarks made at the press conference, Assistant Attorney General Joel Klein added the adjective persistent.

[5] Federal Communications Commission, In *the Matter of Implementation of Section 19 of the Cable Television Consumer Protection and Competition Act,* 2002, Table C-1.

[6] Kagan, Paul Associates. *Major Cable TV System Clusters.* Carmel, California: Paul Kagan Associates 1998; Federal Communications Commission, Tenth *Annual Report.*

[7] If Adelphia is assumed not be clustered, the increase would be over 8 percent. If we calculate only the net increase in large clusters it would be 4 percent.

[8] U.S. General Accounting Office (U.S. GAO), *Issues Related to Competition and Subscriber Rates in the Cable Television Industry,* October 2003; *Telecommunications: Issues in Providing Cable and Satellite Television Service*, October 15, 2003, Appendix IV.

[9] FCC, *Report on Cable Prices,* April 4, 2002, Attachment D-1; February 14, 2001, Attachment D-1; June 2000, Attachment D-1; May 7, 1999, C-1.

[10] FCC, *Report on Cable Prices,* February 14, 2001, Attachment D-1; June 2000, Attachment D-1.

[11] Cooper, Mark, *Cable Mergers and Monopolies* (Economic Policy Institute, 2002), Chapter 7.

[12] Federal Communications Commission, In *the Matter of Implementation of Section 19 of the Cable Television Consumer Protection and Competition Act,* 2005, Eleventh Annual Report, ¶¶166-169.

[13] P. 21

[14] Eleventh Annual Report, ¶141-142

[15] Eleventh Annual Report, ¶186

[16] "The America Channel LLC's Petition to Deny," *In the Matter of Application of the Consent to the Assignment and/or Transfer of Control of Licenses Adelphia Communications Corporation (and Subsidiaries, debtors-in-possession), Assigners to Time Warner Cable Inc. (subsidiaries), Assignees; Adelphia Communications Corporation (and Subsidiaries, debtors-in-possession), Assigners to Comcast Corporation (subsidiaries) Assignees and Transferees; Comcast Corporation, Transferor to Time Warner, Inc., Transferee; Time Warner, Inc., Transferors to Comcast Corporation, Transferee,* MB Docket No. 05-192, July 21, 2005 (hereafter TAC Petition), Exhibit 2.

[17] Perry, Martin, K., "Vertical Integration: Determinants and Effects." In Richard Schmalensee and Robert D. Willig, eds., Handbook *of Industrial Organization* (New York: North-Holland., 1989), p. 247. "[V]ertical mergers may enhance barriers to entry into the primary industry if entrants must operate at both stages in order to be competitive with existing firms and if entry at both stages is substantially more difficult than entry at one stage." Scherer and Ross, F. M., and David Ross, *Industrial Market Structure and Economic Performance* (Houghton Mifflin Company: Boston, 1990), pp. 526-527.

[18] ; Shepherd, William G., *The Economics of Industrial Organization* (Prentice Hall, Englewood Cliffs, N.J., 1985), pp. 289-290.

[19] Perry, 1989, p. 247; Shepherd, 1985, p. 294.

[20] Asch, Peter, and Rosalind Senaca, *Government and the Marketplace* (Chicago: Dryden Press. 1895), p. 248; Shepherd, 1985, p. 302.

[21] Scherer, F. M., and David Ross, *Industrial Market Structure and Economic Performance* (Houghton Mifflin Company: Boston, 1990), p. 524.

[22] There is a growing body of theoretical and empirical analysis that has reinvigorated concerns about the anti-competitive impacts of vertical integration, particularly in the cable industry, see Krattenmaker, T.G., and S. C. Salop, 1986 "Anti-competitive Exclusion: Raising Rivals' Costs to Achieve Power Over Prices," *The Yale Law Journal*, Vol. 92; Ordover, Janusz, A. Oliver Sykes, and Robert D. Willig, "Non-price Anti-Competitive Behavior by Dominant Firms Toward the Producers of Complementary Products," In F. M. Fisher, ed, *Antitrust and Regulation* (Cambridge: MIT Press: 1985).

[23] Asch and Senaca, 1985, p. 248.

[24] Scherer and Ross, 1990, pp. 526-527; Shepherd, 1985, p. 290.

[25] Waterman, David, and Andrew A. Weiss, *Vertical Integration in Cable Television*. Washington, D.C.: AEI Press. 1997, p. 66.

[26] Waterman and Weiss, 1997, pp. 93...94.

[27] U.S. GAO, 2003, p. 30.

[28] Chipty, Tanseen, "Vertical Integration, Market Foreclosure, and Consumer Welfare in the Cable Television Industry." *American Economic Review*. Vol. 91, 2002, p. 429.

[29] Chipty, 2000, p. 429.

[30] Perry, 1989, p. 247.

[31] Asch, Peter and Rosalind Senaca, *Government and the Marketplace* (Dryden Press, Chicago: 1985), p. 248.

[32] See, for example, Taylor, John B, *Economics* (Boston, Houghton Miflin, 2001) Chapter 11; Hasting, Justine, "Factors that Affect Prices of Refined Petroleum Products" (Washington, D.C. Federal Trade Commission Public Conference, August 2, 2001); Cooper, Mark, "Recognizing Limits of Markets, Rediscovering Public Interest in Utilities," *Natural Gas And Electric Power Industry Analysis*, Robert E. Willett, Ed. (Financial Communications Company, Houston 2003).

[33] Viacom International V. Telecommunication Inc., et. al. United States District Court of Southern New York, September 23, 1993.

[34] Yankee Entertainment Sports, *Complaint*, May 5, 2002.

[35] Yankee Entertainment Sports, 2002, para.1, 12.

[36] Yankee Entertainment Sports, 2002, para., 2, 13.

[37] Yankee Entertainment Sports, 2002, para. 16, 29.

[38] Yankee Entertainment Sports, 2002, para. 16, 114.

[39] Yankee Entertainment Sports, 2002, para. 66.

[40] Yankee Entertainment Sports, 2002, para. 70.

[41] Yankee Entertainment Sports, 2002, paras. 53, 67.

[42] Yankee Entertainment Sports, 2002, para. 69.

[43] Yankee Entertainment Sports, 2002, para. 89.

[44] Yankee Entertainment Sports, 2002, para. 107.

[45] Yankee Entertainment Sports, 2002, para. 64.

[46] Yankee Entertainment Sports, 2002, para. 36-40.

[47] Yankee Entertainment Sports, 2002, para. 39.

[48] Yankee Entertainment Sports, 2002, para. 17, 28-29.

[49] Yankee Entertainment Sports, 2002, para. 34-35, 54.

[50] Yankee Entertainment Sports, 2002, para. 30-31.

[51] Yankee Entertainment Sports, 2002, paras. 14, 41.

[52] Yankee Entertainment Sports, 2002, para. 41.

[53] "Petition of TCR Sports Broadcasting Holdings, LLP, to Impose Conditions or, it he Alternative to Deny Parts of the Proposed Transaction," *In the Matter of Application of the Consent to the Assignment and/or Transfer of Control of Licenses Adelphia Communications Corporation (and Subsidiaries, debtors-in-possession), Assigners to Time Warner Cable Inc. (subsidiaries), Assignees; Adelphia Communications Corporation (and Subsidiaries, debtors-in-possession), Assigners to Comcast Corporation (subsidiaries) Assignees and Transferees; Comcast Corporation, Transferor to Time Warner, Inc., Transferee; Time Warner, Inc., Transferors to Comcast Corporation, Transferee*, MB Docket No. 05-192, July 21, 2005, p. 16

[54] Declaration of J. Gregory Sidak and Hal J. Singer, in support of "Petition of TCR Sports Broadcasting Holdings, LLP, to Impose Conditions or, it he Alternative to Deny Parts of the Proposed Transaction," *In the Matter of Application of the Consent to the Assignment and/or Transfer of Control of Licenses Adelphia Communications Corporation (and Subsidiaries, debtors-in-possession), Assigners to Time Warner Cable Inc. (subsidiaries), Assignees; Adelphia Communications Corporation (and Subsidiaries, debtors-in-possession), Assigners to Comcast Corporation (subsidiaries) Assignees and Transferees; Comcast Corporation, Transferor to Time Warner, Inc., Transferee; Time Warner, Inc., Transferors to Comcast Corporation, Transferee*, MB Docket No. 05-192, July 21, 2005

[55] Waterman and Weiss, 1997, p. 56. Keating, Stephen, *Cut Throat: High Stakes and Killer Moves on the Electronic Frontier* (Boulder: Johnson Books, 1999), pp. 17-18, characterizes the incident as described in this paragraph. Recent comments in the program access proceeding summarize these events aptly: "It is also well known that Fox News Channel ("FNC") owes its very existence to Telecommunications, Inc. ("TCI," since acquired by AT&T), whose agreement to carry FNC on systems serving 90% of TCI's subscribers was critical to the successful launch of the network. Not coincidentally, Fox made FNC available to incumbent cable operators on an exclusive basis. Like the saga of News Corp./EchoStar, FNC's launch and subsequent exclusivity to the cable MSOs is a case study of how the largest incumbent cable operators control the destiny of new programming services, and why programmers sell to cable's competitors at their own risk."

Joint Comments, In *The Matter of Implementation of the Cable Television Consumer Protection and Competition Act of 1992, Development of Competition and Diversity in Video Programming Distribution: Section 628 (c)(5) of the Communications Act: Sunset of Exclusive Contract Prohibition*, Federal Communications Commission, CS Dkt. No. 01-290. December 3, 2001, p. 8. "To make room (for Fox News), Malone cleared out existing networks like a bowling ball cracking into the headpin. The arrival of Fox News in Denver pushed Court TV to split the programming day with Spice, a pay-per-view sex network."

According to Grossman, Lawrence. 1997. "Bullies on the Block: Cable Television in New York City." *Columbia Journalism Review*. Jan. 11 1997, Fox fought a similar battle with Time Warner. In 1996, Time Warner (who owned a 20% stake in CNN's parent company, Turner Broadcasting) refused to allow any other cable network to compete with CNN on its cable systems. The nation's largest cable operator at the time, TCI, also owned a stake in CNN, and as a result would also not allow any competitive news services on its systems. Consequently, the U.S. public was denied an alternative news service—despite several attempts at entry from major programmers, e.g. NBC, into the 24-hour news channel business—until the consent decree in the merger of Time Warner and Turner forced the cable operators' hands.

Heidi Przybyla, "BBC uses D.C. as Beachhead for American Invasion," *Washington Business Journal*, suggests that even the BBC was stymied by MSOs who had other cable news programming interests. The BBC was prevented by cable MSOs from establishing a cable news channel as far back as 1991. In 1998, the BBC announced it hoped to form agreements with cable operators to carry BBC World, its international news service, within the next two or three years. A CNN spokesman, Steve Haworth, is quoted as saying, "Competition is always good for journalism, but I think that the BBC will find this to be a very tough marketplace for them. Remember, this is a second attempt for them," referring to BBC World's unsuccessful first attempt to gain US cable distribution. BBC World was launched in 1991 but only made its first appearance in the United States in 1997 after it made a deal with 25 public television stations for them to carry daily news bulletins. BBC, as the Commission knows, was only able to secure some digital distribution after it partnered with MSO-linked Discovery Channel, creating the BBC America channel.

[56] Breyer, R. Michelle, "CNN-Style channel planned for Austin," Austin *American Statesman*, August 22, 1998. p. D1; Tyson, Kim, "Belo adds KVUE to Texas TV Holdings," *Austin American-States-man*. February 26. 1999. P. A1. In August of 1998, Time Warner Cable announced that it would launch an all-news, 24-hour TV channel in Austin, Texas to be available to 220,000 area subscribers, with the specific intent of focusing on central-Texas news. The A.H. Belo Corporation, a media company that currently owns 18 broadcast television stations and four daily newspapers nationwide (including 4 stations and the *Dallas Morning News* in Texas), had also planned to start a cable news channel during the following year, "AT&T Pulls Plug on BayTV News Network," Multichannel News, July 9, 2001.

[57] Waterman and Weiss, 1997, p. 73; Davis, 1998, p. 143.

[58] Waterman and Weiss, 1997, p. 65; Davis, 1998, p. 97

[59] "Barry's New Baby," *Cablevision*, June 11, 2001.

[60] "Minority Nets Continue Distribution Push," *Multichannel News*, December 3, 2001, "BET's Lee Searches for Viacom Synergies," *Multichannel News*, December 3, 2001.

[61] *RCN Telecom Service of New York, Inc. v. Cablevision Corp., DIRECTV v. Comcast; EchoStar v. Comcast*. Problems can also occur on an event-by-event basis (see Everest, 2001, p. 4; Gemini Networks, 2001, p. 3.

[62] Joint Comments, p. 14.

[63] American Cable Association, "Comments of the American Cable Association." In *The Matter of Implementation of the Cable Television Consumer Protection and Competition Act of 1992, Development of Competition and Diversity in Video Programming Distribution: Section 628 (c)(5) of the Communications Act:*

Sunset of Exclusive Contract Prohibition, Federal Communications Commission, CS Dkt. No. 01-290, December 3, 2001, p. 15.

[64] "Comments of Everest Midwest Licensee LLC dba Everest Connections Corporation." In *the Matter of Implementation of the Cable Television Consumer Protection and Competition Act of 1992, Development of Competition and Diversity in Video Programming Distribution: Section 628 (c)(5) of the Communications Act: Sunset of Exclusive Contract Prohibition*, Federal Communications Commission, CS Dkt. No. 01-290, December 3. 2001, p. 6.; "Comments of Qwest Broadband Services, Inc." In *The Matter of Implementation of the Cable Television Consumer Protection and Competition Act of 1992, Development of Competition and Diversity in Video Programming Distribution: Section 628 (c)(5) of the Communications Act: Sunset of Exclusive Contract Prohibition*, Federal Communications Commission, CS Dkt. No. 01-290, December 3. 2001, p. 4.

[65] Everest, p. 6, American Cable Association, 2001, p. 15.

[66] Comments of the Competitive Broadband Coalition, *Implementation of the Cable Television Consumer Protection and Competition Act of 1992*, Cable Services Bureau Dkt. No. 01-290, at 10-11 [Dec. 3, 2001]), p. 11.

[67] Federal Communications Commission, 2001a, para. 28

[68] Joint Comments, 2001, p. 8.

[69] Qwest, 2001, p. 3; Dertouzos and Wildman, 1999.

[70] Joint Comments, 2001, p. 9.

[71] Richard Posner *Antitrust Law: An Economic Perspective* (Chicago: University of Chicago Press, 1976), Robert Bork, (*The Antitrust Paradox: A Policy At War With Itself*, (New York: Basic Books, 1978).

[72] J. Kaplow, "Extension of Monopoly Through Bundling," *Columbia Law Review*, 85:1985; J. A. Sykes, Ordover, A. Sykes and R.D. Willig, "Nonprice Anticompetitive Behavior by Dominant Firms Toward the Producers of Complementary Products," in F.M. Fisher, ed., *Antitrust and Regulation: Essays in Memory of John J. McGowen* (Cambridge, MA, The MIT Press, 1985).

[73] M. Whinston, "Tying Foreclosure and Exclusion," *American Economic Review*, 80: 1990.

[74] O.E. Williamson, "Assessing Vertical Market Restriction: Antitrust Ramifications of the Transaction Cost Approach," *University of Pennsylvania Law Review*, 127:1979; B. Nalebuff, "Bundling as an Entry Barrier," *Quarterly Journal of Economics*, 2004, "Bundling," Manuscript, School of Management, Yale University, 1999; Y. Bakos and Eric Brynjolfsson, "Bundling and Competition on the Internet: Aggregation Strategies for Information Goods," *Marketing Science*, 19:2000.

[75] J. Carbajo, D. de Meza and D. Seidman, "A Strategic Motivation for Commodity Bundling," *Journal of Industrial Economics*, 38: 1990; Y. Chen, "Equilibrium Product Bundling," *Journal of Business*, 70: 1997.

[76] J. P. Choi and C. Stefanadis, "Tying, Investment, and the Dynamic Leverage Theory," *Rand Journal of Economics*, 32:2001.

[77] J. P. Choi, "Tying and Innovation: A Dynamic Analysis of Tying Arrangements," *The Economic Journal* 114: 2004; J. P. Choi, "Preemptive R&D, Rent Dissipation, and the 'Leverage Theory'," *Quarterly Journal of Economics*, 110:1996.

[78] D. W. Carlton, "The Strategic Use of Tying to preserve and Create Market Power in Evolving Industries," *Rand Journal of Economics*, 33:2002;

[79] This observation has been well established in the economics literature for two decades. Recent works extends it to information goods in theory (Yannis Bakos and Erik Brynolfsoson, "Bundling Information Goods: Pricing Profits and Efficiency," ***Management Science***, December 1999, p. 1) and cable in reality (Gregory S. Crawford, ***The Discriminatory Incentives to Bundle in the Cable Television Industry***, April 2, 2004, p. 20).

[80] Numerous examples may be found in the initial comments filed in this proceeding. For example, CCVM (page 9) quotes an Echostar press release: "Among Viacom's strong-arm tactics is the demand that the DISH Network carry Viacom-owned channels of little or no measurable appeal to viewers in exchange for the rights to carry the 16 owned-and-operated CBS stations. Viacom also threatened to withhold the Super Bowl from the DISH Network customers until a federal judge intervened." According to the Pioneer Telephone Association's filing (page 6), "Many broadcast networks have begun to demand regular monthly licensing fees for access to 'free' over-the-air broadcast signals. … One local broadcast network affiliate even went so far as to demand that our small cable system would have to agree to purchase a fixed and substantial amount of advertising on the broadcaster's station, in exchange for consent to retransmit their broadcast system. The American Cable Association's filing states (on page 30) "ACA has described the smaller cable sector's increasing concern about the use of retransmission consents by network owners and affiliate groups. The principal tactic – requiring carriage of affiliated satellite programming as a condition of access to local broadcast signals. As a result, smaller cable companies and their

customers must pay for programming that they would not otherwise choose, solely to receive a free, over-the-air local broadcast station." Echostar's comments (page 1) states "MVPD's flexibility to offer a la carte and tiered services is inhibited today by many factors. First and foremost among them is the practice of large media conglomerates of bundling their must-have programming, including in particular the local network broadcast stations and the most popular cable networks, with programming that consumers do not want. Faced with widespread bundling, MVPDs currently have little choice but to offer broad *packages* [to consumers]." This is just a small sample of the myriad examples in the initial comments filed; this is not a competitive market.

Statement of John Goodman
President of the Coalition for Competitive Access to Content (CA2C)
Given before the Senate Judiciary Committee
December 7, 2006

Good morning. I want to express my appreciation to Chairman Specter and other members of the Judiciary Committee for the opportunity to participate in this hearing. I am pleased to represent the Coalition for Competitive Access to Content, a diverse group of companies and organizations that includes direct broadcast satellite (DBS) providers, broadband service providers (BSPs), telco new entrants, trade associations, and consumer groups that are committed to expanded competition for consumers in the video market place. These member organizations disagree on many other public policy issues, but nonetheless have come to the same conclusion regarding program access reform: assured access to content, particularly regional sports programming, is essential to the development of new high capacity networks that provide video and broadband competition.

Congress has long recognized the direct linkage between access to programming and additional video competition. In 1992, Congress promulgated the original program access provisions that required that video content owned by cable operators be made available to new entrants on fair and non-discriminatory terms.

Access to content is every bit as important today as it was in 1992. The FCC reviewed the application of certain program access rules in 2002 and, concluding that they were still essential, extended their application for 5 years. More recently, Senators Kohl and DeWine have sponsored several valuable GAO studies that document both the need for more wireline video competition and the relationship between access to content and the ability to compete in the marketplace. Regulators reviewing media mergers and

acquisitions have reached the same conclusion. The recent proceedings involving DirecTV/ Newscorp and the more recent Comcast/Time Warner/Adelphia transactions were approved with program access conditions related to sports and other programming. While we applaud the FCC's vigilance in this area, the CA2C believes that a statutory mechanism – not piecemeal adjudication – is necessary and justified to assure access to content.

The current level of vertical integration continues to be significant and expanding. Incumbent cable operator ownership of professional sports franchises and sports programming has expanded since 1992. In addition, a substantial portion of current vertical integration is concentrated in programming that has the highest viewership and value. The CA2C has attempted to document the current level of vertical integration. As we submit these summary profiles, the committee should feel free to share this information with the referenced cable companies for their review, validation, correction, and expansion as appropriate.

Unfortunately, Congress's program access provisions – written in 1992 – have not kept pace with today's technology and market structure. Cable operators can control exclusive rights to programming delivered to their headends by fiber rather than satellites. This is called the "terrestrial loophole." This is why a DBS subscriber in Philadelphia cannot receive Comcast's sports network with Flyers, Phillies, and 76ers games. And this is why a DBS subscriber in San Diego cannot receive Cox's sports network with Padres' games. The FCC has looked at this issue and concluded it has no authority to deal with any terrestrially delivered content until Congress amends current legislation.

Accordingly, the CA2C provided input for the "Sports Freedom" provisions in the telecommunications legislation introduced by Senators Stevens and Inouye earlier this year. These provisions closed the terrestrial loophole and enhanced the framework related to sports programming by, among other things, applying arbitration procedures to resolve certain disputes. These provisions were similar to the conditions created for the DirecTV/Newscorp merger.

We supported new legislation because it will have equal application to all MVPDs and sustain the right market structures to promote the development of competition. We should not rely on mergers, acquisitions, or other particular market events to address these industry-wide matters. Moreover, the FTC and the FCC should be directed and empowered to deal with anti-competitive issues in the market that include competitive access to content. In short, we do not seek for Congress to establish an entirely new legal framework of economic regulation and prices controls; nor should particular players in the market be singled out. Rather, a rational and measured updating and extension of the rules is in order.

Opponents to program access legislation have publicly acknowledged that the existing rules have been effective within their jurisdictional limits. However, they now oppose program access rules. They claim these rules are not needed because current markets are fully competitive and that there are limited current examples of abuse or denied access. But the market reality of key programming, especially local and regional sports programming concentrated in the hands of a few cable operators, undermines that view.

Even incumbent cable operators have asked for conditions guaranteeing access to content. The DirecTV/NewsCorp merger was the first time that an incumbent video provider faced a potential threat of some other network operator having control of essential content. Suddenly, they were asking for merger conditions that sounded a lot like the standards CA2C members have promoted to bring video competition to the market.

I want to again thank you for this opportunity to be with you this morning and look forward to your questions.

UNITED STATES OF AMERICA
FEDERAL TRADE COMMISSION
WASHINGTON, D.C. 20580

Prepared Statement of the Federal Trade Commission

Sports Programming and Cable Distribution:
The Comcast/Time Warner/Adelphia Transaction

Presented by
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Before the
Committee on the Judiciary
United States Senate

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I. Introduction

Mr. Chairman and members of the Committee, I am Michael Salinger, Director of the Bureau of Economics of the Federal Trade Commission. I am pleased to appear before you to present the Commission's testimony on the FTC investigation into the acquisition by Comcast Corporation and Time Warner Cable Inc. ("TWC") of the cable assets of Adelphia Communications Corporation ("Adelphia"), and into related aspects of the transaction in which Comcast and TWC swapped various cable systems.[1] After a thorough investigation, the Commission closed the matter without taking any action. The Commission's decision not to file an antitrust case was explained in a statement by Chairman Majoras and Commissioners Kovacic and Rosch.[2] Commissioners Harbour and Leibowitz issued a separate statement that concurred in part and dissented in part in the Commission's decision .[3] My testimony builds on those statements and explains the theoretical and empirical economic work that buttressed the staff's findings in this important investigation.

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[1] This written statement represents the views of the Federal Trade Commission. My oral presentation and responses to questions are my own and do not necessarily represent the views of the Commission or any Commissioner.

[2] Statement of Chairman Deborah Platt Majoras, Commissioner William Kovacic, and Commissioner J. Thomas Rosch, Concerning the Closing of the Investigation Into Transactions Involving Comcast, Time Warner Cable, and Adelphia Communications (January 31, 2006), *available at* http://www.ftc.gov/os/closings/ftc/0510151twadelphiamajoras kovacic_rosch.pdf.

[3] Statement of Commissioners Pamela Jones Harbour and Jon Leibowitz (concurring in part and dissenting in part), Concerning the Closing of the Investigation Into Transactions Involving Comcast, Time Warner Cable, and Adelphia Communications (January 31, 2006), *available at* http://www.ftc.gov/os/closings/ftc/0510151twadelphialeibowitz harbour.pdf (Advocating baseball-style arbitration because of concerns that the transaction, in some markets, created incentives for vertically integrated firms to disadvantage distribution competitors using sports programming.).

II. The Commission's Authority to Enforce Section 7 of the Clayton Act

The Federal Trade Commission is charged with enforcing Section 7 of the Clayton Act, which prohibits mergers and acquisitions where the effect of the transactions "may be substantially to lessen competition, or to tend to create a monopoly."[4] Under the Hart-Scott-Rodino Act, parties to mergers and acquisitions above certain thresholds generally must provide the Commission with an opportunity to review the proposed transaction prior to its consummation.[5] Prior to the expiration of an initial 30 day waiting period, the Commission can request that the parties provide additional information relating to the proposed transaction in order for the Commission to complete its review. In that event, the parties may not consummate their transaction until 30 days after they have substantially complied with the request for additional information. The Commission does not have the authority to prohibit parties from closing their transaction if, at the end of the staff's investigation, the Commission decides that a transaction is anticompetitive . Instead, to prevent parties from consummating a proposed merger or acquisition, the Commission must prove to a federal district court that it is reasonably likely that the transaction will have anticompetitive effects and thereby violate Section 7. In addition, if the Commission does not have sufficient evidence that the transaction would violate Section 7, the Commission will not seek or accept any structural divestiture or behavioral remedy even if they are offered by the parties or if the Commission believes that it could convince the parties to offer such relief.

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[4] 15 U.S.C. § 18.

[5] 15 U.S.C. § 18a. The Commission shares federal antitrust enforcement responsibility with the Antitrust Division of the United States Department of Justice.

III. The Adelphia Transaction

The Comcast/TWC/Adelphia transaction involved three parts. First, Comcast and TWC proposed to jointly acquire substantially all of the assets of Adelphia, which had filed for bankruptcy protection in June 2002. Under the agreement, TWC would receive various Adelphia cable systems totaling about 4.4 million subscribers and Comcast would acquire Adelphia's majority interests in two joint ventures with Comcast, representing about 1.36 million subscribers. Second, Comcast and TWC proposed to swap various cable systems. This portion of the transaction would result in Comcast receiving cable systems from TWC serving approximately 2.4 million subscribers and TWC receiving systems from Comcast serving 2.5 million subscribers.

Third, Comcast proposed to redeem its minority interests in TWC affiliated entities by receiving cash and various cable systems serving approximately 600,000 subscribers.

The net gain for Comcast from the overall transaction would be 1.8 million subscribers, increasing its total number of subscribers in wholly-owned systems to approximately 23.3 million. TWC would add 3.5 million subscribers, bringing its total number of subscribers in wholly-owned systems to approximately 14.4 million.

IV. The Investigation

The staff of the FTC's Bureau of Competition, working closely with the staff of the FTC's Bureau of Economics, conducted an extensive seven-month investigation to determine if the transaction and subsequent swaps would violate Section 7 of the Clayton Act. During the investigation, the staff conducted more than 40 interviews with various multichannel video programming distributors ("MVPDs"), including prospective entrants, independent and affiliated

programmers, consumer group advocates, regional sports networks ("RSNs"), sports leagues, and teams, and sports media consultants. The staff also reviewed more than one million pages of documents submitted by the parties, conducted investigational hearings of several key employees of the parties, and reviewed extensive data. Additionally, the FTC staff worked closely with the staff of the Federal Communications Commission ("FCC"), which was also investigating the proposed transaction under its own separate regulatory authority. Finally, the FTC staff discussed their investigation with representatives of several state attorneys general and briefed two Congressional subcommittees interested in the impact of the proposed transaction.

As an initial matter, the FTC staff determined that TWC and Comcast were not acquiring any cable assets that competed with their existing assets. In other words, the transaction eliminated no horizontal competition between the parties.

It was also very clear from the outset that the parties' principal objective in making the acquisition and asset swap was to increase "clustering" in the TWC and Comcast cable assets. Clustering enables cable firms to realize economies of scale associated with providing cable service in contiguous areas. By acquiring contiguous systems, TWC and Comcast could lower several categories of costs, such as management, administrative and marketing costs, as well as the expense of providing system upgrades. In addition, TWC and Comcast could use clustering to position themselves better to compete with local telephone companies and other providers in the delivery of video and telephone service.

Against this background, the FTC staff examined a number of vertical theories of potential competitive harm. The increased clustering of TWC and Comcast assets in some metropolitan areas gave them higher market shares of the households in those areas. The staff

considered whether that would enable the companies to extract anticompetitive contractual concessions with other firms involved in video distribution. One potential harm on which the FTC staff focused was the possibility that the transaction would cause consumer harm by affecting the terms on which MVPDs contract to carry RSNs.

RSNs have been a growth product for cable distributors. RSN programming consists of broadcasts of local sports programming of professional sports teams, including, for example, the National Basketball League, the National Hockey League, and Major League Baseball. The teams sell the rights to transmit some or all of their games to the RSN. The RSN then licenses to MVPDs the rights to provide the RSN programming to their subscribers. RSN programming is popular with the public, and RSNs typically charge a premium fee to the cable and satellite systems that distribute it.[6] In some areas, Comcast or TWC own or have an ownership interest in the local RSN.

The investigation explored whether the increased clustering from the transaction made it more likely that Comcast or TWC (or the RSN if owned by Comcast or TWC) would enter into the kinds of distribution arrangements that effectively foreclosed their competitors in the video distribution markets, *e. g.*, satellite, cable overbuilders, and telephone companies, from carrying the RSN programming. The investigation also analyzed whether the transaction was likely to cause Comcast or TWC to increase the prices at which they make available to other MVPDs the right to carry RSNs in which Comcast or TWC have an ownership interest.

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[6] There have been disagreements between RSNs and the cable and satellite distributors about the value of the programming. For over a year, the Mid Atlantic Sports Network ("MASN"), which owns the rights to the Washington Nationals broadcasts, was unable to agree to a carriage fee with Comcast, the largest cable network in the Washington area.

The FTC staff obtained significant evidence on the workings of sports programming markets, as well as each relevant geographic market affected by the transaction. The investigation focused on the limited number of geographic areas where the transaction would lead to significantly higher market shares for Comcast or TWC post-consummation. In each of these markets, the staff reviewed whether TWC or Comcast would actually be able to enter into exclusionary contracts, whether such exclusive contracts would be a viable strategy from the perspective of the sports team itself and whether exclusive contracts would be profitable for TWC or Comcast. After careful consideration, the staff concluded for various reasons that the evidence did not indicate that the proposed transaction was likely to make exclusive contracts profitable for either Comcast or TWC in the geographic markets impacted by the transaction. For example, in one geographic area, the staff's economic analysis demonstrated that it would be unprofitable for TWC to obtain the exclusive distribution rights for the local sports team because an insufficient number of satellite customers were likely to switch to TWC. Historical evidence from other markets where the RSN rights are held on an exclusive basis by a cable company show that the necessary level of switching could not be expected. In other markets, the evidence showed that the local sports teams were unwilling to enter into exclusive agreements and did not believe that TWC or Comcast would be able to force them to do so.

Even if the staff had determined that the transaction likely would have led to additional exclusivity in sports programming, that fact alone would be insufficient to conclude that the transaction would violate Section 7 of the Clayton Act. For a transaction to violate Section 7, the increased risk of foreclosure would need to create a likely risk of substantial harm to competition. That means, in essence, that the transaction would need to make consumers worse

off on balance than if the transaction did not take place. The Commission majority concluded that the investigation did not produce evidence that indicated that the transaction was likely to reduce competition. Indeed, under certain circumstances, exclusive arrangements may have procompetitive benefits for consumers by helping firms differentiate themselves and compete more effectively.

In certain industries, specialized regulatory agencies, in addition to the antitrust enforcement authorities, have the authority to review mergers. In the communications industry, this jurisdiction resides with the FCC, which has the authority under certain circumstances to prohibit a transaction under a broad "public interest" standard. As noted, the FCC also investigated the transaction and ultimately allowed it to be consummated,[7] finding that "the potential public interest harms of the transactions, as conditioned, are outweighed by the potential public interest benefits."[8] Some of the conditions required by the FCC for the transfer of the licenses include prohibiting Comcast or TWC from offering an affiliated RSN on an exclusive basis to any MVPD, prohibiting Comcast or TWC from unduly or improperly influencing the decision of any affiliated RSN to sell programming to an unaffiliated MVPD or the prices, terms and conditions of such sale, and providing for commercial arbitration if an MVPD and an affiliated RSN cannot reach an agreement on the terms and conditions of carriage, or if an unaffiliated RSN is unable to reach a carriage agreement with Comcast or TWC. These conditions will remain in effect for six years.

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[7] *See* http://www.fcc.gov/transaction/tw-comcast_adelphia-clockhis.html.

[8] FCC Approves Adelphia/Time Warner/Comcast License Transfer, FCC Press Release (July 13, 2006).

I want to conclude by stressing that the Commission's decision to close its investigation of this transaction does not mean that it cannot or will not intervene in these markets in the future. As the Commission noted in its closing statement, it will remain vigilant regarding the conduct of Comcast and TWC on a going-forward basis. If facts emerge that indicate Comcast or TWC is engaging in conduct that harms competition to the detriment of consumers, the Commission will investigate and, if appropriate, take action under the antitrust laws. Indeed, the types of exclusionary conduct by cable companies that would cause consumer harm would be directly actionable under Sections 1 and 2 of the Sherman Act.

Thank you for your attention. I would be pleased to respond to your questions.

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