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A Condensed Review of Retransmission Consent and Other Federal Rules Affecting Programmer-Distributor Negotiations

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Charles B. Goldfarb
Specialist in Industrial Organization and Telecommunications Policy
Resources, Science, and Industry Division

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Summary

When conflicts arise between a programmer (a broadcaster or a cable network owner) and a multichannel video programming distributor (MVPD, usually a cable or satellite operator) about the carriage of particular video programming, the price for that programming, or the tier on which the programming is to be offered to the end user, many consumers can be affected. Recently there have been several incidents in which a negotiating impasse between a programmer and a distributor has resulted in the programmer refusing to allow the MVPD to carry, or the MVPD choosing not to carry, a program network. While contractual terms, conditions, and rates are determined by private negotiations, they are strongly affected by a number of federal statutory provisions and regulatory requirements, including the statutory retransmission consent and must-carry rules, the FCC program exclusivity rules, local-into-local and distant signal provisions in satellite laws, copyright law provisions relating to cable and satellite, statutory commercial leased access requirements and program carriage and nondiscriminatory access provisions, and the FCC's media ownership rules.

The recent increase in negotiating impasses appears to be the result of structural market changes that have given programmers with "must-have" programming much greater leverage, particularly when they are negotiating with small distributors. Competitive entry in distribution — almost all cable companies now face competition from two satellite companies, and are beginning to face competition from telephone companies — has emboldened programmers with popular programming to demand cash payment from distributors for the right to carry that programming. In particular, local broadcasters increasingly are using the statutory retransmission consent requirement to demand cash payment from small cable companies who could lose subscribers to the satellite providers and new telephone entrants if they reach an impasse with the broadcaster and can no longer carry the local broadcast signals. In the past, the cable companies were the only MVPD in a market and could use that countervailing power to refuse to pay cash for carriage. Thus, ironically, competition in the distribution market may be resulting in higher programming costs that MVPDs may have to pass on to their subscribers.

The small cable companies have argued that some of the existing statutory and regulatory requirements were implemented at a time when cable was a monopoly and were intended to protect broadcasters. Now that the market dynamics have changed, they argue, some of these rules should be changed to allow for more even-handed negotiations. At the same time, however, as a result of consolidation and clustering in the cable industry there are a few very large cable companies, which primarily serve major markets, as well as the two national satellite operators, that appear to have sufficient market strength to be able to withstand many of the demands of the programmers with must-have programming and to place small independent programmers at a negotiating disadvantage. This report will be updated as warranted. For a more detailed version of this report, see CRS Report RL34078.

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Overview

Virtually all U.S. households have a television and almost 86% of these television households get their video programming by subscribing to a multichannel video programming distributor (MVPD) — in most cases a cable operator or a direct broadcast satellite (DBS) operator — rather than relying upon "free" over-the-air broadcast television signals.[2] As a result, when conflicts arise between programmers and MVPDs about the carriage of particular video programming, the price for that programming, or the tier on which the programming is to be offered to the end user (for example, on a basic or premium tier, on a "top 60" or a "top 120" tier, or on an analog or digital tier), many consumers can be affected.

Recently, there have been several incidents in which a negotiating impasse between a programmer and an MVPD has resulted in the programmer refusing to allow the MVPD to carry, or the MVPD choosing not to carry, a program network, forcing the MVPD's subscribers to choose between foregoing that program network or switching to a competing MVPD that did carry the program network.[3] There also have been a number of situations in which programmer-distributor negotiations have been resolved without any disruption in program carriage, but only after the negotiations played out in public, with subscribers and public officials being warned

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[1] This report is a condensed version of RL34078, *Retransmission Consent and Other Federal Rules Affecting Programmer-Distributor Negotiations: Issues for Congress*, by Charles B. Goldfarb.

[2] *In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, Federal Communications Commission, MB Docket No. 05-255, Twelfth Annual Report, adopted February 10, 2006, released March 3, 2006, at para. 8. As of June 2005, there were 109.6 million television households, of which approximately 94.2 million subscribed to an MVPD service. Of the latter, 69.4% received video programming from a franchised cable operator and 27.7% from a DBS operator.

[3] Even where the impasse involves broadcast programming that is transmitted over the air, most households that subscribe to an MVPD no longer have an antenna and therefore at a minimum would have to obtain and install an antenna to continue to receive the programming. In these cases, the MVPD typically has offered to provide a free "rabbit-ears" antenna, although in many cases a higher quality rooftop antenna is needed to get good over the air reception, and some households cannot get decent reception even with a rooftop antenna. Indeed, that inability to receive broadcast signals over the air was the original impetus for cable television, which was then called community antenna television, or CATV.

of the danger of losing access to particular programming and being encouraged by each side to contact the other side in order to place pressure on them to compromise.

Although the contractual terms, conditions, and rates at which programmers make their programming available to distributors are determined by private negotiations, there are a number of federal statutory provisions and regulatory requirements that strongly affect those negotiations.[4] These include:

- **the retransmission consent and must-carry rule**s, which govern the carriage of television broadcast signals by cable operators.[5] Under these rules, every three years each local commercial broadcast television station must choose between (1) negotiating a retransmission consent agreement with each cable system operating in its service area, whereby if agreement is reached the broadcaster is compensated[6] by the cable system for the right to carry the broadcast signal, and if agreement is not reached, the cable system is not allowed to carry the signal; or (2) requiring each cable system operating in its service area to carry its signal, but receiving no compensation for such carriage.[7] With this mandatory election,

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[4] For a detailed discussion of many of these statutory provisions and regulatory requirements, see Federal Communications Commission, *Retransmission Consent and Exclusivity Rules: Report to Congress Pursuant to Section 208 of the Satellite Home Viewer Extension and Reauthorization Act of 2004* (FCC Retransmission Consent Report), September 8, 2005, available at [http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-260936A1.pdf], viewed on May 21, 2007.

[5] The Cable Television Consumer Protection and Competition Act of 1992 (P.L. 102-385) established new rules, placed into Sections 325 and 614 of the Communications Act, as amended (47 U.S.C. 534). These rules apply to all cable operators. AT&T has claimed that, due to the technology employed, its MVPD service is an information service rather than a cable service, and thus not subject to cable rules. It views the retransmission consent rules as part of the copyright licensing framework and has agreed to negotiate for retransmission consent, but it views the must-carry rules as part of the cable regulatory regime that does not apply to its service. This is a controversial position.

[6] Compensation can take the form of cash payments, the MVPD's purchase of advertising time on the broadcast station, the broadcaster being given free advertising time on the MVPD's system, the MVPD's carriage (and tier placement) of other program networks owned by the broadcaster, or some combination of these.

[7] Section 614(b)(3)(A) of the Communications Act states that "A cable operator shall carry in its entirety, on the cable system of that operator, the primary video ... transmission of each of the local commercial television stations carried on the cable system...." As broadcasters have deployed digital technology, they have been able to use their new digital spectrum to transmit multiple video streams, not just a single stream, and/or to transmit their programming in high-definition as well as standard format. The broadcasters have sought an interpretation of the must-carry rule that would require cable operators to carry both their analog and their digital transmissions and, where they are offering multiple video streams or high-definition transmissions, that would require cable operators to carry their multiple streams and high-definition transmissions. To date, the FCC has not adopted that interpretation, but it is currently under discussion. As a result, carriage of these additional

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broadcasters with popular programming that are confident the local cable systems will want to carry that programming can make the retransmission consent election and be assured compensation for such carriage, and broadcasters with less popular programming that the local cable systems might otherwise not choose to carry can make the must carry election and be assured that their signal will be carried by all local cable systems. In many cases local broadcasters that are affiliated with a national broadcast network and have elected the retransmission consent option have (as part of their affiliation agreement) assigned to the network the right to negotiate the terms of retransmission consent.

- a number of Federal Communications Commission (FCC or Commission) **exclusivity rules**[8] that give local broadcasters the exclusive right to distribute certain programming (the network program non-duplication rules[9] and syndicated exclusivity protection rules[10]) or that protect a sports team's or sports league's distribution rights to a sporting event taking place in a local market (the sports programming blackout rules[11]). These rules, which tend to mirror

[7] (...continued)
video transmissions has been subject to retransmission consent negotiations, and is not mandatory on the part of cable or satellite operators.

[8] These rules are found in Part 76 of the FCC's rules. For a description of these rules, see the FCC Retransmission Consent Report, at footnote 8 and at paras. 17-30.

[9] Commercial television station licensees are entitled to protect the network programming they have contracted for by exercising non-duplication rights against more distant television broadcast stations carried on a local cable television system that serves more than 1,000 subscribers. Commercial broadcast stations may assert these non-duplication rights regardless of whether or not their signals are being transmitted by the local cable system and regardless of when, or if, the network programming is scheduled to be broadcast. Generally, the zone of protection for such programming cannot exceed 35 miles for stations licensed to a community in the Commission's list of top 100 television markets or 55 miles for stations licensed to communities in smaller television markets. In addition, a cable operator does not have to delete the network programming of any station which the Commission has previously recognized as significantly viewed in the cable community.

[10] With respect to non-network programming, cable systems that serve at least 1,000 subscribers may be required, upon proper notification, to provide syndicated protection to broadcasters who have contracted with program suppliers for exclusive exhibition rights to certain programs within specific geographic areas, whether or not the cable system affected is carrying the station requesting this protection. However, no cable system is required to delete a program broadcast by a station that either is significantly viewed or places a Grade B or better contour over the community of the cable system.

[11] A cable system located within 35 miles of the city of license of a broadcast station where a sporting event is taking place may not carry the live television broadcast of the sporting event on its system if the event is not available live on a local television broadcast station, if the holder of the broadcast rights to the event, or its agent, requests such a blackout. The holder of the rights is responsible for notifying the cable operator of its request for program deletion at least the Monday preceding the calendar week during which the deletion is (continued...)

the terms found in most network-affiliate contracts and station-syndicator contracts, limit the ability of a cable operator that has not been able to reach a retransmission consent negotiation with a local broadcaster that transmits network or syndicated programming to import the same programming from a more distant broadcaster.

- the **local-into-local and distant signal provisions** in various statutes that govern the carriage of television broadcast signals by satellite operators,[12] which define which households are eligible to receive distant broadcast network signals and local network signals and include several copyright provisions. Under the Satellite Home Viewer Act, direct-to-home satellite providers were granted a compulsory copyright license to retransmit television signals of distant networks stations to unserved households and to retransmit signals of certain non-network broadcast stations (called "superstations") to any household. The Satellite Home Viewer Improvement Act created a new statutory copyright license for satellite carriage of stations to any subscriber within a station's local market, without distinction between network and non-network signals or served or unserved households.

- cable-related statutory **copyright provisions**, which set specific terms, conditions, and rates, including mandatory licenses, for certain uses of programming.[13] For example, cable systems enjoy a royalty-free permanent compulsory copyright license — that is, do not have to pay copyright fees — for the carriage of broadcast signals of stations located in their local market areas (called "designated market areas" or DMAs). But cable systems are required to pay royalties under a congressionally granted compulsory

[11] (...continued)
desired. If no television broadcast station is licensed to the community in which the sports event is taking place, the 35-mile blackout zone extends from the broadcast station's licensed community with which the sports event or team is identified. If the event or local team is not identified with any particular community (for instance, the New England Patriots), the 35-mile blackout zone extends from the community nearest the sports event which has a licensed broadcast station. The sports blackout rule does not apply to cable television systems serving less than 1,000 subscribers, nor does it require deletion of a sports event on a broadcast station's signal that was carried by a cable system prior to March 31, 1972. The rule does not apply to sports programming carried on non-broadcast program distribution services such as ESPN. These services, however, may be subject to private contractual blackout restrictions.

[12] Satellite Home Viewer Act of 1988 (SHVA), P.L. 100-667, 102 Stat. 3935, Title II; Satellite Home Viewer Improvement Act of 1999 (SHVIA), P.L. 106-113, 113 Stat. 1501, 1501A-526 to 1501A-545; and Satellite Home Viewer Extension and Reauthorization Act of 2004 (SHVERA), P.L. 108-447, 118 Stat. 2809. For a discussion of these rules governing satellite carriage of local and distant signals, see CRS Report RS22175, *Satellite Television: Provisions in SHVERA Affecting Eligibility for Distant and Local Analog Network Signals*, by Julie Jennings.

[13] Copyright Act of 1976 (17 U.S.C. §§ 111, 119, and 122).

copyright license for the carriage of the signals of broadcasters located outside the DMA within which the cable system is located. The royalty-free license extends to the secondary transmission of out-of-DMA broadcast stations, however, if it can be shown that those out-of-DMA signals are "significantly viewed" by those households within the cable system's service area that only receive their television signals over-the-air.

- the **commercial leased access requirements** in section 612 of the Communications Act, which require a cable operator to set aside channel capacity for commercial use by video programmers unaffiliated with the operator.[14]

- the **program carriage provisions** in section 616 of the Communications Act directing the FCC to establish regulations governing program carriage agreements and related practices between cable operators or other MVPDs and programmers that

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[14] Communications Act of 1934, as amended, Sec. 612 (47 U.S.C. § 532). This statutory framework for commercial leased access was first established by the Cable Communictions Policy Act of 1984 (P.L 98-549, 98 Stat. 2779). Cable operators with fewer than 36 channels must set aside channels for commercial use only if required to do so by a franchise agreement in effect as of the enactment of Sec. 612. Operators with 36 to 54 activated channels must set aside 10% of those channels not otherwise required for use or prohibited from use by federal law or regulation. Operators with 55 to 100 activated channels must set aside 15% of those channels not otherwise required for use or prohibited from use by federal law or regulation. Cable operators with more than 100 activated channels must designate 15% of such channels for commercial use. The Cable Television Consumer Protection and Competition Act of 1992 (P.L. 102-385) established new rules, modifying Sec. 612, that required the FCC to (a) determine the maximum reasonable rates that a cable operator may establish for commercial use of designated channel capacity; (b) establish reasonable terms and conditions for such use, including those for billing and collections; and (c) establish procedures for the expedited resolution of disputes concerning rates or carriage. In implementing the statutory directive to determine maximum reasonable rates for leased access, the Commission adopted a maximum rate formula for full-time carriage on programming tiers and for à la carte services, and a prorated rate for part-time programming. One condition of the FCC's approval of the transfer of licenses of the bankrupt Adelphia Communications Corporation to Comcast Corporation and Time Warner Inc., is that if an unaffiliated programming network is unable to reach an agreement pursuant to the Commission's commercial leased access rules with Comcast or Time Warner, that network may elect commercial arbitration of the dispute, where the arbitrator would be directed to resolve the dispute using the rate formula specified in the Commission's rules. Another condition allows an unaffiliated regional sports network that is unable to reach a carriage agreement with Comcast or Time Warner to elect commercial arbitration of the dispute. See *In the Matter of Applications for Consent to the Assignment and/or Transfer of Control of Licenses: Adelphia Communications Corporation (and subsidiaries, debtors-in-possession), Assignors, to Time Warner Cable Inc. (subsidiaries), Assignees; Adelphia Communications Corporation (and subsidiaries, debtors-in-possession), Assignors and Transferors, to Comcast Corporation (subsidiaries), Assignees and Transferees; Comcast Corporation, Transferor, to Time Warner Inc., Transferee; Time Warner Inc., Transferor, to Comcast Corporation, Transferee,* Memorandum Opinion and Order, adopted July 13, 2006, released July 21, 2006, at paras. 109 and 181.

would prevent an MVPD from requiring a financial interest in a program service as a condition for carriage, from coercing a programmer to grant exclusive carriage rights, or from discriminating against an unaffiliated programmer in a fashion that unreasonably restrains the ability of that programmer to compete, when the programming is distributed over satellite.[15]

- the **requirements for nondiscriminatory access to programming in which a cable operator has an attributable interest** in section 628 of the Communications Act, which directs the FCC to establish rules to prevent a vertically integrated cable operator from discriminating in the prices, terms, and conditions at which it makes its programming available to non-affiliated MVPDs or have exclusive access to the programming in which it has an attributable interest.[16] But these prohibitions do not hold if the vertically integrated company's programming is distributed over terrestrial facilities (for example, over broadband lines), an exception that frequently applies to regional sports networks and potentially could apply to all cable program networks as broadband fiber optic cable becomes more widely deployed. This exception has been termed by some the "terrestrial loophole."

[15] Communications Act of 1934, as amended, Sec. 616 (47 U.S.C. § 536).

[16] Communications Act of 1934, as amended, Sec. 628 (47 U.S.C. § 548). When NewsCorp, which owns many cable networks, acquired from Hughes Electronic Corporation a large ownership interest in DirecTV, thus creating a vertically integrated programmer-distributor entity, the FCC conditioned the transfer of the spectrum licenses upon a agreement to abide by the same non-discrimination requirements, even though the new company would not have been so required under the existing statutory provisions. (*In the Matter of General Motors Corporation and Hughes Electronic Corporation, Transferors, and the New Corporation Limited, Transferee, for Authority to Transfer Control*, Memorandum Opinion and Order, FCC 03-330, Appendix F, 2004.) The FCC imposed a similar condition on the transfer of the licenses of the bankrupt Adelphia Communications Corporation to Time Warner and Comcast. See *In the Matter of Applications for Consent to the Assignment and/or Transfer of Control of Licenses: Adelphia Communications Corporation (and subsidiaries, debtors-in-possession), Assignors, to Time Warner Cable Inc. (subsidiaries), Assignees; Adelphia Communications Corporation (and subsidiaries, debtors-in-possession), Assignors and Transferors, to Comcast Corporation (subsidiaries), Assignees and Transferees; Comcast Corporation, Transferor, to Time Warner Inc., Transferee; Time Warner Inc., Transferor, to Comcast Corporation, Transferee*, Memorandum Opinion and Order, adopted July 13, 2006, released July 21, 2006, at Appendix B.

- the **broadcast ownership rules**[17] and **cable ownership rules**[18], which can affect the relative negotiating strength of programmers and distributors by restricting or allowing their reach in national or local markets. For example, some parties have argued that changes in broadcast ownership rules that allow broadcasters to own more than one television station in a market has significantly strengthened the retransmission consent bargaining position of those broadcasters that own or control more than one station in a local market.[19]

- certain **statutory exemptions from the antitrust laws** for sports leagues.[20]

Recently, there have been more frequent incidents of programmers and MVPDs failing to reach contractual agreements, and in several instances one or the other party — or end users who were affected by the impasse — have sought federal government intervention either at the FCC or with Congress. The parties seeking intervention often propose modification of existing statutory provisions or regulatory requirements that allegedly favor one side in the negotiations or undermine the successful consummation of negotiations. Although these impasses have involved a number of different issues, the most controversial (and widely publicized) conflicts have involved unresolved retransmission consent negotiations.

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[17] The FCC has long regulated broadcast ownership as a means of promoting diversity, competition, and localism in the media without regulating the content of broadcast speech, pursuant to sections 307, 308, 309(a), and 310(d) of the Communications Act (47 U.S.C. §§ 307, 308, 309(a), 310(d)), which authorize the Commission to grant and renew broadcast station licenses in the public interest.

[18] Section 613(f) of the Cable Television Consumer Protection and Competition Act of 1992 amended the Communications Act of 1934, directing the FCC to conduct proceedings to establish reasonable limits on the number of subscribers a cable operator may serve (horizontal limit) and the number of channels a cable operator may devote to its affiliated programming networks (vertical, or channel occupancy limit). Congress intended the structural ownership limits mandated by Section 613(f) to ensure that cable operators did not use their dominant position in the MVPD market, acting unilaterally or jointly, to unfairly impede the flow of video programming to consumers. (47 U.S.C. § 533(f))

[19] See, for example, Linda Moss and Mike Farrell, "Dueling for Dollars," *Multichannel Newswire*, March 5, 2007, available at [http://www.multichannel.com/index.asp?layout=articlePrint&articleid=CA6421302], viewed on June 28, 2007.

[20] In its 1922 ruling in *Federal Baseball Club of Baltimore v. National Baseball Clubs*, the Supreme Court ruled that baseball is a sport subject to state regulations, not a business involved in interstate commerce that would be subject to the federal antitrust laws. Although the Supreme Court acknowledged in its 1953 decision in *Toolson v. New York Yankees, Inc.* and again in its 1972 decision in *Flood v. Kuhn* that the baseball's antitrust exemption was "an anomaly," it ruled that it is up to Congress to change baseball's antitrust exemption. Other sports leagues do not enjoy the same broad antitrust exemption as baseball. But the Sports Broadcasting Act of 1961 (15 U.S.C. 1291) created a limited antitrust exemption that allows a league to negotiate the broadcasting rights for all the teams in a football, baseball, basketball, or hockey league. The act was amended in 1966 to exempt the combining of any professional football leagues.

There are three basic functional components to the provision of video programming: producing content; assembling content into a programming package, such as a network, that can be efficiently distributed; and distributing the programming to end users. (For convenience, in this report, the content assembler is called a programmer.)

In most cases, the programmer is a media company that packages individual programs or program series to create an over-the-air broadcast network or a cable network. That programmer may or may not own the production studio or sports team where the creative talent (actors, directors, athletes, etc.) directly produces the content, that is, may or may not vertically integrate "backwards" into direct production. On occasion, a sports team or league will vertically integrate forward by packaging its own games and other programming into a network under its own brand name (for example, a National Football League, Major League Baseball, or Yankees network). Also, sometimes a company is both a programmer and a distributor. For example, while an over-the-air broadcaster is just a programmer for the majority of households that receive their video programs from an MVPD, it is also a distributor of that programming to the minority of households that continue to receive their programming over-the-air. Similarly, most of the large MVPDs have vertically integrated backward and now have partial or total equity interests in some of the cable networks distributed over their cable or satellite systems. Several MVPDs also own sports teams (for example, Cablevision owns the New York Knicks) and thus are content producers, as well. Moreover, the large media companies that own broadcast networks also own cable networks and often tie distributor access to their broadcast networks to agreement to carry some of their cable networks.

Although existing statutory rules give the local broadcast station the right to negotiate the terms under which it makes its programming available for retransmission by MVPDs, many of those local broadcasters are affiliated with a national television network and, in their affiliation agreements with the national network, give the network the right to negotiate the terms of retransmission consent. Moreover, increasingly the negotiations between large programmers and large distributors also involve video-on-demand rights to large portions of the programmer's library of content, as well as provisions setting conditions on how the programmer can make its programming available for Internet, cellphone, and other new avenues of distribution. In addition, during the transition from analog to digital transmission and the initial deployment of high definition technology, programmer-distributor negotiations increasingly involve issues of whether a program will be carried in multiple formats (analog and digital, high definition and standard definition) and whether a network will be placed on an analog or digital tier.

The relationship between programmer and distributor is characterized by mutual need — the programmers need distributors that have direct contact with the potential audience; the distributor needs programmers with good content to attract subscribers. At the same time, there is an inherent tension as each seeks to capture the lion's share of the value that consumers place on that content. Each must weigh the potential loss if an impasse occurs and the programmer refuses to permit the distributor to carry the programming or if the distributor chooses not to carry the programming. For example, for the programmer that potential loss could take the form of foregone compensation from the MVPD and/or foregone advertising revenues as advertisers respond to a reduced audience,[21] both of which could be substantial if the MVPD's subscribers represent a significant portion of the programmer's total audience and if those subscribers do not switch to another MVPD that does carry the programmer's network. For the distributor, that potential loss could take the form of foregone subscriber revenue if, without the programming as part of its offering, some end users shift to a competing MVPD, as well as foregone advertising revenues. The losses could be substantial if many subscribers switched to a competing MVPD. Given these risks, negotiating impasses usually are avoided. Over time, market forces have led to the adoption of business models that serve content providers, programmers, and distributors.

But these business models represent an unstable equilibrium. When market conditions that affect the relative negotiating strength of programmers and distributors change, the newly strengthened party typically attempts to change the prevailing business model to its advantage. That is happening today. Programmers are taking advantage of structural market changes favorable to them to pressure MVPDs to make cash payments for programming that up till now was available either for free or for non-cash considerations (or, where cash payments have been made in the past, to make higher cash payments). Some MVPDs have had sufficient countervailing market power to resist, or limit, these changes, but others have not. This had led to calls by the smaller, often rural, MVPDs for modifications to the retransmission consent rules and other federal rules that allegedly favor programmers — and, in particular, local broadcast stations — in their negotiations with distributors.

Market Changes Affecting the Programmer-Distributor Relationship

The increase in programmer-distributor conflicts is, in large part, the result of several structural changes in the video market that are affecting the relative negotiating strengths of the various parties and hence undermining prevailing business models and affecting the availability and pricing of video programming for consumers.

More Distribution Options

The most significant structural change is the increase in the number of program distribution options. Today, programmers can distribute their product not only through traditional broadcast television stations and cable operators, but also through direct broadcast satellite operators and other satellite companies, the new

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[21] Kagan Research reported in *Economics of Basic Cable Networks, 2006* (at p. 5) that the advertiser-supported cable networks had gross advertising revenues of $13.7 billion and also had license fee revenues of $13.7 billion in 2004. Kagan projected that in 2009 those totals would be $25.4 billion and $24.2 billion, respectively. In contrast, broadcast networks historically have received almost all of their revenues from advertising, not from per subscriber fees imposed on MVPDs. Broadcaster attempts to increase those per subscriber fees have been at the core of the recent broadcaster-MVPD retransmission consent conflicts.

multichannel video offerings of the major telephone companies, cable "overbuilders,"[22] on-line video streams, and even cellular telephones. As a result, programmers have more options available to them to reach audiences and are able to negotiate with distributors from a position of strength, often demanding terms, conditions, and rates that are more favorable to themselves and less favorable to distributors than those that have prevailed in the past.[23] The market implications are greatest for "must-have" programming, such as major sports programming and the programming of the four major broadcast networks, for which a significant portion of subscribers have a sufficiently strong intensity of demand that they consider carriage of that programming a prerequisite for subscribing with an MVPD. An MVPD that does not offer must-have programming may find itself at a significant competitive disadvantage in the market. By contrast, the prevailing business model was developed — and some of the programmer-distributor contracts that are currently expiring were negotiated — in the early and mid 1990s, when cable operators typically were the monopoly MVPD in their service area and therefore had countervailing market power when negotiating with programmers, even programmers with must-have programming.

One group of distributors — small and mid-sized cable companies — has been placed in a particularly difficult position by this structural market change. They often face direct competition from the two major satellite companies, DirecTV and DISH Network. These cable companies have far fewer subscribers than the major satellite companies and thus when negotiating with programmers typically do not pose a serious risk to the programmers if there is an impasse and the programming is not carried; a programmer's foregone per subscriber fees from the cable companies and foregone advertising revenues would not be substantial. By contrast, a programmer's revenues could be significantly reduced if one of the satellite companies discontinued carriage, since each of the satellite carriers have more than 13 million subscribers.[24] Moreover, many of the smaller cable companies have limited or no ability to offer telephone and broadband access services and therefore limited ability to offer bundled video/telephone/broadband services that tend to foster customer retention even when favored programming is no longer carried. Thus, if an impasse were to occur, a smaller cable company would face significant risk of losing subscribers to satellite companies. In fact, where a smaller cable company has had an impasse with a programmer, sometimes the programmer or a satellite company that has a retransmission agreement with the programmer (and competes against the cable company) has offered a "bounty" of up to $200 to households to switch to the

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[22] These are companies that have been awarded franchises by local franchising authorities and have built their own wireline networks in areas already served by an incumbent cable operator. These overbuilders frequently offer broadband access service as well as cable service and often serve smaller geographic areas than the incumbent cable operator, sometimes serving only high-rise buildings.

[23] For example, a Sinclair Broadcast Group executive reportedly has stated that as cable, satellite, and telephone companies all seek to distribute Sinclair's broadcast signals, Sinclair has more bargaining power than it had in the past. See Joe Morris, "Cable, WCHA at Odds: Broadcast Dispute Might Go To Court," *Charleston Gazette*, July 7, 2006, at p. 1.C.

[24] This is a greater concern for a national programmer (such as a cable network or a broadcast network) than for a local programmer (such as a local broadcast station).

satellite service, with these offers marketed over the programmer's network while the programmer-cable company negotiations are still on-going.[25]

Ironically, the market consequence of greater competition in the distribution of video programming appears to be greater negotiating leverage for programmers with popular — and especially must-have — programming, resulting in higher programming prices that MVPDs tend to pass through at least partially to subscribers.

Consolidation and Clustering of Cable Operators

At the same time that additional distribution options have become available to video programmers, consolidation (acquisitions resulting in a small number of large firms serving an increasing portion of total subscribers, nationwide) and clustering (acquisitions resulting in individual firms serving an increasing portion of subscribers in a particular local market) are occurring among cable operators and the two major satellite operators are growing, so that the largest video distributors are serving a higher share of total MVPD subscribers than they have in the past and the large cable operators' serving areas have become increasingly concentrated into a small number of very large clusters. These trends are the result of acquisitions by the large cable companies of smaller cable companies, swaps among cable systems of local cable systems that have allowed single companies to become the dominant cable provider in metropolitan statistical areas or beyond, and successful market growth by the two large DBS operators, DirecTV and DISH Network.

Table 1 lists the 25 largest cable operators, which are often referred to as multiple system operators or MSOs, and the number of subscribers they had as of December 2006. It is noteworthy that the largest MSO, Comcast, had almost as many subscribers as numbers 3 through 25 combined.

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[25] It is not always clear whether it is the satellite company or the programmer that is actually paying the customer to switch MVPD. For example, when Sinclair Broadcast Group and Mediacom Communications were in an impasse in retransmission consent negotiations late in 2006, Mike Wilson, the general manager of Sinclair's Fox 17 station in Iowa issued a statement to viewers, stating in part that "the termination of our relationship with Mediacom need not limit your ability to continue to watch us.... you may choose to subscribe to either DirecTV or to the Dish Network, both of which will continue to carry FOX 17. We particularly encourage you to call DirecTV ... because if you sign up with them prior to December 1, 2006 and comply with certain requirements, FOX 17 WILL PAY YOU $150 (which will be applied as a rebate against your DirecTV bill, which will be applied as fifteen $10 rebates against each of your first 15 monthly DirecTV bills)!" The Wilson statement is available at [http://www.longren.org/2006/10/30/more-on-mediacom-vs-sinclair/], viewed on June 27, 2007.

Table 1. The 25 Largest Cable Operators as of December 2006

Rank	Cable Operator	Number of Subscribers	Rank	Cable Operator	Number of Subscribers
1	Comcast	24,161,000	14	Service Electric	287,800
2	Time Warner	13,402,000	15	Armstrong Group	231,600
3	Charter	5,398,900	16	Atlantic Broadband	231,500
4	Cox	5,395,100	17	Midcontinent	195,900
5	Cablevision	3,127,000	18	Pencor Services	182,900
6	Bright House	2,307,400	19	Knology	178,600
7	Mediacom	1,380,000	20	Millenium Digital	157,100
8	Suddenlink	1,360,000	21	Buckeye	145,500
9	Insight	1,322,800	22	Northland	144,300
10	CableOne	641,500	23	MidOcean	138,400
11	RCN	371,100	24	Grande	137,500
12	WideOpenWest	361,200	25	MetroCast	137,300
13	Bresnan	294,000			

Source: Table prepared by National Cable and Telecommunications Association based on data from Kagan Research, LLC, available at [http://www.ncta.com/ContentView.aspx? contentId=73], viewed on June 28, 2007.

Had the satellite operators, DirecTV and DISH Network, been included in this list, they would have ranked second and fourth, respectively.[26] But satellite operators have a somewhat different market impact because they have subscribers dispersed all around the country, while cable companies tend to cluster their systems in a limited number of geographic areas. (An individual cable cluster most likely consists of multiple cable franchises negotiated with many local jurisdictions.) In the early years of the cable industry, most of the larger firms bidding for cable franchises did not focus their efforts on narrow geographic regions. As a result, the larger cable operators tended to have cable franchise that were widely scattered geographically. Subsequently, many of these large firms traded franchises, to develop clusters in a smaller number of geographic areas. Clustering provides economies of scale in operations, marketing, and customer service. It also strengthens a cable operator's retransmission consent negotiating position with broadcasters, who are less likely to risk the foregone subscriber fees and advertising revenues from an impasse with (and discontinued signal carriage by) a cable operator if that operator serves a large portion of the broadcaster's serving area.

[26] According to the 2006 10-K reports filed by DirecTV and EchoStar Communications (the parent of DISH Network) with Securities and Exchange Commission (SEC), as of December 31, 2006, DirecTV had approximately 16 million subscribers in the U.S. (at p. 3) and DISH Network had 13.105 million subscribers (at p. 1).

There are 113 cable clusters serving at least 100,000 subscribers.[27] But 102 of those clusters are owned by the five largest cable operators and only two are owned by cable operators that are not among the 10 largest.

Cable system consolidation and clustering have different programmer-distributor negotiating implications when the programmer has national reach (for example, a national cable program network or a national broadcast network) vs. local reach (for example, a local broadcast station). As explained below, consolidation increases the leverage of a cable system relative to national program networks, while clustering increases the leverage of a cable system relative to local broadcast stations.

Negotiating with a cable program network.

Cable program networks get approximately half their revenues from per subscriber fees imposed on MVPDs and half from advertising.[28] And those advertising fees depend on the number of subscribers reached, so the more subscribers an MVPD reaches, the more valuable that MVPD is to the program network. Cable program networks that fail to achieve substantial penetration on MVPD systems face financial peril. In recent proceedings at the FCC, parties have filed comments asserting that in order to generate the advertising revenues necessary for success, a national program network must reach between 40 and 60 million, and perhaps as many as 75 million, subscribers.[29] Carriage on the major MVPD systems — Comcast, Time Warner, DirecTV, and DISH Network — therefore is key to cable program network success. Cable network business strategies therefore focus on obtaining and retaining such carriage. For a new cable network, that might involve giving one of the major MVPDs an equity interest in exchange for carriage. For an established cable network with a strong brand identity, that might involve creating a sister network and demanding of MVPDs carriage of the new network in lieu of cash for carriage of the established network. But even an established program network is unlikely to risk a negotiating impasse that results in discontinued carriage by any of those large MVPDs.

The 20 most widely distributed advertiser-supported cable program networks each are available to more than 90,000,000 households via MVPD subscription.[30]

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[27] Kagan Research, *Broadband Cable Financial Databook*, 26th edition, 2006, at pp. 27-28.

[28] See footnote 21above.

[29] See *In the Matter of Applications for Consent to the Assignment and/or Transfer of Control of Licenses: Adelphia Communications Corporation (and subsidiaries, debtors-in-possession), Assignors, to Time Warner Cable Inc. (subsidiaries), Assignees; Adelphia Communications Corporation (and subsidiaries, debtors-in-possession), Assignors and Transferors, to Comcast Corporation (subsidiaries), Assignees and Transferees; Comcast Corporation, Transferor, to Time Warner Inc., Transferee; Time Warner Inc., Transferor, to Comcast Corporation, Transferee,* Memorandum Opinion and Order, adopted July 13, 2006, released July 21, 2006, at para. 101 and fn. 354.

[30] See table of the advertiser-supported cable program networks available to the largest number of MVPD subscribers, prepared by National Cable and Telecommunications Association based on data from Kagan Research, LLC, available at

(continued...)

These cable program networks enjoy carriage on each of the four largest MVPD systems — the systems of the two largest cable operators as well as on the systems of the two major DBS operators.[31] As shown in **Table 1**, subscriber reach falls quite quickly beyond those large MVPDs. While cable program networks will seek carriage on all MVPDs, as the subscriber reach of the MVPD falls, the financial risk to a cable program network provider of failing to reach a carriage arrangement with the MVPD falls. This may make it easier for the cable network provider to push harder for a high per subscriber fee from a smaller MVPD. From the perspective of a small or mid-sized cable operator, however, failing to reach a carriage arrangement for a relatively popular cable program network that is carried by DirecTV and/or DISH Network can be risky. Thus, a cable operator's negotiating position vis-a-vis cable network programmers will be strengthened by consolidation.

Negotiating with a national broadcast network.

When a local broadcast station that is affiliated to a broadcast network has assigned its retransmission consent rights to the network, the negotiations between the network and the MVPDs are likely to be somewhat akin to those between large cable programmers and MVPDs — with the national subscriber reach of the MVPD an important factor. The major broadcast networks own both multiple broadcast streams and cable networks, and are likely to seek compensation in some combination of: the MVPD's carriage (and tier placement) of other program networks owned by the broadcaster, the MVPD's purchase of advertising time on the broadcast station, the broadcaster being given free advertising time on the MVPD's system, and cash payments. The broadcast networks, in offering the most popular programming, enjoy an even stronger negotiating position than most cable program networks, but even the major broadcast networks are unlikely to want to risk an impasse with a large MVPD that serves 10 million or more subscribers.

Negotiating with a local broadcast station or non-network broadcast group.

The negotiating dynamic may be quite different when a broadcast station is conducting its own negotiations with MVPDs — which appears to be happening more often these days. In this situation, the broadcaster's reach is limited to the local market in which its station is located or, in the case of a station that is part of a non-network broadcast group, the local markets in which the group has stations. Its concern will not be with the total subscriber reach of the MVPDs with which it is negotiating, but rather with the subscriber reach of those MVPDs within the local markets in which the group has stations. DBS operators are likely to offer service in many or all of those markets, but an individual cable company, even one as large as Comcast or Time Warner, is unlikely to operate in all those local markets. What becomes most important, then, is whether the cable company is clustered in the

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[30] (...continued)
[http://www.ncta.com/ContentView.aspx?contentId=74], viewed on June 28, 2007.

[31] Moreover, these cable program networks most likely have attained carriage on the most basic tier offered by these MVPDs — that is, the one with largest number of subscribers, for example, the "top 60" tier, rather than the "top 120" tier.

market or markets in which the broadcaster has stations. There are many cable clusters that serve a substantial portion of the households in the local broadcast markets in which they are located. In these situations, the local broadcasters are less likely to risk a negotiating impasse with the clustered cable company and therefore likely to face constraints on the demands they can make for retransmission consent compensation.

Charter Communications CEO Neil Smit has stated that actions it has taken to increase the densities of its existing clusters have strengthened its position in retransmission consent negotiations, making it more difficult for station groups to play hardball given that they would put greater portions of their ad revenues at stake.[32] One industry observer has described this negotiating situation as follows:

> Cable operators have more clout than telcos and even DBS. Cable operators are big enough in major markets to take a broadcaster dark in 60%-80% of local homes overnight. That would guarantee immediate pain as major advertisers cancel. But a DBS operator might serve just 10%-20% of local homes so it can inflict far less pain. Telcos are in the weakest position.[33]

More Program Networks/Fragmented Audiences

Another major structural market change has been the dramatic expansion in the number of program networks (sometimes referred to as channels) available to consumers, with a resulting fall in average audience size per channel. The number of video channels received by the average U.S. household increased from 18.8 channels in 1985 to 104.2 channels in 2006, but neither the number of television households nor the average household viewing time per day increased nearly so dramatically during that period.[34] Thus the average audience size per program network has fallen substantially.

This proliferation in program networks has had two general market implications. On the one hand, the typical program network has an audience share of less than 1%, and unless its programming has very strong appeal to a subset of subscribers who would be willing to pay separately for that programming, is not likely to command

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[32] See Mike Farrell, "Smit: Charter System Sales Could Help Retrans Talks," *Multichannel Newswire*, March 7, 2007, available at [http://www.multichannel.com/index.asp?layout=articlePrint&articleid=CA6422613], viewed on June 27, 2007.

[33] John M. Higgins, "Money Talks: CBS Braces for Cable Showdown," *Broadcasting & Cable*, March 27, 2006, at p. 10.

[34] Nielsen Media Research data from the following sources — number of channels received, National People Meter Sample, presented in a press release dated March 19, 2007, available at [http://www.nielsenmedia.com] (under "Latest News," then "More," then "Last Six Months," the March 19, 2007), viewed on June 27, 2007; television households, NTI, September each year, available at [http://www.tvb.org/rcentral/mediatrendstrack/tvbasics/02_TVHouseholds.asp], viewed on June 27, 2007; time spend viewing television, per day, per household, NTI annual averages, Audimeter sample for 1985, People Meter Sample for all other years, available at [http://www.tvb.org/rcentral/mediatrendstrack/tvbasics/08_TimeViewingHH.asp], viewed on June 27, 2007.

much compensation from MVPDs for carriage rights. It may well be that if such a program network is not affiliated with an MVPD or with a major programmer it will have to rely on the commercial leased access rules and pay to gain access to an MVPD.[35]

On the other hand, the relatively few program networks that attract larger audiences are valuable to MVPDs for two reasons. First, a program network that attracts a larger audience is, other things equal, likely to have more viewers who might choose among competing MVPDs based on the availability of that network's programming; there is greater business risk to MVPDs not to carry that program network. Second, larger audiences tend to attract more advertising revenues for the MVPD.

According to Kagan Research, in 2005, of the several hundred advertising-supported cable networks, only 8 received from MVPDs average monthly license fees of 40 cents or more per subscriber, only 24 received fees of 20 cents or more, only 51 received fees of 10 cents or more, and only 112 received fees of 2 cents or more.[36] Clearly, the current price-driven programmer-distributor impasses do not directly involve the vast majority of program networks; programmers cannot command significant price increases for them and, in any case, losing the right to carry such a program network is unlikely to result in significant subscriber migration to competing MVPDs.

Some program networks, however, remain extremely valuable to MVPDs and, in fact, in some ways network proliferation has increased the value of these networks, even if their audience share has shrunk over time. Although the major broadcast networks' share of U.S. television household usage has fallen substantially over time, they continue to capture relatively large audiences. More than 25% of all television usage (including usage to watch VCRs and to play video games) is spent viewing the national programming offered by the four major broadcast networks and the local and syndicated programming offered by those networks' local broadcast station affiliates, and that is projected to continue to approach 25% of all usage at the end of the decade.[37] Since both the national programming and the local programming offered by these major network affiliates attract such relatively large audiences, an MVPD in a market where there is competition from other MVPDs could find itself at risk of losing substantial numbers of subscribers if a contract negotiation impasse resulted in it not carrying the programming of one of those affiliates.

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[35] See footnote 14 above.

[36] Kagan Research, *The Economics of Basic Cable Networks, 2006,* 12th Annual Edition, 2005, at pp. 58-60.

[37] Media Dynamics, Inc., *TV Dimensions 2006,* Annual Report. The usage shares attributed to broadcast networks covers their network-originated programming. The usage shares attributed to network affiliates covers their locally-originated programming plus syndicated programming. The average hours of set usage weekly counts multiple-set usage to different sources at the same time as separate exposures.

Data on the cumulative weekly reach of various program networks also show the breadth of viewership enjoyed by the major broadcast networks.[38] In any given week *each* of the four major networks is viewed (for at least one ten-minute segment) by more than 70% of all U.S. television households, while the cable network with the greatest weekly cumulative market reach, USA, is viewed by only 37.7% of U.S. television households.[39]

Moreover, the four major broadcast networks provide almost all of the most popular television programs.[40] During the 2005-2006 television season, the 100 individual television programs with the largest audiences all were major broadcast network programs. Although other broadcast programmers provided shows that ranked among the second one-hundred in ratings, the highest-rated advertiser-supported cable network program was ranked 236, the second highest-rated cable network program was ranked 389. For the foreseeable future the major broadcast networks are likely to continue to provide the lion's share of the most popular television programs.

There often is a timing element to must-have programming that programmers can use strategically in their negotiations with distributors. Television households are far more likely to switch MVPD providers if they fear the loss of particular time-sensitive programming, such as the Super Bowl, the Olympic Games, the National Football League season, or the finale of American Idol or some other extremely popular series. Some programmers have effectively timed their negotiations with distributors to take advantage of such program schedules.[41] In some cases, programmers with the rights to sports events have agreed to month-to-month extensions of lapsed agreements with MVPDs until a time when a key sports event was imminent and then used the threat of lost access to that sports event as leverage to complete a more favorable distribution agreement with the MVPDs.[42]

Despite the dominance of the four major broadcast networks, at least a dozen cable networks have succeeded in attracting more than 25% of all television households for at least one 10-minute segment each week. Not surprisingly, these cable networks generally have been able to command larger than average per

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[38] Nielsen Media Research Television Activity Report, NHI First Quarter 2007, available at [http://tvb.org/rcentral/mediatrendstrack/tvbasics/ 10_Reach_BdcstvsCable.asp], viewed on June 27, 2007.

[39] If the recent decreases in major broadcast network audiences persist, however, the gap between broadcast network reach and cable network reach may shrink.

[40] Television Bureau of Advertising, Viewer Track, "Top-rated programs of 2005-06 in Households," based on data from Nielsen Galaxy Lightning 9/19/05-5/24/06, Advertising-Supported Subscription TV only, available at [http://www.tvb.org/central/ViewerTrack/ FullSeason/05-06-season-hh.asp], viewed on June 27, 2007.

[41] See, for example, Linda Moss and Mike Farrell, "Dueling for Dollars," *Multichannel Newswire*, March 5, 2007, available at [http://www.multichannel.com/index.asp?layout= articlePrint&articleid=CA6421302], viewed on June 27, 2007, which includes a discussion of how broadcasters have used timing to their negotiating advantage.

[42] Id.

subscriber fees from MVPDs.[43] Those networks commanding high per subscriber license fees that did not have broad reach into households tended to fall into one of two categories — sports networks or news networks — that have unique demand characteristics.[44]

Audience fragmentation also appears to be affecting the relationship between the large broadcast networks and their affiliated broadcast stations. Traditionally, under the network-affiliate contracts, the networks assumed the retransmission consent rights of their affiliates, in exchange for making cash payments to the affiliates. The broadcast networks then typically negotiated retransmission consent agreement in which the MVPDs agreed to carry new, or less popular, cable program networks owned by the broadcast networks (for example, MSNBC or ESPN Classic) as partial compensation for carrying the broadcast network. Recently, the broadcast networks seem to be changing their business strategy, giving back to their affiliate broadcast stations the right to negotiate retransmission consent compensation from MVPDs in exchange for reducing or eliminating the cash payments they make to their affiliate stations. According to a report in *Multichannel Newswire:*

And during the past several years, the "Big Four" networks have renegotiated affiliate deals to eventually eliminate once-lucrative network compensation fees paid to stations to carry programming from ABC, CBS, Fox, and NBC.

> Perhaps not coincidentally, those fees began to decline precipitously in 2005, right around the time that retransmission consent revenue [for the affiliate stations] began to rise. For example, in 2005, network compensation at Hearst-Argyle fell 35.9% from $28.8 million to $19.1 million and dipped another 48.7% in 2006 to $9.8 million.

At Nexstar, network compensation dipped 22.4% in 2005, to $6.6 million, and fell 36.4% to $4.2 million in 2006. At Sinclair, the drop-off was less dramatic — 7% in 2005, from $14.3 million to $13.3 million (the company has not yet released 2006 network compensation) — but the station owner expects more dramatic declines in the coming years.

In its 2005 annual report, Sinclair even went so far as to say that retransmission consent fees have "replaced the steady decline in revenues from television network compensation."[45]

The trend toward greater program network proliferation and fragmented audiences is complicated by several significant technologically-driven forces. During the transition from analog to digital technology, programmers of both cable networks and broadcast networks are trying to get MVPDs to carry their programming in both

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[43] Kagan Research, *Economics of Basic Cable Networks, 2006*, 12th Annual Edition, 2005, at p. 58.

[44] For example, in an interview that appeared in the May 7, 2007 edition of *Broadcasting & Cable* (at pp. 14-16), Jim Bewkes, president and chief operating officer of Time Warner, stated that about half of CNN's viewers do not watch any other television, "so if you're trying to reach that audience, you want to reach them there."

[45] Linda Moss and Mike Farrell, "Dueling for Dollars," *Multichannel Newswire*, March 5, 2007, available at [http://www.multichannel.com/index.asp?layout=articlePrint&articleid=CA6421302], viewed on June 27, 2007.

analog and digital format — and to carry their digital programming in high definition as well as standard format. Thus, a single program network now might seek multiple channels on an MVPD system to offer analog, digital, and high-definition feeds. At the same time, the deployment of digital technology is allowing broadcasters to provide multiple digital signals (that is, multiple video programs) on their licensed spectrum, not just a single signal. A broadcaster that previously provided programming for one channel on an MVPD system now may seek multiple channels, which, depending on how the FCC ultimately implements the must-carry and retransmission consent rules in a multicast digital environment, could result in a larger portion of an MVPD's system being set aside exclusively for broadcast program networks. Whether these technological changes strengthen the negotiating positions of programmers or distributors may well depend almost entirely on how the FCC, or Congress, adopts the must-carry and retransmission consent rules for this new environment. In the short run, however, to obtain carriage of multiple signals in their retransmission consent negotiations with MVPDs, broadcasters may have to compromise on other objectives, such as higher cash payments.

Cable System Revenue is Growing From High Speed Internet Access and Telephone Services

Most cable operators have upgraded their systems over the past decade and now are able to offer a wide array of services over their broadband networks, including high speed data, telephone, and digital video services, as well as traditional analog video services. The revenue base of the cable system operators is diversifying, with fastest growth occurring in high speed data, telephone, and digital tier video services.[46] Most subscribers who select these newer services purchase them as part of a bundled package with basic cable service. This trend is helping cable operators in their negotiations with programmers in two ways. First, subscribers who purchase service bundles are less likely to switch to a competing MVPD if their current provider were to lose carriage of a particular program network, even a popular network. This is particularly the case if the competing MVPD cannot offer the full array of services that the cable company does; for example, satellite companies often cannot offer high speed data and telephone services at a price or uplink speed that is competitive with cable companies. Second, if a cable company is enjoying rapid revenue growth from non-video services, it may be more willing to hold the line in its negotiations with programmers because it is easier to absorb a potential loss of video revenues stemming from an impasse and loss of program carriage when other revenues are growing. On the other hand, the revenues generated by these "triple play" offerings may allow a cable company to pay more for programming.

There has been an interesting market response to the growth in cable system revenues from non-video services. As these new revenue sources have increased the average revenue generated per subscribing household (known in the industry as average revenue per unit, or ARPU), the value of existing cable systems has grown and this has been reflected in the price per subscriber at which cable systems have been sold. This, in turn, has affected at least one programmer-distributor negotiation. On July 1, 2006, Suddenlink Communications completed the purchase from Charter

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[46] Kagan Research, *Broadband Cable Financial Databook*, 26th Edition, 2006, at p. 8.

Communications of cable systems in West Virginia with 240,000 subscribers, 200,000 of whom live in the Charleston, WV service area of a Sinclair Broadcast Group-owned television station (WCHS, an ABC affiliate) and another television station (WVAH, a Fox affiliate) for which Sinclair has a local marketing agreement. The retransmission consent agreement between Charter and Sinclair had expired prior to the Suddenlink purchase,[47] so Suddenlink entered retransmission consent negotiations with Sinclair before the purchase was completed. Sinclair had sought $4 million in cash payments over three years. But when Sinclair learned that the purchase price was $800 million, it raised its demand to more than $42 million. Sinclair's vice president and general counsel reportedly stated that, "If they're paying $3,200 per sub[scriber], why shouldn't a piece of that be coming to us?"[48] This raises an interesting issue. To the extent the high cable system valuation is a function of the programming provided by Sinclair, Sinclair would seem to have a strong claim for larger cash payments. But to the extent the valuation is not related to Sinclair's programming, if Sinclair were nonetheless able to command larger cash payments that might suggest that the current retransmission consent process may be allowing programmers to siphon off funds that might, from a public policy perspective, be better left to cable operators to expand their broadband infrastructure capabilities.

Issues for Congress: Proposals for Statutory and Regulatory Change

The negotiations between programmers and distributors, although private, are strongly affected by statutory and regulatory requirements and cannot be properly characterized as free-market. Those requirements were enacted to foster the three pillars of U.S. media policy — localism, diversity of voices, and competition. Congress tried to craft them in a fashion that would minimize — but not eliminate — government intrusion in the market. The specific public policy objectives they were intended to further include: fostering local programming, especially local broadcast programming; fostering diversity of news and public affairs voices and entertainment choices; fostering competition in all media markets; encouraging innovative programming; keeping cable and satellite subscription rates affordable; and fostering infrastructure investment. Sometimes government intervention to foster one of these objectives will impede another.

It is possible that, as market conditions have changed, statutes or regulations that did not unduly favor one party over another when they were enacted, or that were intended to favor a party that was viewed as being in a disadvantageous position, now affect negotiations in an unintended fashion. For example, the various rules relating to cable carriage of broadcast signals — retransmission consent, network non-duplication, and syndicated exclusivity rules — were developed at a time when the local cable operator typically was the only MVPD in a broadcaster's service area and

[47] See Mike Farrell, "Suddenlink, Sinclair in Retrans Clash," *Multichannel News*, July 5, 2006, available at [http://www.multichannel.com/index.asp?layout=articlePrint&articleID=CA6349903], viewed on June 27, 2007.

[48] Mike Farrell, "Suddenlink in Retrans Row," *Multichannel News*, July 10, 2006, at p. 8.

there was concern that cable operators might refuse to carry local signals or in some other way threaten the viability of local broadcasting. Today, with competitive provision of multichannel video services by satellite and telephone systems, the tables are somewhat turned, and broadcasters with must-have programming often can negotiate from a position of strength, especially with cable systems whose subscribers do not represent a significant portion of a broadcaster's audience.

The earlier discussion of market trends showed there is great variability in the negotiating strength of both individual programmers and individual distributors. Almost all impasses that resulted in MVPDs not carrying particular programming occurred outside major markets. Despite the trend toward greater programmer negotiating strength, in major markets distributors tend to have enough market clout to be able to reach agreements they can live with. This is not the case in smaller markets. In this new market environment, it is possible that the "one size fits all" regulations currently in place may no longer be fostering the public policy objectives they were intended to advance — especially outside major markets. Most of the proposals for modification of the current statutory and regulatory framework have come from parties that operate in smaller markets. In reviewing these proposals, it is important to consider their potential impact on large markets as well as smaller markets and to try to determine whether any changes should and could be limited to those markets where the current statutory and regulatory framework may be failing to safeguard the public against lost programming or higher prices. Also, it is important to note that the parties that have been proposing statutory or regulatory changes often cite the combined impact of multiple rules — for example, the impact of retransmission consent and program exclusivity rules in markets where a broadcaster owns multiple stations that are affiliated to two or more major broadcast networks. Would changing just one of the existing rules resolve alleged existing problems or create new ones? Would changing multiple rules represent overkill?

Specific Proposals to Modify Current Statutes and Regulations[49]

Most of the federal statutes and regulations affecting programmer-distributor negotiations were enacted before the recent structural market changes and, indeed, several were specifically intended to strengthen the negotiating position of broadcasters. Not surprisingly, then, most of the proposals to modify current statutes and regulations have come from small distributors that are now in a relatively weak negotiating position. These proposals include:

- revising the retransmission consent, network non-duplication, and syndicated exclusivity rules to allow MVPDs to import distant signals when a retransmission consent impasse develops.

- requiring broadcasters to publish rate cards that would apply to all MVPDs.

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[49] These proposals are discussed in detail in CRS Report RL34078, *Retransmission Consent and Other Federal Rules Affecting Programmer-Distributor Negotiations: Issues for Congress,* by Charles B. Goldfarb.

- requiring parties to submit to binding arbitration to resolve leased access, program carriage, or retransmission consent disputes.

- strengthening the FCC test for what constitutes "good faith" retransmission consent negotiations.

- prohibiting tying arrangements under which programmers require MVPDs to carry their less popular programming in order to obtain the rights to carry their more popular programming.

- requiring programmers to offer their broadcast and cable networks to distributors on an à la carte basis.

- prohibiting programmers from requiring their networks to be placed on the expanded basic service tier.

- prohibiting the ownership or control of more than one television station in a market or prohibiting a "duopoly" owner from tying retransmission consent for one station to another.

- not requiring MVPDs to get retransmission consent from broadcasters if their subscribers have set-top boxes on the customer premises that can pick up local broadcast station signals directly off the air.

- closing the "terrestrial loophole" exception to the requirement for nondiscriminatory access to programming in which a cable operator has an attributable interest.

- clarifying the definition of a regional sports network.