Testimony of Gene Kimmelman,
Senior Director for Advocacy and Public Policy,
Consumers Union

On behalf of
Consumers Union and the Consumer Federation of America

Before the
Senate Commerce, Science, and Transportation Committee

On

Cable Television and the Dangers of Deregulation

May 6, 2003

Washington Office
1666 Connecticut Avenue, N.W. Suite 310 • Washington, D.C. 20009-1039
(202) 462-6262 • fax (202) 265-9548 • http://www.consumersunion.org

SUMMARY

It began in 1984 with the Cable Communications and Policy Act, and a simple and appealing proposition: lift the shackles of regulation on the cable industry and competition will flourish, resulting in lower prices and more choices for consumers. It progressed to broadcast programming with the elimination of public interest programming obligations, and the decision to eliminate the limit on network ownership of prime time programming and culminated in the 1996 Telecommunications Act with the lifting of limits on broadcast station ownership. Consumers were told not to fear deregulation; competition and the antitrust laws would prevent excessive concentration.

Today, almost 20 years later, the evidence of failed promises is everywhere.

- The expected benefits of cable deregulation have not been realized. Robust competition did not materialize, the industry consolidated into a few dominant firms, and rates charged to consumers skyrocketed (see Table 1, p.15). Except during a four-year period in the early 1990's when Congress reregulated cable prices, rates have risen and continue to rise almost three-times faster than inflation. Since passage of the 1996 Telecommunications Act, cable rates have risen over 50%.[1]

- The broadcast networks, which once were limited to ownership of a quarter of prime time production, now own almost three quarters. Independent production has all but disappeared from the high volume viewing of prime time, both over-the-air and through the cable wire.

- Two of the largest national broadcasters have exceeded the cap set by Congress on the permissible number of stations they may own. Concentration in radio markets has advanced at a shocking pace.

Yet these facts have not weakened many policymakers' enthusiasm for allowing more deregulation and more mergers across all media industries and markets.

The recently announced proposed merger between the News Corporation ("News Corp./Fox") and Hughes Electronics Corporation's satellite television unit DIRECTV ("DirecTV"), combined with the Federal Communications Commission's (FCC) current efforts to relax or eliminate media ownership rules that restrict ownership of multiple television stations, newspapers and radio stations both locally and nationally, threaten to harm meaningful competition between media companies. Most importantly, this lack of competition will mean that control of media that Americans rely upon most for news, information and entertainment could eventually be placed in the hands of a few powerful media giants.

[1] Bureau of Labor Statistics, Consumer Price Index (March 2003). From 1996 until March 2003, CPI increased 19.3% while cable prices rose 50.3%, 2.6 times faster than inflation.

Consider the powerful interaction of the FCC's rush to lift media ownership rules and the proposed merger between a major network and the largest direct broadcast satellite (DBS) network. In the next month, the FCC is likely to relax ownership rules in a manner that would open the door to further concentration of ownership in a few hands, consolidation of outlets in national chains and conglomeration of control over different types of media. The FCC is considering:

- Relaxing the ban on news/broadcast cross-ownership would allow broadcasters to buy newspapers in the same communities they own local stations (even when there is only one dominant newspaper in that community). News Corp./Fox already has cross ownership ventures.

- Raising or eliminating the cap on how many television stations national TV networks may own (which was set at a level of stations servicing 35% of the population by Congress in 1996) would extend national network control over local stations. News Corp./Fox already far exceeds the cap.

- Letting a single TV broadcaster own more than 2 stations in a single market. News Corp./Fox already owns 2 broadcast stations in New York, Los Angeles, Dallas, Washington, D.C., Houston, Minneapolis, Phoenix, and Orlando.

- Although less likely, permitting national TV networks to buy each other (e.g., Fox purchase NBC or Viacom/CBS purchase Disney/ABC).

Unfortunately, the antitrust laws are not enough to prevent the excessive consolidation in the marketplace of ideas that would result from any combination of transactions under these relaxed rules. Antitrust has never been used effectively to promote competition in and across media where there is no clear way – like advertising prices -- of measuring competition/ diversity in news sources, information and points of view presented through the media.

Consumers Union[2] and the Consumer Federation of America[3] believe Congress should review and alter the laws that enabled industry consolidation spurred by excessive deregulation to weaken or undermine competitive conditions in media markets. The News Corp./DirecTV merger is likely to lead to higher prices for both satellite TV and cable TV, since the combined company can maximize its earnings by inflating the prices it charges for its broad array of popular programming that all cable and satellite customers purchase. And this transaction, in

---

[2] 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 4 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.

[3] 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 an cooperative organizations, with more than 50 million individual members.

conjunction with relaxed media ownership rules, will spur a wave of mergers among the remaining national broadcast networks, satellite and cable giants.

We believe it is time for Congress to intervene and finally deliver more choices and lower prices for the media services consumers want, and to prevent excessive relaxation of media ownership which threatens the critical watchdog function media companies play in our nation's democracy. It is time for Congress to drop the rhetoric and look at the reality of deregulated video markets. Congress should:

- Reconsider its grant of retransmission rights to broadcasters, where a broadcaster also owns a second means of video distribution.
- Let consumers pick the TV channels they want for a fair price.
- Prevent all forms of discrimination by those who control digital TV distribution systems and those who control the most popular programming in a manner which prevents competition in the video marketplace.
- Strengthen, rather than weaken, media ownership rules, to prevent companies from owning the most popular sources of news and information in both the local and the national markets.

THE NEWS CORPORATION/DIRECTV MERGER

If competition in the multichannel video market had performed up to its hope and hype, the NewsCorp./Fox/DirecTV merger might not be so threatening. But in light of the failure of deregulation, it presents a problem for public policy that cannot be ignored. There are two points of power in the marketplace – distribution and program production. The problem with News Corp./Fox is that it combines the two.

The reach of News Corp./Fox's media empire is truly staggering. The following are highlights of some News Corp./Fox properties in the U.S.:

- Broadcast Television Stations (35 stations, including two broadcast stations in New York, Los Angeles, Dallas, Washington DC, Houston, Minneapolis, Phoenix and Orlando)
- Filmed Entertainment (20th Century Fox Film Corp., Fox 2000 Pictures, Fox Searchlight Pictures, Fox Music, 20th Century Fox Home Entertainment, Fox Interactive, 20th Century Fox Television, Fox Television Studios, 20th Television, Regency Television and Blue Sky Studios)
- Cable Network Programming (Fox News Channel—the most watched cable news channel, Fox Kids Channel, FX, Fox Movie Channel, Fox Sports Networks, Fox Regional Sports Networks, Fox Sports World, Speed Channel, Golf Channel, Fox Pan American Sports, National Geographic Channel, and the Heath Network)

- Publishing (New York Post, the Weekly Standard, HarperCollins Publishers, Regan Books, Amistad Press, William Morrow & Co., Avon Books, and Gemstar – TV Guide International)

- Sports Teams and Stadiums (Los Angeles Dodgers, and partial ownership in the New York Knicks, New York Rangers, LA Kings, LA Lakers, Dodger Stadium, Staples Center, and Madison Square Garden)

News Corp./Fox's merger with DirecTV adds a new, nationwide television distribution system to News Corp./Fox's programming/production arsenal. DirecTV is the nation's largest satellite television distribution system, with more than 11 million customers and the ability to serve all communities in the United States.

News Corp./Fox's vast holdings provide it with leverage in several ways. "The biggest, most powerful weapon News Corp./Fox has is 'a four-way leverage against cable operators, competing with satellite and using the requirement that cable get retransmission consent to carry Fox-owned TV stations, while potentially leveraging price for Fox-owned regional sports networks and its national cable and broadcast networks. . .'"[4]

One of News Corp./Fox's most important weapons is significant control over regional and national sports programming. Mr. Murdoch often describes sports programming as his "battering ram"[5] to attack pay television markets around the world. As David D. Kirkpatrick noted in an April 14, 2003 *New York Times* article regarding Mr. Murdoch's control over sports programming:

> In the United States, News Corp./Fox's Entertainment subsidiary now also controls the national broadcast rights to Major League Baseball, half the Nascar racing season and every third Super Bowl. On cable, Fox controls the regional rights to 67 of 80 teams in the basketball, hockey and baseball leagues as well as several major packages of college basketball and football games, which it broadcasts on more than 20 Fox regional sports cable networks around the country. By acquiring DirecTV, Mr. Murdoch gains the exclusive right to broadcast the entire slate of Sunday NFL games as well.
>
> With DirecTV, Mr. Murdoch can start a new channel with immediate access to its subscribers, currently 11 million. He has other leverage in Fox News, now the most popular cable news channel, and essential local stations in most major markets around the country.[6]

It is important to consider the ramifications of Mr. Murdoch's control of over 40% of Fox broadcast stations nationwide, control of 11.2 million satellite subscribers, and his stranglehold

[4] Diane Mermigas, *"News Corp.'s DirecTV Monolith."* Mermigas on Media Newsletter, (Apr. 16, 2003), quoting Tom Wolzien, a Sanford Bernstein Media Analyst.
[5] David D. Kirkpatrick, *"Murdoch's First Step: Make Sports Fans Pay."* The New York Times, Apr. 14, 2003.
[6] Id., Emphasis added.

over regional sports programming. With those extensive holdings, News Corp./Fox is in a position to determine what new programming comes to market, and to undercut competitive programming. The company will be able to decide what programming it does not want to carry and may be able to indirectly pressure cable operators (by offering a lower price for Fox programming as an inducement) not to carry programming that competes with Fox offerings. We believe Mr. Murdoch has a right as an owner to put whatever he wants on his system, but with the FCC moving to relax media ownership rules, companies like News Corp./Fox will have the ability to control key sources of news and information in an unprecedented manner.

The merger between News Corp./Fox and DirecTV is extremely unlikely to stop skyrocketing cable rates and could very well exacerbate the problem. According to David Kirkpatrick's *New York Times* article:[7]

> some analysts said the structure of the deal suggested Mr. Murdoch hoped to use DirecTV mainly to punish other pay television companies and benefit his programming businesses. The Fox Entertainment Group, an 80 percent-owned subsidiary of News Corporation, will own a 34 percent stake in DirecTV's parent, creating the potential for programming deals that favor Fox over DirecTV.
>
> 'My sense is that the major purpose for News Corporation controlling DirecTV is to use it as a tactical weapon against the cable companies to get them to pay up for its proprietary programming,' said Robert Kaimowitz, chief executive of the investment fund Bull Path Capital Management.

While News Corp./Fox has agreed to abide by the FCC's program access requirements,[8] this pledge could end up being nothing more than a tool for pumping up cable prices. That is, while News Corp./Fox agrees to make its programming available on non-discriminatory terms and conditions, there is absolutely nothing that would prevent News Corp./Fox from raising the price that it charges itself on its satellite system, in return for increased revenues from the other 70 million cable households. If a cable system refuses to pay the increased price, then News Corp./Fox will be able to threaten cable operators to use its newly acquired satellite system to capture market share away from cable in those communities.

An article in the *Washington Post*[9] recently detailed the way this might work:

> For instance, News Corp./Fox raised the cost of his Fox Sports content to some cable systems by more than 30 percent this year, according to one cable operator.

---

[7] David Kirkpatrick, *"By Acquiring DirecTV, Murdoch Gets Upper Hand."* The New York Times, Apr. 10, 2003.

[8] "As part of the acquisition, News Corp. and DIRECTV has agreed to abide by FCC program access regulations, for as long as those regulations are in place and for as long as News Corp. and Fox hold an interest in DIRECTV, as if News Corp. and its subsidiaries were vertically integrated programming vendors. Specifically, News Corp. will continue to make all of its national and regional programming available to all multi-channel distributors on a non-exclusive basis and on non-discriminatory prices, terms and conditions. Neither News Corp. nor DIRECTV will discriminate against unaffiliated programming services with respect to the price, terms or conditions of carriage on the DIRECTV platform." Fox Entertainment Group Press Release, *"News Corporation Agrees to Obtain 34% of Hughes Electronics for $6.6 billion in Cash and Stock."* (Apr. 9, 2003), http://www.newscorp.com/feg/fegpress/feg_181.html.

[9] Frank Ahrens, *Murdoch's DirecTV Deal Scares Rivals."* Washington Post, Apr. 11, 2003.

> Like most officials interviewed yesterday, he refused to be identified, saying he had to continue dealing with News Corp./Fox.
>
> Most recently, in Florida, News Corp./Fox pulled its Fox Sports regional sports programming off of competitor Time Warner Cable's system over a rate dispute. News Corp./Fox wanted to charge more than Time Warner was willing to pay, but the conflict was resolved and service restored. "If this happens when Rupert owns DirecTV, you can assume DirecTV will go into the market and just pound away at the cable system," said one cable channel executive.

And price is only the beginning of the problems in this industry. Even in the 500-channel cable universe, control of prime time programming rests in the hands of a very few media companies. Given the enormous power that will be concentrated in News Corp./Fox as a result of the DirecTV transaction, not only will the combined entity be able to insist on top dollar for its programming, it will be able to determine who makes it and who fails in the programming marketplace.

CABLE RATES HAVE ESCALATED

In 1984, proponents of cable deregulation argued that competition from broadcasters and hoped-for sources like satellite television would keep prices down for consumers. The actual result? Massive consolidation and skyrocketing rates. In response, Senators Danforth, Gorton, Inouye and others led the charge in the early 1990s to clamp down on some of the most egregious excesses resulting from cable deregulation. However, in the 1996 Telecommunications Act, Congress went in the opposite direction, deregulating cable when the industry promised that it would become an aggressive competitor to local phone companies, and new competitors were entering the cable market.

But the cable industry has failed to deliver on its promises to Congress, regulators and the American people. Despite the growth of satellite TV, the promise of meaningful competition to cable TV monopolies remains unfulfilled. Cable rates are up 50% since Congress passed the 1996 Telecommunications Act, nearly three times as fast as inflation.[10]

In response to constant consumer complaints regarding the ever-escalating cost of cable service, cable providers explain that their hands are tied due to price increases from programmers and capital investments required to make new services available. The simple truth is that cable operators have been showing burgeoning profits to Wall Street, which runs at odds with what they have told their customers and policymakers.

If programming costs were really the sole cause of rising prices, then the cable industry's operating margins—the difference when costs are subtracted from revenues—would not be

[10] Bureau of Labor Statistics, Consumer Price Index (March 2003). From 1996 until March 2003, CPI increased 19.3% while cable prices rose 50.3%, 2.6 times faster than inflation.

rising. But the facts are just the opposite. The operating margin for the industry as a whole was projected to reach $18.8 billion per year in 2002, $7 billion more than it was in 1997.[11]

Operating revenues per subscriber have also increased dramatically over that period, from $208 per year to $273. That is, after taking out all the operating costs, including programming costs, cable operators have increased their take per subscriber by over 30 percent.

The increase in operating revenue is just under $5.50 per month. Basic rate increases over this period were about $8.50 per month. In other words, almost two thirds of the basic rate increases have been taken below the (operating cost) line. To put this another way, each $1 per month price increase raises industry revenues by about $800 million per year. Basic rate increases are driving the increased operating cash flow of the industry.

The fact that cable operators carry the basic rate increases directly to the bottom line underscores a second important point about the industry. The digital upgrade essentially pays for itself though the sale of digital tiers and high speed Internet to tens of millions cable subscribers.

The ability of cable operators to raise rates and increase revenues, even with rising programming costs, stems from the market power they have at the point of sale. They would not be able to raise prices and pass program price increases through but for that monopoly power.

COMPETITION TO CABLE NOT ROBUST

Head-to-head competition between cable companies is virtually non-existent. Out of 3000 plus cable systems, head-to-head competition exists in fewer than 200, although another 150 have certified entry. In short, only about 10 percent of franchise territories have experienced head-to-head competition between cable companies. While a number of other communities have authorized additional overbuilding, this activity is slowing, as the regional bell operating companies pull back and pure overbuilders retrench.[12]

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 and one-half 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.

This monopoly 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, up by almost 75 percent.[13] Just over one-half of all subscribers were

---

[11] Federal Communications Commission, *Ninth Annual Report, In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, MB docket No. 02-145 (Dec. 31, 2002).
[12] Federal Communication Commission,2001b,p. 20, notes that cable operators in only 330 communities have been granted status as effectively competitive on the basis of overbuilding.
[13] Federal Communications Commission, 2002b, Table C-1.

clustered in 1997 but by 2000 four-fifths were.[14] The FCC has found that clustering is associated with higher prices.[15]

The failure of competition in multichannel video is most evident in local markets. Only one cable company serves over 95 percent of the homes passed in the country.[16] Satellite has about 10 million subscribers in markets where cable and satellite meet. In these markets, there are only 8 million satellite only subscribers. This suggests that cable retains a market share at the point of sale of well over 85 percent.[17] The antitrust concentration index (the Hirschmann-Herfindahl index or HHI) at the local level is above 7000. These market shares and levels of concentration make cable operators virtual monopolies.[18]

The wave of concentration in the industry after deregulation is striking at the national level. When cable was deregulated in 1984, the distribution segment was not concentrated at all (HHI about 350), with the equivalent of about 30 equal sized competitors. A decade later, concentration had advanced to the point where the distribution segment had the equivalent of about 11 equal-sized competitors (HHI about 930). This is just close to the moderately concentrated threshold. Although the FCC claims that the Multichannel Video Program Distribution (MVPD) market falls just below the level of being moderately concentrated (HHI = 954), it arrives at this conclusion by ignoring Comcast's substantial direct ownership interests in Time Warner Systems and Cablevision, as well as its stake in Time Warner Entertainment (TWE). Taking Comcast's ownership interests into account places the cable TV market into the moderately concentrated category.

Satellite competition has failed to prevent price increases on cable because cable and satellite occupy somewhat different product spaces. First and foremost, the lack of local channels on satellite systems in many communities prevents satellite from being a substitute for cable; in fact, many satellite subscribers also purchase cable service for the express purpose of receiving local channels. And while many larger communities now receive local broadcast channels from satellite, service is not as attractive as cable in several respects and many consumers simply cannot subscribe. Many urban consumers cannot receive satellite services because of line of sight problems, or because they live in a multi-tenant dwelling unit where only one side of the building faces south.

Restrictions on multiple TV set hookups also make satellite more costly. The most recent data on the average price for monthly satellite service indicates that consumers pay between $44 and $80 a month to receive programming comparable to basic cable programming. This monthly fee often includes two separate charges above the monthly fee for basic satellite programming – one fee to hook a receiver up to more than one television in the household, and another fee so consumers are able to receive their local broadcast channels.

[14] Kagan, 1998.
[15] Federal Communications Commission, 2002b, p. 31.
[16] Federal Communications Commission, 2002b, p. 20.
[17] Federal Communications Commission, 2001b, p.34, notes increasing urban subscribers, but figure show that satellite is still disproportionately rural.
[18] Rosston and Shelanski, 2002, p. 23, give a hypothetical local market with a cable firm having an 80 percent market share and satellite having 20 percent in making a point about the impact of concentration in national markets. They never discuss the local HHI, which would be 6800. This meets the antitrust definition of a monopoly.

Satellite customers often subscribe to receive high-end services not provided (until the recent advent of digital cable) on cable systems, such as high-end sports packages, out of region programming, and foreign language channels. In essence, it is an expensive – but valuable -- product for consumers that want to receive hundreds of channels.

If satellite were a close substitute for cable, one would expect that it would have a large effect on cable. In fact, the FCC's own findings and data have contradicted the cable industry claims for years. The FCC found that satellite only "exerts a small (shown by the small magnitude of DBS coefficient) but statistically significant influence on the demand for cable service."[19] In the same econometric estimation, the FCC concluded that the "the demand for cable service is somewhat price elastic (i.e. has a price elasticity of minus 1.45) and suggests that there are substitutes for cable."[20] This elasticity is not very large and the FCC recognizes that in using the adjective "somewhat." The FCC also attempted to estimate a price effect between satellite and cable. If cable and satellite were close substitutes providing stiff competition, one would also expect to see a price effect. Most discussions of in economics texts state that substitutes exhibit a positive cross elasticity.[21] The FCC can find none. In fact, it found quite the opposite. The higher the penetration of satellite, the higher the price of cable.[22]

The most recent annual report on cable prices shows that the presence of DBS has no statistically significant or substantial effect on cable prices, penetration or quality.[23] This is true when measured as the level of penetration of satellite across all cable systems, or when isolating only areas where satellite has achieved a relatively high penetration.[24] At the same time, ownership of multiple systems by a single entity, large size and clustering of cable systems

---

[19] Report on Cable Industry Prices, February 14, 2002, p. 36.
[20] Report on Cable Industry Prices, February 14, 2001, p. 36.
[21] Pearce, George, The Dictionary of Modern Economics (MIT Press, Cambridge, 1984), p. 94. Cross Elasticity of Demand. The responsiveness of quantity demanded of one good to a change in the price of another good. Where goods i and j are substitutes the cross elasticity will be positive-i.e. a fall in the price of good j will result in a fall in the demand for good i as j is substituted for i. If the goods are complements the cross elasticity will be negative. Where i and j are not related, the cross elasticity will be zero. Taylor, John, B., Economics (Houghton Mifflin, Boston, 1998), p. 59.

A sharp decrease in the price of motor scooters or rollerblades will decrease the demand for bicycles. Why? Because buying these related goods becomes relatively more attractive than buying bicycles. Motor scooters or rollerblades are examples of substitutes for bicycles. A substitute is a good that provides some of the same uses or enjoyment as another good. Butter and margarine are substitutes. In general, the demand for a good will increase if the price of a substitute for the good rises, and the demand for a good will decrease if the price of a substitute falls.

Bannock, Graham, R.E. Banock and Evan Davis, Dictionary of Economics (Penguin, London, 1987).

Substitutes. Products that at least partly satisfy the same needs of consumers. Products are defined as substitutes in terms of cross-price effects between them. If, when the price of records goes up, sales of compact discs rise, compact discs are said to be a substitute for records, because consumers can to some extent satisfy the need served by records with compact discs. This account is complicated by the fact that, when the price of an item changes, it affects both the REAL INCOME 01 consumers and the relative prices of different commodities. Strictly, one product is a substitute for another if it enjoys increased demand when the other's prices rises and the consumer's income is raised just enough to compensate for the drop in living standards caused (pp. 390-391).

Cross-price elasticity of demand. The proportionate change in the quantity demanded of one good divided by the proportionate change in the price of another good. If the two goods are SUBSTITUTES (e.g. butter and margarine), this ELASTICITY is positive. For instance, if the price of margarine increases, the demand for butter will increase (p. 99).

[22] Report on Cable Prices, p. 11.
[23] Federal Communications Commission, 2002b.
[24] Federal Communications Commission, 2001b, describes the DBS variable as the level of subscription. Federal Communications Commission, 2002b, uses the DBS dummy variable.

results in higher prices.[25] Vertical integration with programming results in fewer channels being offered (which restricts competition for affiliated programs).[26]

In other words, one could not imagine a more negative finding for intermodal competition or industry competition from the FCC's own data. All of the concerns expressed about concentrated, vertically integrated distribution networks are observed and the presence of intermodal competition has little or no power to correct these problems. The claims that the cable industry makes about the benefits of clustering and large size – measured as price effects – are contradicted by the data. In fact, only intramodal, head-to-head competition appears to have the expected effects. The presence of wireline cable competitors lowers price and increases the quality of service.

While we hope that satellite will ultimately have a price disciplining effect in those communities where satellite offers local broadcast stations it is clear that the single most important variable in cable prices is whether there is a cable overbuilder in a particular community. Wire-to-wire competition does hold down cable rates and satellite does not seem to do the trick. The U.S. General Accounting office describes this phenomenon:

> Our model results do not indicate that the provision of local broadcast channels by DBS companies is associated with lower cable prices. In contrast, the presence of a second cable franchise (known as an overbuilder) does appear to constrain cable prices. In franchise areas with a second cable provider, cable prices are approximately 17 percent lower than in comparable areas without a second cable provider.[27]

In other words, where there are two satellite and one cable company in a market, prices are 17 percent higher than where there are two cable companies and two satellite providers in a market. If we had this type of competition nationwide, consumers could save more than $5 billion a year on their cable bills.

PROGRAM PRODUCTION

The failure of competition in the cable and satellite distribution market is matched by the failure of competition in the TV production market. In the 1980s, as channel capacity grew, there was enormous expansion and development of new content from numerous studios.

---

[25] The cluster variable was included in the Federal Communications Commission 2000a and 2001b Price reports. Its behavior contradicted the FCC theory. It has been dropped from the 2002 report. The MSO size was included in the 2002 report. System size has been included in all three reports.

[26] Vertical integration was included in Federal Communications Commission, 2002b.

[27] U.S. General Accounting Office, *Report to the Subcommittee on Antitrust, Competition, and Business and Consumer Rights, Committee on the Judiciary, U.S. Senate: Issues in Providing Cable and Satellite Television Services."* October 2002. In an important clarifying footnote, the report finds that:

> "This was a larger effect than that found by FCC in its 2002 *Report on Cable Industry Prices* (FCC 02-107). Using an econometric model, FCC found that cable prices were about 7 percent lower in franchise areas when there was an overbuilder. One possible explanation for the difference in results is that we conducted further analysis of the competitive status of franchises that were reported by FCC to have an overbuilder. We found several instances where overbuilding may not have existed although FCC reported the presence of an overbuilder, and we found a few cases where overbuilders appeared to exist although FCC had not reported them. We adjusted our measurement of overbuilder status accordingly.

Policymakers attributed the lack of concentration in the production industry to market forces and pushed for the elimination of the Financial Interest in Syndication rules (Fin-Syn) that limited network ownership and syndication rights over programming. The policymakers were wrong.

Following the elimination of the Fin-Syn rules in the early 1990s, the major networks have consolidated their hold over popular programming. The market no longer looks as promisingly competitive or diverse as it once did. Tom Wolzien, Senior Media Analyst for Bernstein Research, paints the picture vividly—he details the return of the "old programming oligopoly":

> Last season ABC, CBS and NBC split about 23% [of television ratings]. . . But if the viewing of all properties owned by the parent companies – Disney, NBC, and Viacom – is totaled, those companies now directly control television sets in over a third of the TV households. Add AOL, Fox and networks likely to see consolidation over the next few years (Discovery, A&E, EW Scripps, etc.), and five companies or fewer would control roughly the same percentage of TV households in prime time as the three net[work]s did 40 years ago. The programming oligopoly appears to be in a process of rebirth.[28]

In addition, the number of independent studios in existence has dwindled dramatically since the mid-1980s. In 1985, there were 25 independent television production studios; there was little drop-off in that number between 1985 and 1992. In 2002, however, only 5 independent television studios remained. In addition, in the ten-year period between 1992 and 2002, the number of prime time television hours per week produced by network studios increased over 200%, whereas the number of prime time television hours per week produced by independent studios decreased 63%.[29]

Diversity of production sources has "eroded to the point of near extinction. In 1992, only 15 percent of new series were produced for a network by a company it controlled. Last year, the percentage of shows produced by controlled companies more than quintupled to 77 percent. In 1992, 16 new series were produced independently of conglomerate control, last year there was one."[30]

The ease with which broadcasters blew away the independent programmers should sound a strong cautionary alarm for Congress. The alarm can only become louder when we look at the development of programming in the cable market. One simple message comes through: those with rights to distribution systems win.

Of the 26 top cable channels in subscribers' and prime time ratings, all but one of them (the Weather Channel) has ownership interest of either a cable MSO or a broadcast network. In other words, it appears that you must either own a wire or have transmission rights to be in the

[28] Tom Wolzien, *"Returning Oligopoly of Media Content Threatens Cable's Power."* The Long View, Bernstein Research (Feb. 7, 2003). Emphasis added.
[29] Coalition for Program Diversity, Jan. 28, 2003.
[30] Victoria Riskin, President of Writers Guild of America, West. *Remarks at FCC EnBanc Hearing, Richmond, VA* (Feb. 27, 2003).

top tier of cable networks. Four entities – AOL, Liberty/Fox, ABC/Disney and CBS/Viacom -- account for 20 of these channels.

Of the 39 new cable networks created since 1992, only 6 do not involve ownership by a cable operator or a national TV broadcaster. Sixteen of these networks have ownership by the top four programmers. Eight involve other MSOs and 10 involve other TV broadcasters. Similarly, a recent cable analysis identified eleven networks that have achieved substantial success since the passage of the 1992 Act. Every one of these is affiliated with an entity that has guaranteed carriage on cable systems.[31]

Moreover, each of the dominant programmers has guaranteed access to carriage on cable systems – either by ownership of the wires (cable operators) or by carriage rights conferred by Congress (broadcasters).

- AOL Time Warner has ownership in cable systems reaching over 12 million subscribers and cable networks with over 550 million subscribers.
- Liberty Media owns some cable systems and has rights on Comcast systems and owns cable networks with approximately 880 million subscribers. Liberty owns almost 20% of News Corp./Fox.
- Disney/ABC has must carry-retransmission rights and ownership in cable networks reaching almost 700 million subscribers.
- Viacom/CBS has must carry-retransmission rights and ownership in cable networks reaching approximately 625 million subscribers.
- Fox (has must carry-retransmission and ownership in cable networks reaching approximately 370 million subscribers and a substantial cross ownership interest with Liberty).

These five entities have ownership rights in 21 of the top 25 cable networks based on subscribers and prime time ratings. They account for over 60 percent of subscribers to cable networks, rendering this market a tight oligopoly. Other entities with ownership or carriage rights account for four of the five remaining most popular cable networks. The only network in the top 25 without such a connection is the Weather Channel. It certainly provides a great public service, but is hardly a hotbed for development of original programming or civic discourse. Entities with guaranteed access to distribution over cable account for 80 percent of the top networks and about 80 percent of all subscribers' viewing choices on cable systems.

When we examine the ownership of broadcast and cable networks, we discover that almost three-quarters of them are owned by six corporate entities.[32] The four major TV

[31] Federal Communications Commission, *Ninth Annual Report, In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, MB docket No. 02-145 (Dec. 31, 2002).
[32] One of the more ironic arguments offered by the cable operators feeds off of the observation that broadcast networks have carriage rights. They argue that even if cable operators foreclosed their channels to independent programmers, these

networks, NBC, CBS, ABC, Fox, and the two dominant cable providers, AOL Time Warner (which also owns a broadcast network) and Liberty (with an ownership and carriage relationship with Comcast and Fox), completely dominate the tuner. Moreover, these entities are thoroughly interconnected through joint ventures.

If distribution rights win then an entity like News Corp./Fox/DirecTV would create a powerhouse with guaranteed transmission rights on all three of the technologies used to distribute TV to the home. It will own broadcast stations, have must carry/retransmission rights on cable and satellite because of the broadcast licenses it holds, and own the largest satellite network. This is an immense power of distribution for a company that is vertically integrated into both broadcast and cable programming.

In the 1992 Cable Act, Congress recognized that the Federal government "has a substantial interest in having cable systems carry the signals of local commercial television stations because the carriage of such signals is necessary to serve the goals . . . of providing a fair, efficient, and equitable distribution of broadcast services."[33] Congress also recognized that "[t]here is a substantial government interest in promoting the continued availability of such free television programming, especially for viewers who are unable to afford other means of receiving programming."[34]

These governmental interests, as well as a finding that "[c]able television systems often are the single most efficient distribution system for television programming," formed the original rationale behind Retransmission Consent. Because a majority of the country was receiving broadcast television service through cable, it was necessary to require that cable systems carry local broadcast signals. However, a merger between News Corp./Fox and DirecTV would change the landscape against which Retransmission Consent was created. Given that this transaction will provide News Corp./Fox with assets that no local broadcaster had in 1992 when Retransmission Consent was originally put in place – it will have a satellite distribution system capable of reaching a majority of the country – it seems that the original logic behind the rule is strained in the present circumstances. Not only will News Corp./Fox own its own transmission system, but it also owns other programming that it bundles with its network programming, which may give it too much market power in negotiating cable and other carriage agreements. Congress should revisit the necessity of Retransmission Consent as it pertains to stations owned and operated by News Corp./Fox.

CONCLUSION

Consumers Union and Consumer Federation of America believe that Congress should step in and help consumers get a better deal from cable and other media companies.

---

programmers could sell to the broadcast networks. This ignores the fact that cable operators control the vast majority of video distribution capacity. There are approximately 60 channels per cable operator on a national average basis (Federal Communications Commission, 2002b, p. 10). There are approximately 8 broadcast stations per DMA on a national average basis (BIA Financial, 2002). Each broadcast station has must carry rights for one station. They can bargain for more, particularly in the digital space, but the cable operators control more stations there as well. In other words, if we foreclose 85 percent of the channels, the programmers will be able to compete to sell to the remaining 15 percent of the channels. Needless to say, this prospect does not excite independent programmers.

[33] Public Law 102-385, Section 2(a)(9).

[34] Public Law 102-385, Section 2(a)(12).

Congress should impose a new set of nondiscrimination requirements that would enable all media distributors and consumers to purchase video programming and related services on an individual – as opposed to bundled – basis under terms that maximize competition and choice in the marketplace. Congress must reexamine the enormous market power and leverage that Retransmission Consent provides broadcast programmers – particularly one like News Corp. which, as a result of the merger with DirecTV, will own a new nationwide video distribution system (in addition to its over-the-air broadcast distribution system). And Congress should require cable and satellite operators to offer consumers the right to select the channels they want to receive at a fair price – in other words, require an a la carte program offering from all video distributors. Since the average household watches only about a dozen channels of video programming, this requirement could empower consumers to help discipline excesses in cable (or satellite) pricing, and could possibly spur more competition.

Congress must also carefully consider all the ramifications associated with the rulemakings on media ownership. If media ownership limits are significantly relaxed or eliminated by the FCC then the News Corp./DirecTV deal may look almost harmless in comparison to an avalanche of media mergers that ensue. It is completely unfair to force American consumers to accept inflated cable rates and inadequate TV competition. But excess consolidation in the news media is even worse: the mass media provides Americans the information and news they need to participate fully in our democratic society. Without ownership rules that effectively limit consolidation in media markets, one company or individual in a town could control the most popular newspaper, TV and radio stations, and possibly even a cable system, giving it dominant influence and power over the content and slant of news. This could reduce the diversity of cultural and political discussion in that community.

The cost of deregulating media is very high. The cost of market failure in media markets is the price we pay when stories are *not* told, when sleazy business deals and bad accounting practices do *not* surface, when the watchdog decides that it would rather gnaw on the bone of softer news than chase down the more complicated realities that must be uncovered to make democracy function.

Cable Rates
Skyrocketing Except Under Regulation (1992 - 1996)