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# THE ECONOMICS OF RETRANSMISSION CONSENT

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March 2009

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## EXECUTIVE SUMMARY

Congress created retransmission consent in 1992 to ensure that broadcasters would be able to negotiate in a free marketplace for fair compensation for their programming.

Examining retransmission consent from an economic perspective, this study demonstrates that retransmission consent achieves Congress' intended purpose of establishing a market based mechanism to ensure that broadcasters receive an economically efficient level of compensation for the value of their signals. This compensation ultimately benefits consumers by enriching the quantity, diversity, and quality of available programming, including local broadcast signals.

In particular, the evidence demonstrates that:

- The market for television programming is highly competitive. The sellers' side of the video programming market (broadcasters) is relatively unconcentrated and is becoming less concentrated while the buyers' side (the multichannel video program distributors market) is experiencing consolidation at both the national and local levels. In 2006, the four MVPDs with the largest shares served 63 percent of all MVPD subscribers, up from 50 percent in 2002. National networks depend on just four purchasers to reach nearly 70 percent of all MVPD subscribers nationwide. Thus, broadcasters do not have monopoly power, and are not in a position to extract excessive retransmission consent fees from cable operators or other program distributors.

- Broadcasters are more vulnerable to economic losses, by losing viewers and advertising revenues, from retransmission consent disputes than are cable operators and other program distributors. An MVPD's refusal to carry a national network, or even the threat of a refusal, can significantly jeopardize that network's ability to operate efficiently, and in the worst case, could cause that network to fail.

- Overall, programming costs account for a small proportion of cable operators' revenues, and this proportion is falling. Cable operators' gross profits increased from $48.96 per subscriber per month in 2003 to $62.99 per subscriber per month in 2006, an increase of $14.03 or 29 percent. During that same period, programming expenses per subscriber per month increased from $15.63 to $18.47, an increase of $2.84 per subscriber per month or just 18 percent. Thus, cable operators' profits per subscriber rose by about five times as much as their programming expenses, or nearly twice as much in percentage terms.

- Retransmission consent fees simply cannot be responsible for any significant portion of cable operator's increasing monthly fees. For many years, cable operators refused to pay monetary compensation for retransmission consent. Some recent retransmission consent agreements, however, include monetary compensation. While such compensation is an important source of revenue for broadcasters, it is trivial when compared with cable operators' revenues and costs. Monetary retransmission consent fees are projected to increase by just $1.08 per subscriber per month in the next decade; during the same period, cable revenues per

subscriber will go up approximately 45 times as much, by $48.38. Retransmission consent fees account for only two tenths of one percent of cable revenues today, and industry analysts predict they will never rise above one percent.

- Concerns about negotiating impasses in retransmission consent negotiations are misplaced. Analysis demonstrates that an American household is about 10 times as likely to experience a complete cable system outage, and about 24 times as likely to experience an electricity outage, as it is to be deprived of its first-choice television channel because of a retransmission consent dispute.

Overall, retransmission consent represents an economically efficient regime that results in reasonable compensation for the value of broadcaster programming, and adoption of proposals to repeal or weaken the system would harm consumer welfare.

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## I. INTRODUCTION

Prior to 1992, cable operators were not required to compensate broadcast television stations for retransmitting local broadcast signals on their cable systems. In the Cable Television Consumer Protection Act of 1992 (Cable Act), Congress gave broadcasters the right to negotiate with cable systems for reasonable compensation ("retransmission consent"), or alternatively, to require cable systems to carry their signals on an uncompensated basis ("must carry"). Initially, cable operators refused to pay cash for broadcasters' signals, and broadcasters were forced either to opt for "must carry" or to accept in-kind compensation. More recently, broadcasters and cable systems have begun reaching retransmission consent agreements which include at least some cash compensation.

Cable operators, understandably, would prefer to return to the pre-1992 era, when broadcasters had no right to even negotiate for compensation. They raise various objections to the retransmission consent regime, arguing in essence that broadcasters have market power, that this market power allows broadcasters to extract unreasonably high compensation, and that this unreasonable compensation translates into higher retail prices for cable television service. These claims are most often heard during negotiations over the terms of retransmission consent, as cable operators seek to bring public pressure to bear on broadcasters to accept lower compensation.

This paper examines the performance of the retransmission consent regime from the perspective of economic efficiency and consumer welfare. The evidence shows that broadcasters do not have a negotiating advantage over program distributors (multichannel video programming distributors, referred to as MVPDs), and that retransmission consent has not led to excessive payments from cable operators to broadcasters in the past and will not lead to excessive

payments in the future. Rather, retransmission consent simply provides broadcasters with a means of obtaining an economically efficient level of compensation for their broadcast signals which, while important from the perspective of broadcasters, is inconsequential from the perspective of cable operators and their customers. Furthermore, both broadcasters and cable system operators have strong economic incentives to agree on terms of carriage. Hence, negotiating impasses are extremely rare and typically brief. The proportion of consumers affected by such impasses is infinitesimally small. In short, the current retransmission consent regime is an economically efficient, market-based approach to compensating broadcasters for the value of their signals.

The remainder of this paper is organized as follows. Section II provides a brief history of retransmission consent, including the 1992 Cable Act and the evolution of retransmission consent negotiations from "in kind" compensation towards monetary compensation for broadcast carriage. Section III explains the economics of retransmission consent negotiations, including specifically the relative bargaining power of broadcasters and cable operators as they seek to negotiate agreements. Section IV analyzes cable operators' claims about the connections between retransmission consent and subscription prices for consumers, and finds that compensation for retransmission consent has not in the past and will not in the future have a discernible impact on retail cable prices. Section V addresses concerns about the effect of carriage interruptions resulting from impasses in retransmission consent negotiations, and demonstrates that the impact on consumers of such impasses is negligible. Section VI presents a brief conclusion.

## II. THE HISTORY AND EVOLUTION OF RETRANSMISSION CONSENT

Congress created retransmission consent in 1992 to ensure that broadcasters would be able to negotiate in a free and competitive marketplace for fair compensation for retransmission and, in turn, resale of their broadcast signals. This section explains Congress' purpose in establishing retransmission consent, and summarizes the results of the retransmission consent regime since it was put in place 17 years ago.

### A. Before Retransmission Consent: The Pre-Cable Act Era

For nearly five decades, until passage of the Cable Act, cable systems were able to charge customers for viewing local broadcast signals without compensating the broadcasters – or even obtaining broadcasters' permission – for the right to retransmit the station's signal. At the same time, however, broadcast stations were prohibited from rebroadcasting or retransmitting another broadcast station's signal without consent.

Cable television in the U.S. dates to the late 1940s, when "community antennas" were erected on mountains and hills in rural communities in order to capture television broadcast signals and distribute them to local residents who could not receive clear signals using standard antennas. By 1962, there were nearly 800 cable systems serving approximately 850,000 subscribers.[1]

As cable grew from a purely "antenna" service to a full-fledged video competitor, the issue of compensation for retransmission of broadcast signals by cable operators became increasingly important. In 1959, based on its interpretation of Section 325 of the Communications Act (which the FCC determined banned *wireless* but not *wired* retransmission of broadcast signals), the FCC ruled that the Act did not require cable systems to obtain

1. *See* NCTA, *History of Cable* (available at www.ncta.com/About/About/HistoryofCableTelevision.aspx)

broadcasters' consent to retransmit their signals.[2] The FCC's decision stood until passage of the Cable Act in 1992.

On the other hand, the Commission grew increasingly concerned about the impact of the importation of out-of-market broadcast signals by cable operators on in-market broadcast stations. Thus, in 1963, the Commission conditioned the grant of a microwave license to a cable operator on the cable operator's agreement to carry the signal of the local broadcast station,[3] and it extended this "must carry" requirement to all cable operators in 1966.[4] In 1985, however, the courts invalidated the FCC's must-carry rules.[5] Thus, until must-carry was reinstated by the Cable Act (and, in 1997, upheld by the Supreme Court),[6] cable operators were not obligated to carry local broadcast stations on their systems (and many did not).[7]

On the copyright front, the Supreme Court ruled in 1968 (covering carriage of local broadcast signals) and 1974 (covering carriage of distant signals – i.e., carriage of broadcast signals originating outside the local market), that existing copyright laws did not require cable operators to compensate broadcasters for retransmitting their signals.[8] Thus, by the mid-1970s, cable operators were required to carry local stations, but neither the FCC nor copyright laws

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2. *See* Senate Report 109-92 (Cable Television Consumer Protection Act of 1992) citing 26 F.C.C. 403, 429-30 (1959).
3. *See Carter Mountain Transmission Corp v. FCC*, 321 F.2d 359 (1963).
4. *See* 2 F.C.C. 2d 725. See also 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* (hereafter "*SHVERA Report*") (Sep. 8, 2005) at ¶7.
5. *See SHVERA Report* at 4; see also *Quincy Cable TV, Inc. v. FCC*, 768 F.2d 1434 (D.C. Cir. 1985).
6. *See Turner Broadcasting System, Inc., et al. v. Federal Communications Commission, et al*. 520 U.S. 180 (1997).
7. *See Cable Television Consumer Protection and Competition Act of 1992* (S. Rep. No. 102-92, 102d Cong., 1st Sess., 1991; 1992 U.S.C.C.A.N. 1133) (hereafter *Senate Report*) at 1175-77.
8. *See*, e.g., Register of Copyrights, *Satellite Home Viewer Extension and Reauthorization Act, Section 109 Report* (June 30, 2008) (hereafter *Section 109 Report*) at 2 (citing *Fortnightly Corp. v. United Artists Television*, 392 U.S. 390 (1968) and *Teleprompter Corp. v. Columbia Broad. Sys., Inc.*, 415 U.S. 394 (1974)).

required them to compensate broadcasters or to compensate copyright holders of broadcast programming content.

The issue of copyright compensation for broadcast programming content was addressed by Congress in its 1976 rewrite of the Copyright Act. Congress determined in Section 111 of the 1976 Copyright Act that retransmission of the programming in broadcast signals – though limited by FCC regulations – would be subject to payment of copyright royalties under a statutory compulsory copyright license, but that retransmission of local broadcast signals did not require cable operators to pay a broadcast station for retransmitting the station's signals.[9]

Direct broadcast satellite (DBS) services emerged in the 1970s and 1980s. In 1988, in the Satellite Home Viewer Act, Congress permitted (and established a compulsory copyright license for) DBS operators to retransmit programming from distant, out-of-market broadcast network stations, but limited that right to serving otherwise *unserved* households, i.e., those without the ability to receive local broadcast signals.[10]

The situation in the late 1980s, then, was that cable operators were permitted to retransmit local broadcast programming, and broadcasters had no rights to even negotiate for compensation. Furthermore, after the repeal of the FCC's must-carry rules in 1985, neither cable nor DBS systems were required to carry broadcast programming on their systems. Thus, MVPDs could pick and choose the local broadcast stations of their choice, and restransmit and sell those signals to their subscribers without securing the consent of the stations.

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9. *See Section 109 Report* at 3-4. In 1972, the FCC imposed restrictions on distant signal carriage which effectively limited the ability of cable operators to import distant signals. Those rules were repealed by the FCC in 1980, and then reinstated in 1988. See *Section 109 Report* at 3-5 (citing Federal Communications Commission, *Cable Television Report and Order*, Docket No. 18397 (February 2, 1972) at ¶ 75; *Final Report and Order*, Dockets 20988 and 21284 (July 22, 1980); and, *Amendment of Parts 73 and 76 of the Commission's Rules Relating to Program Exclusivity in the Cable and Broadcast Industries*, 3 FCC Rcd 5299 (1988).

10. *See*, e.g., Section 109 Report at 83.

## B. The 1992 Cable Act

As cable grew rapidly in the late 1980s and early 1990s, Congress became concerned that it had tilted the competitive playing field too far in favor of cable and against broadcasters – indeed, that it had created a "distortion in the video marketplace that threaten[ed] the future of over-the-air broadcasting [by supporting] a system under which broadcasters in effect subsidize the establishment of their chief competitors."[11] It responded by passing the 1992 Cable Act,[12] which created the retransmission consent regime for carriage of local broadcast programming by cable operators and re-imposed must-carry obligations. Under the Cable Act, broadcasters must, every three years, choose between must carry and retransmission consent. If they choose must carry, they are guaranteed carriage on cable systems operating within their broadcast footprints, but receive no compensation; if they choose retransmission consent, they are not guaranteed carriage, but have the right to "negotiate in good faith" for compensation.[13]

In passing the Cable Act, Congress specifically recognized that the market for broadcast programming had changed dramatically. The Senate report accompanying the bill noted, for example, that when the FCC originally interpreted Section 325 of the Communications Act to allow free retransmission by cable (in 1959), "cable systems had few channels and were limited to an antenna function of improving reception of nearby broadcast signals," so that the FCC's

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11. *See Senate Report* at 1168.

12. Cable Television Consumer Protection Act of 1992, Pub. L. No. 102-385 (1992); the FCC's implementing regulations are at 47 C.F.R § 76.55-62 (cable must carry) and 47 C.F.R. § 76.64 (cable retransmission consent).

13. In passing the Cable Act, Congress recognized that satellite operators were treated differently from cable operators in the 1976 Copyright Act, and thus did not impose retransmission consent on DBS. It extended retransmission consent to DBS operators in 1999 in the Satellite Home Viewer Improvement Act (SHVIA), while at the same time permitting DBS operators to carry local broadcast signals even to households that were not "unserved." DBS operators are not subject to the must carry requirement. However, if they choose to carry any local broadcast stations, they are required to carry all stations that have elected must carry (the "carry one, carry all" rule). See *SHVERA Report* at ¶¶13-14. SHVIA was extended in 2004 by the Satellite Home Viewer Extension and Reauthorization Act of 2004, Pub. L. No. 108-447 (2004) (SHVERA); implementing regulations are at 47 C.F.R.

"interpretation had little practical consequences (*sic*) and did not unreasonably disrupt the rights that broadcasters possess in their signals."[14] However, the report continued,

> That situation… has changed dramatically. Cable systems now include not only local signals, but also distant broadcast signals and the programming of cable networks and premium services. Cable systems compete with broadcasters for national and local advertising revenues. Broadcast signals, particularly local broadcast signals, remain the most popular programming carried on cable systems, representing roughly two-thirds of the viewing time on the average cable system. It follows logically, therefore, that a very substantial portion of the fees which consumers pay to cable systems is attributable to the value they receive from watching broadcast signals. Due to the FCC's interpretation of section 325, however, cable systems use these signals without having to seek the permission of the originating broadcaster or having to compensate the broadcaster for the value its product creates for the cable operator.[15]

The effect of retransmission consent, the report concluded, would be to "establish a marketplace for the disposition of the rights to retransmit broadcast signals" without "dictat[ing] the outcome of the ensuing marketplace negotiations" – negotiations which, Congress recognized, might result in monetary compensation, in-kind compensation, or no compensation at all.[16]

In addition to creating retransmission consent, the Cable Act also reinstated the must-carry obligation. As with retransmission consent, its decision to do so was motivated by a sense that the competitive field had become tilted in favor of cable operators. Referring to the concerns that led Congress to embrace must-carry in the Cable Act of 1984, the Senate Report found that

> The subsequent demise of local television [after must-carry was overturned in 1985], the growth of the cable industry, and the fact that no

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§76.66. SHVERA also made several changes in the compulsory license regime affecting distant signal carriage by DBS operators. See *SHVERA Report* at ¶¶15-16).

14. *See Senate Report* at 1168.
15. *See Senate Report* at 1168.
16. *See Senate Report* at 1168-1169.

> effective competition to local cable systems has developed in the interim, have created just the competitive imbalance that the Committee feared in 1984.[17]

Thus, the Cable Act established a market-based mechanism for the determination of compensation for carriage of broadcast signals by MVPDs, based on voluntary agreements between broadcasters and operators, while at the same time (by re-imposing must carry) ensuring that cable operators and consumers would continue to have access to all broadcast channels.

### C. Retransmission Consent in Practice

Not surprisingly, cable operators opposed the retransmission consent and must carry provisions of the Cable Act. Once it passed, they generally refused to pay cash compensation for broadcast signals. Instead, they have negotiated some agreements with some broadcasters that provided no consideration and other agreements in which the broadcaster granted the MVPD permission to carry its signal in exchange for "in-kind" compensation (such as "free" advertising) or for an agreement that the cable operator would carry affiliated content (such as local news and weather channels, or affiliated cable networks). As the FCC explained in 2005,

> During the first round of retransmission consent negotiations, broadcasters initially sought cash compensation in return for retransmission consent. However, most cable operators – particularly the largest multiple system operators (MSOs) – were not willing to enter into agreements for cash, and instead sought to compensate broadcasters through the purchase of advertising time, cross-promotions, and carriage of affiliated channels. Many broadcasters were able to reach agreements that involved in kind compensation by affiliating with an existing non-broadcast network or by securing carriage of their own newly-formed non-broadcast networks. Broadcast stations that insisted on cash compensation were forced to either lose cable carriage or grant extensions allowing cable operators to carry their signals at no charge until negotiations were complete.[18]

Despite their success in fending off broadcasters' efforts to win monetary compensation, cable operators, sometimes joined by DBS operators, continued to argue that broadcasters had an

17. *See Senate Report* at 1187.

unfair advantage in negotiations and that retransmission consent should be weakened or repealed.[19] Perhaps not coincidentally, these arguments have tended to surface at times when policymakers were showing increasing concern about rising cable television rates.[20] To counter the resulting criticism, some cable operators argued (incorrectly, as shown below) that rising programming costs were to blame for rising cable prices, and retransmission consent was largely responsible for rising programming costs.[21]

In early 2000s, broadcasters began to negotiate retransmission consent agreements that included monetary compensation with DBS operators, telephone companies entering the video market, and ultimately cable operators.[22] One result was that cable and DBS operators redoubled their criticism of retransmission consent, warning that paying monetary compensation would force them to raise their prices even faster.[23]

Over the years, cable and DBS operators have put forward several proposals to weaken retransmission consent, including: (1) replacing the current obligation of broadcasters to "negotiate in good faith"[24] with binding arbitration; (2) allowing cable systems to import more duplicating broadcast signals from other (more distant) markets; (3) limiting broadcasters' ability

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18. *SHVERA Report* at ¶10.

19. See, e.g., *In the Matter of Inquiry on Rules Affecting Competition in the Television Marketplace* (Comments of Joint Cable Commenters) MB Docket No. 05-28 (March 1, 2005) at 6.

20. While one can reasonably debate the appropriate metric for measuring the price of cable television, it is indisputable that the monthly subscription rate for cable TV service increased faster than the rate of inflation throughout the 1990s.

21. *See*, e.g., Federal Communications Commission, *In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, MB Docket No. 06-189 (Comments of the Coalition For Retransmission Consent Reform) (Nov. 29, 2006), at 4-5 (hereafter Coalition Comments).

22. While retransmission consent agreements are confidential, it appears that the first significant one in which a cable operator agreed to pay monetary compensation to a broadcaster in exchange for the right to carry that broadcaster's signal was reached in 2005. *See* Craig Moffett et al, *U.S. Media: Cash for Retrans a Net Positive for TV Stations, But Full Financial Benefit Will Likely Require Patience*, Bernstein Research (Mar. 21, 2006), at 3. *See also* John Higgins, Cable, Broadcast Battles End, *Broadcasting & Cable* (Feb. 6, 2006); and *SHVERA Report* at ¶10.

23. See Coalition Comments at 6.

to negotiate cable carriage of affiliated cable networks and affiliated broadcast stations; and, (4) barring broadcasters from requesting cash-for-carriage.[25] The FCC has had multiple proceedings to examine such proposals, but at the end of the day has rejected them all.

Cable and DBS operators have also attempted to influence retransmission consent negotiations by filing complaints with the FCC claiming that broadcasters were failing to "negotiate in good faith." For example:

- In August 2001, the FCC ruled on a complaint filed by Echostar against Young Broadcasting alleging that Young failed to negotiate in good faith. The Commission denied the Echostar complaint, noting that the "back and forth" that had taken place between the parties was evidence of "precisely the judgment that Congress generally intended the parties to resolve through their own interactions and through the efforts of each to advance its own economic self-interest." Moreover, the Commission found that Echostar had abused the complaint process by systematically demanding confidentiality for various documents while selectively making portions of those documents available to the media.[26]

- In January 2005, Cox filed a complaint alleging that Nexstar Broadcasting Group and Mission Broadcasting were failing to negotiate in good faith in their efforts to win monetary compensation for their broadcast signals, but the dispute was settled before the FCC could rule on the complaint.[27]

- On January 4, 2007, the Commission issued an Order denying an October 2006 complaint by Mediacom against Sinclair Broadcasting for failing to negotiate in good faith over carriage of 13 Sinclair stations. The Order concluded that "This dispute, at bottom, arises from a fundamental disagreement between the parties over the appropriate valuation of Sinclair's signals. Such disagreements, without more, however, are not indicative of a lack of good faith. Even with good faith, impasse is possible."[28]

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24. The "good faith negotiation" obligation was codified by the FCC in 2000. *See* Federal Communications Commission, *Implementation of the Satellite Home Viewer Improvement Act of 1999: Retransmission Consent Issues,* 15 FCC Rcd 5445 (2000).

25. *See* e.g., Charles B. Goldfarb, *Retransmission Consent and Other Federal Rules Affecting Programmer-Distributor Negotiations: Issues for Congress* (Congressional Research Service, July 9, 2007) (hereafter, *CRS Report*); *SHVERA Report* at ¶¶39, 46.

26. *See* Federal Communications Commission, *In the Matter of EchoStar Satellite Corporation v. Young Broadcasting, Inc. et al, Memorandum Opinion and Order,* CSR-5655-C (August 6, 2001) at ¶¶14, 35.

27. *See CRS Report* at 31-32.

28. *See* Federal Communications Commission, *In the Matter of Mediacom Communications Corporation v. Sinclair Broadcast Group, Inc.: Emergency Retransmission Consent Complaint and Complaint for Enforcement for Failure to Negotiate Retransmission Consent Rights in Good Faith, Memorandum Opinion and Order*, CSR-7058-C (January 4, 2007) at ¶24.

Thus, despite the complaints of cable and DBS operators, the FCC has consistently refused to break with Congress' intention to allow compensation for broadcast carriage to be determined by good faith negotiations between the parties. No broadcaster has ever been found by the FCC to have breached its obligation to negotiate retransmission consent in good faith. In its 2005 report to Congress, the Commission concluded that the retransmission consent and must-carry provisions were achieving their intended goals.

> Together, must-carry and retransmission consent provide that all local stations are assured of carriage even if their audience is small, while also allowing more popular stations to seek compensation (cash or in-kind) for the audience their programming will attract for the cable or satellite operator. Must-carry alone would fail to provide stations with the opportunity to be compensated for their popular programming. Retransmission consent alone would not preserve local stations that have a smaller audience yet still offer free over-the-air programming and serve the public in their local areas.[29]

Despite the FCC's continued support for retransmission consent, it seems clear that cable and DBS operators will continue to seek its dilution or repeal. The sections below analyze the various arguments that have been advanced against retransmission consent and demonstrate from the consumer's perspective that these arguments are without merit.

## III. THE ECONOMICS OF RETRANSMISSION CONSENT NEGOTIATIONS

Proposals to weaken retransmission consent are premised at least in part on the assumption that broadcasters possess the power to impose uneconomic terms or supracompetitive prices on MVPDs. As this section explains, the evidence demonstrates otherwise. First, the evidence shows that the market for MVPD video programming (of which broadcast programming is a part) is far less concentrated and has lower barriers to entry than the market for video distribution (i.e., the market for cable television), which is more concentrated and for which barriers to entry are relatively high. Thus, cable operators possess greater market

power, overall, than broadcasters. Second, the evidence demonstrates that both broadcasters and cable operators have strong incentives to reach agreements, but that broadcasters likely suffer higher losses as a result of negotiating impasses than do cable operators. Thus, broadcasters have, if anything, less bargaining power in retransmission consent negotiations than do cable operators.

## A. Concentration and Market Power in the Video Programming and Video Distribution Markets

The outcomes of negotiations between broadcasters and MVPDs are a function of the bargaining power of each side. One way to think about bargaining power is in terms of the degree of monopoly power held by the upstream seller (the broadcaster) and monopsony power held by the downstream buyer (the MVPD). In a market with many sellers of perfectly interchangeable products, and a single buyer, all bargaining power rests with the buyer: The buyer will pay the competitive price for the product, and sellers will earn zero economic rents. Conversely, in a market with a single seller and many undifferentiated buyers, the seller will be able to charge the monopoly price, and (assuming entry is constrained) will earn positive economic rents.

The market for broadcast programming is neither a pure monopoly nor a pure monopsony. Rather, both broadcasters and MVPDs have a degree of market power, but for significantly different reasons: Broadcasters produce differentiated products, which by nature are associated with a degree of market (but not monopoly) power. MVPDs, on the other hand, possess monopsony power as a result of high concentration and barriers to entry.

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29. *SHVERA Report* at ¶33.

The evidence presented below shows that the market for programming is unconcentrated and barriers to entry are low, while the market for video distribution is concentrated and subject to substantial entry barriers. Moreover, trends in these two markets are towards increasing concentration in the market for distribution, and decreasing concentration in the market for programming. At the national level, the number of programming options is increasing while the distribution market is becoming more concentrated as a result of consolidation among cable operators. In local cable markets, mergers and "system swaps" have resulted in an increase in clustering – that is, markets in which a single cable operator serves all or most of the households in a broadcast viewing area. The increase in clustering has placed cable operators in a stronger bargaining position vis-à-vis broadcasters, who produce an inherently local product.[30]

### 1. The Market for Video Programming is Highly Competitive

Broadcast content is part of the larger market for television programming. Thus, broadcast networks compete directly with cable networks for viewing time and advertising dollars in local television advertising markets.[31] The evidence demonstrates that the market for television programming is highly competitive, with low levels of concentration and rapid entry.

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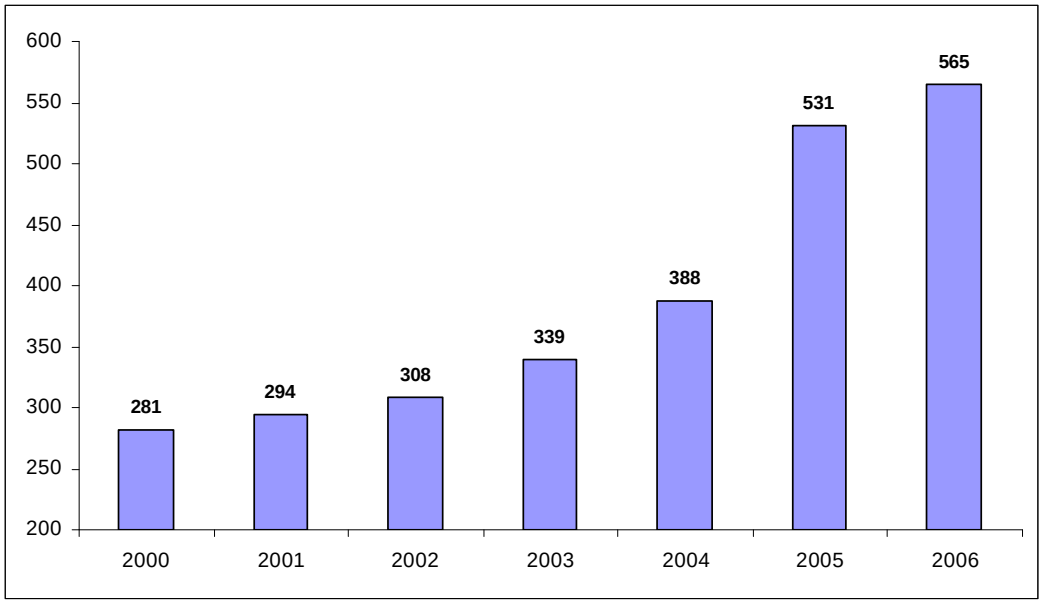
30. While broadcast programming is inherently local, retransmission negotiations often involve broadcasters who own stations in multiple markets (e.g., Fisher Communications) negotiating with MVPD operators who distribute programming in many of those same markets (e.g. Dish Network).

31. Both the FCC and the Department of Justice (DOJ) have embraced the existence of local advertising markets. See, e.g., *In re Applications of Pegasus Broadcasting, LLC, Transferor, and Chancellor Media Corporation of Los Angeles, Transferee*, adopted Aug. 11, 1999, ¶ 40, available at www.fcc.gov/Bureaus/Mass_Media/Orders/1999/fcc99218.wp; *In re Applications of NYNEX Corporation Transferor, and Bell Atlantic Corporation, Transferee, for Consent to Transfer Control of NYNEX Corporation and Its Subsidiaries*, File No. NSD-L-96-10, Memorandum Opinion & Order, adopted Aug. 14, 1997, at ¶ 55, available at http://www.fcc.gov/Bureaus/Common_Carrier/Orders/1997/fcc97286.txt; *In re Applications of Shareholders of Citicasters, Inc., Transferor, and Jacor Communications, Inc., Transferee*, Memorandum Opinion & Order, adopted Sep. 17, 1996, ¶ 10, available at http://www.fcc.gov/Bureaus/Mass_Media/Orders/1996/fcc96380.txt; Press Release, Department of Justice, *Abry Broadcast Partners Abandons Deal with Bastet Broadcasting*, July 16, 1999, available at http://www.usdoj.gov/atr/public/press_releases/1999/2565.pdf; Department of Justice, *Antitrust Division Merger Challenges, Meredith Corp./First Media Television, L. P.*, Sep. 16, 1998, available at http://www.usdoj.gov/atr/public/4523h.htm.

As shown in Figure 1 below, the FCC reports that there were 565 satellite-delivered national programming networks in 2006, that the number more than doubled between 2000 and 2006, and continues to increase. This evidence of rapid entry is inconsistent with the notion of market power for any incumbent programmers, broadcasters included.

FIGURE 1:
NUMBER OF NATIONAL SATELLITE-DELIVERED PROGRAMMING NETWORKS 2000-2006[32]




Competition authorities sometimes use measures of industry concentration as indicators of the potential for anticompetitive conduct. Table 1 below shows the prime-time audience share of the six leading producers of television programming, as reported by Bernstein Research. Four

32. *See* Federal Communications Commission, *In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, Thirteenth Annual Report, MB Docket No. 06-189 (Jan. 16, 2009); Federal Communications Commission at ¶20 [hereafter Thirteenth MVPD Report], *In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, Twelfth Annual Report, MB Docket No. 05-255 (Mar. 3, 2006) [hereafter Twelfth MVPD Report] , at ¶157; Federal Communications Commission, *In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, Eleventh Annual Report, MB Docket No. 04-227 (Feb. 4, 2005), at ¶145 [hereafter Eleventh MVPD Report]; Federal Communications Commission, *In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, Tenth Annual Report, MB Docket No. 03-172 (Jan. 28, 2004), at ¶17; Federal Communications Commission, *In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, Ninth Annual Report, MB Docket No. 02-145 (Dec. 31, 2002), at ¶13; Federal Communications Commission, *In the Matter of Annual Assessment of*

of the firms – CBS, Disney, NBC, and News Corporation – own broadcast stations; two – Time Warner and Viacom – do not.

The data show that the six-firm concentration ratio in the broadcast programming industry has remained stable over time, at approximately 70 percent. Moreover, the Herfindahl-Hirschman Index (HHI), the most commonly accepted measure of industry concentration, has decreased by nearly 100 points since 2000 – from 978 to 881.[33] The Department of Justice and the Federal Trade Commission classify markets where the HHI is below 1,000 as "unconcentrated," and find that mergers in such markets are "unlikely to have anticompetitive effects."[34]

TABLE 1:
PRIME TIME AUDIENCE SHARES (PERCENT) AND HERFINDAHL-HIRSCHMAN INDICES FOR THE SIX LEADING PRODUCERS OF TV PROGRAMMING (2000-2006)

| | **2000** | **2001** | **2002** | **2003** | **2004** | **2005** | **2006** |
|---|---|---|---|---|---|---|---|
| **Time Warner** | 14 | 13 | 14 | 13 | 12 | 11 | 11 |
| **News Corporation** | 8 | 9 | 8 | 12 | 10 | 10 | 10 |
| **NBC Universal** | 12 | 11 | 12 | 12 | 11 | 12 | 12 |
| **Disney** | 18 | 16 | 15 | 14 | 14 | 15 | 16 |
| **Viacom** | 5 | 6 | 7 | 6 | 7 | 8 | 8 |
| **CBS** | 15 | 16 | 15 | 14 | 13 | 14 | 14 |
| **Combined Share** | 72 | 71 | 71 | 71 | 67 | 70 | 71 |
| **HHI Index** | 978 | 919 | 903 | 885 | 779 | 850 | 881 |

*Source*: Share data from Nielsen Media Research and Wolzien LLC as reported in Michael Nathanson, et. al., *Big Thinking on Small Caps: As Primetime Content Distribution Expands, Will Local Broadcasters Go The Way of Your Local Record Store?* Bernstein Research (January 17, 2007), at Exhibit 1.

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*the Status of Competition in the Market for the Delivery of Video Programming*, Eighth Annual Report, CS Docket No. 01-129 (Jan. 14, 2002), at ¶13.

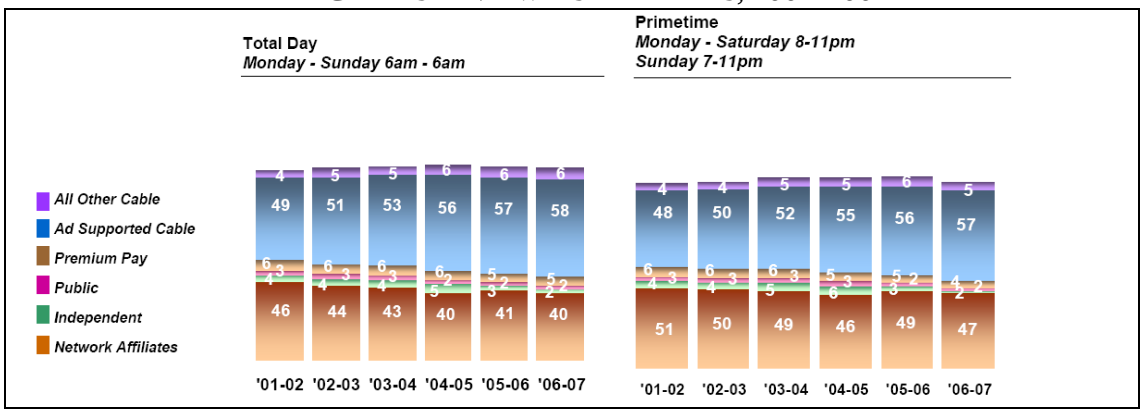
33. By ignoring the remaining firms in the market, this calculation understates the HHI, but only slightly. For example, if the remaining 29 percent of the market in 2006 were divided equally among 20 firms, the calculated HHI would increase by only 42 points, to 923, still well within the "unconcentrated" range. In fact, the remaining share is divided among many more than 20 firms.

34. See U.S. Department of Justice and U.S. Federal Trade Commission, Horizontal Merger Guidelines (1997) at 15-16.

These data demonstrate that the overall market for television programming is highly competitive, with low concentration, low or non-existent barriers to entry, and diverse ownership. In such a market, there is no basis for believing that *any* seller is in a position to command higher-than-competitive prices.

The data also demonstrate that broadcast programming is losing share to cable networks, and that the decline is expected to continue in the future. As shown in Figure 2, basic cable's share of the total day viewing audience surpassed that of the seven broadcast networks (ABC, CBS, NBC, FOX, WB, UPN and Pax) in the 2000-2001 viewing season, and its share of prime time viewing surpassed the networks two years later. The most recent data shows basic, ad supported cable programming holding a 58 percent share of total day viewing (compared with 42 percent for network and independent broadcasters combined) and a 57 percent share of primetime viewing (compared with a 49 percent share for broadcasters).[35] When premium channels and pay-per-view viewing is included, cable's share rises to 69 percent for total day, and 66 percent for prime time.

FIGURE 2:
AC NEILSEN VIEWERSHIP TRENDS, 2001-2007

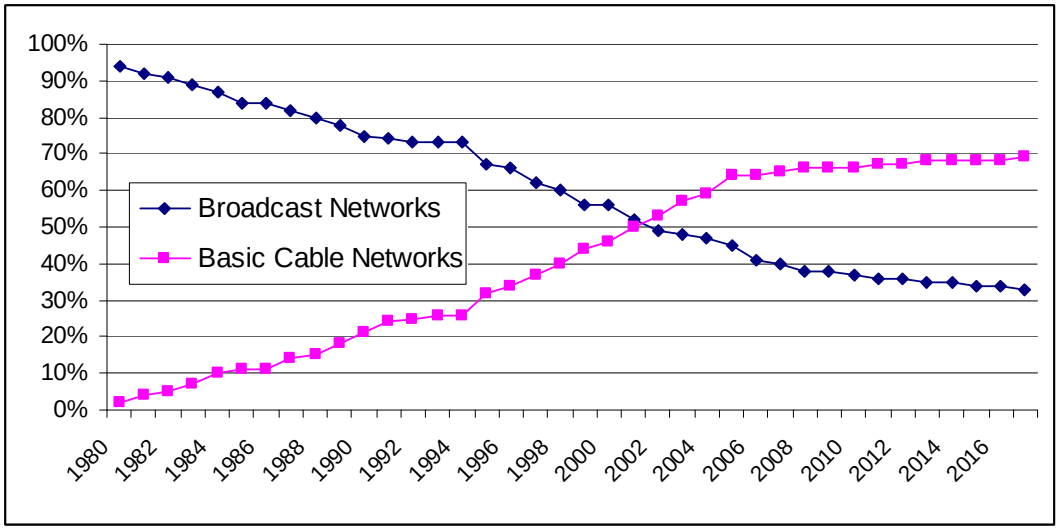



*Source: AC Nielsen Television Viewing Audience, 2007*

The shift in audience share from broadcast to cable is expected to continue into the future. Figure 3 shows SNL Kagan's projection for broadcast versus basic cable viewing shares through 2017.

Within the next decade, basic cable's share is projected to grow to nearly 70 percent, while broadcast networks – though they will continue to provide widely viewed content to large audiences – overall will command less than a third of the market in terms of overall viewing.

FIGURE 3:
ACTUAL AND PROJECTED BROADCAST VS. BASIC CABLE VIEWING SHARES
(1980-2017)




*Source: SNL Kagan, Cable Futurecast*

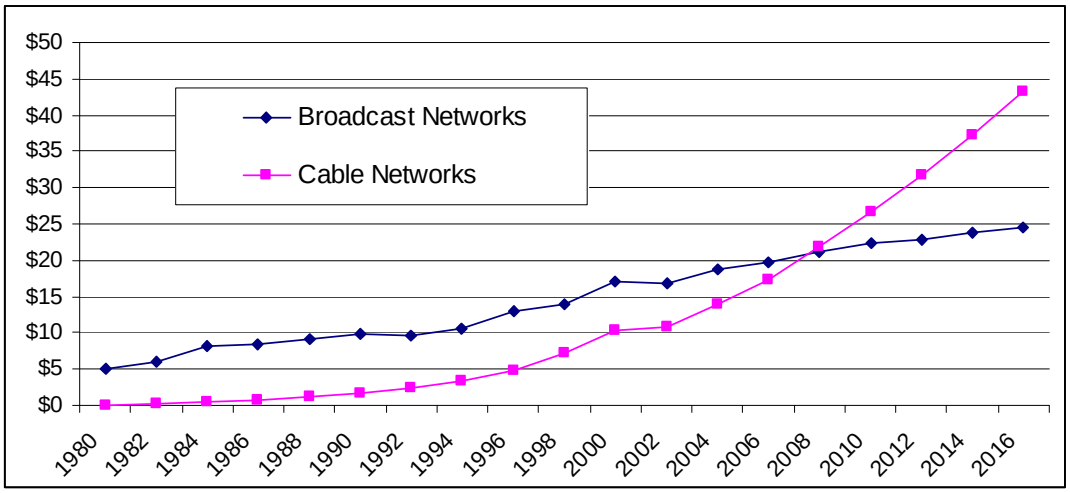
Ratings, of course, translate directly into revenues, and the revenue data also show the rise of cable programming. Figure 4 below shows the total revenues of broadcast and cable networks as reported by SNL Kagan. As the figure indicates, in 2008, for the first time, cable

35. Note: Nielsen ratings measure the proportion of households tuned to a particular channel at a particular time. Since households with multiple TVs may be tuned to multiple stations, the ratings to not necessarily sum to 100 percent.

network revenues exceeded broadcast network revenues, and the gap is expected to grow over time.

FIGURE 4:

ACTUAL AND PROJECTED TOTAL REVENUES,
BROADCAST NETWORKS VS. CABLE NETWORKS (1980-2016; $BILLIONS)




*Source: SNL Kagan, Cable Futurecast*

Taken together, the data above demonstrate two things: The market for television programming is highly competitive, with low concentration and rapid entry; and, the share of that market that is commanded by broadcast programming is low from the perspective of competition analysis – indeed, lower than in 1992 when Congress enacted retransmission consent due to its concern that the competitive playing field unduly favored cable. Broadcasters, simply put, do not have monopoly power.

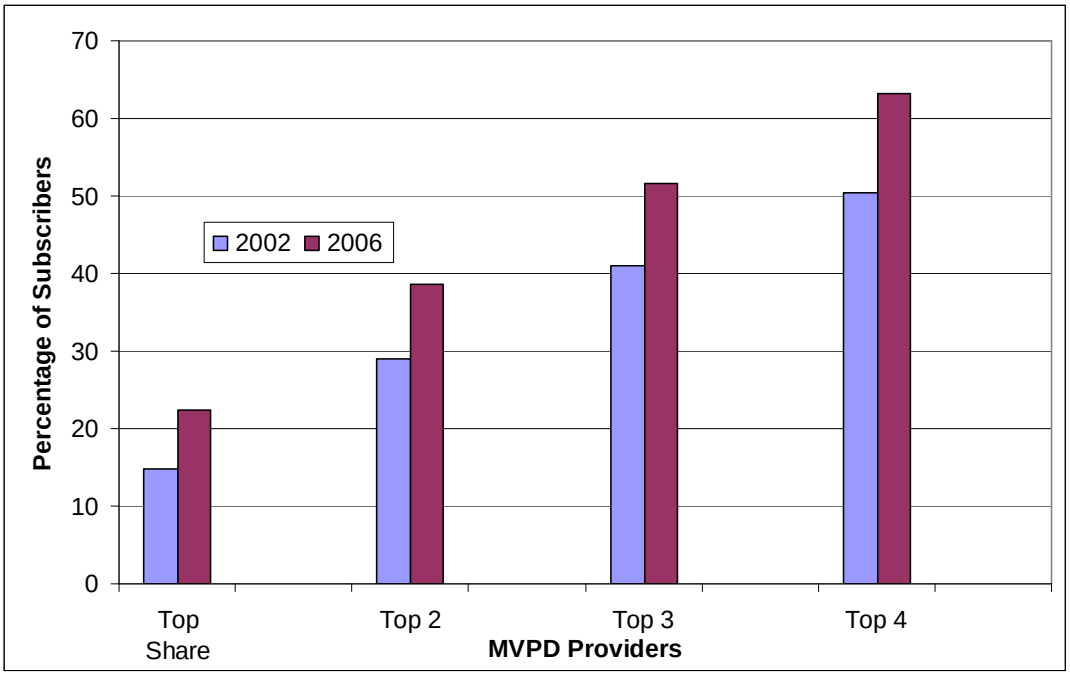
### 2. Concentration in the National MVPD Market Has Increased

While the sellers' side of the video programming market is unconcentrated and becoming less concentrated, the buyers' side – that is, the MVPD market – is experiencing consolidation at both the national and local levels.[36]

The national market for program distribution has seen significant consolidation in recent years as large cable acquisitions, including the acquisition of Adelphia by Comcast and Time Warner, have increased buyer concentration. As shown in Figure 5, in 2006, the four MVPDs with the largest shares served 63 percent of all MVPD subscribers, up from 50 percent in 2002.[37] When Adelphia's share is added to the shares of the top four, reflecting the acquisition of Adelphia by Comcast (#1) and Time Warner (#4), the top four MVPDs in 2006 served over 68 percent of the MVPD market – an increase of 18 percentage points from 2002. Thus, national networks depend on just four purchasers to reach nearly 70 percent of all MVPD subscribers nationwide. An MVPD's refusal to carry a national network, or even the threat of a refusal, can significantly jeopardize that network's ability to operate efficiently, and in the worst case, could cause that network to fail.

36. The consolidation among cable operators that is leading to higher concentration shows some signs of being offset by the entry of telephone companies, but concentration will remain high relative to the market for programming, as barriers to entry are substantial.

FIGURE 5:
INCREASE IN MARKET SHARE OF LARGEST MVPD PROVIDERS: 2002-2006




*Source: Thirteenth MVPD Report, at Appendix B, Table B-4; Twelfth MVPD Report, at Appendix B, Table B-4*

### 3. MVPD Concentration in Individual Local Markets Has Increased

Cable acquisitions have not only increased national buyer concentration ratios, which increases their bargaining power relative to national programming networks, they have also led to increased concentration in markets. But acquisitions are not the only means by which cable operators have increased local market shares: In recent years, they have engaged in large numbers of cable system "swaps," in which two multi-system operators (MSOs) trade cable systems in different geographic areas to build larger "clusters." Higher cable system concentration at the local level increases the bargaining power of cable systems relative to local programmers.

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37. Thirteenth MVPD Report at Tables B-3, B-4, Twelfth MVPD Report at Tables B-3, B4. The share of subscribers served by the top ten MVPDs has also increased, from approximately 84 percent in 2002 to 87 percent in 2006.

As reported by the FCC, clustering via system swaps has become increasingly common:

> Cable operators continue to pursue a regional strategy of 'clustering' their systems. Many of the largest MSOs have concentrated their operations by acquiring cable systems in regions where the MSO already has a significant presence, while giving up other holdings scattered across the country. This strategy is accomplished through purchases and sales of cable systems, or by system 'swapping' among MSOs.[38]

Data from SNL Kagan show the number of clusters with 500,000 or more subscribers rose from 29 systems in 2005, covering 29.8 million subscribers, to 43 in 2007, covering 38.1 million subscribers.[39] A cable operator's refusal to carry a local station (once that station has elected retransmission consent, and thus is not eligible for must carry) in a clustered area, or even the threat of a refusal, can significantly jeopardize that local station's ability to operate.

## B. Cable Operators Have Significant Advantages in Bi-Lateral Negotiations

In addition to the standard measures of market power presented above, the bargaining relationship between broadcasters and programming distributors can also be thought of in terms of each side's ability to bear the costs of a bargaining impasse. While cable operators complain that broadcasters have the upper hand, the evidence demonstrates otherwise.

As an initial matter, it is important to note that both broadcasters and MVPDs have very strong incentives to reach agreements, for two primary reasons: First, both industries are characterized by high fixed costs, meaning that any reduction in output (i.e., a reduction in the number of viewers/subscribers) is, in the short run, not matched by a decline in costs. Second, both industries' products are highly perishable, meaning that a product that is not sold at the time it is produced cannot simply be put in a warehouse to be sold later. Thus, if a negotiating impasse leads broadcasters to lose viewers (and hence advertising revenues), or cable companies

38. Eleventh MVPD Report at ¶141.

to lose subscribers, the loss of revenues translates directly into lost profits, and can never be made up. As the FCC has concluded, "the retransmission consent process provides 'incentives for *both* parties to come to mutually beneficial arrangements,'" and "the failure to resolve local broadcast carriage disputes through the retransmission consent process potentially is detrimental *to each side*."[40]

While both sides lose when a local broadcast signal is pulled from a cable operator's channel lineup, the evidence suggests that broadcasters lose more. When impasses occur, and broadcast stations are pulled from an MVPD's channel lineups, the primary cost to the MVPD is the potential loss of subscribers (who may either switch to another MVPD, such as from cable to DBS, or simply go back to over-the-air). The primary cost to a broadcaster, on the other hand, is the combination of lost compensation from the MVPD plus lost advertising revenues.

Most industry analysts believe the costs of impasses fall disproportionately on broadcasters. Bernstein Research, for example, concludes that retransmission negotiating leverage is "steeply asymmetrical" in favor of cable operators,[41] primarily because "subscribers leave distributors for competitors only slowly, while advertising revenues are lost right away."[42] Moreover, Bernstein explains, "negotiating leverage for retransmission consent is a function of local market share."[43] Thus,

> At the end of the day, if retrans[mission] negotiations reach an impasse, the TV station owners can choose to pull their signal from the cable system. However, financially this is profoundly damaging to the TV station's P[rofit] &L[oss] given

39. Data for 2007 data from SNL Kagan, Broadband Cable Financial Databook; 2005 data from SNL Kagan as reported in Thirteenth MVPD Report at Table B-2.

40. *SHVERA Report* at ¶44 (citing News-Hughes Order, 19 FCC Rcd at 556-7, ¶180) (emphasis added).

41. Bernstein Research, *Cable and Satellite: Asymmetrical "Retrans" Leverage Favors Cable over Satellite and Telcos*, Mar. 21, 2006 (hereafter *Bernstein Report*) at 1. See also Merrill Lynch, *Brief Thoughts on Media*, Mar. 16, 2006, at 2 ("We are simply not convinced that broadcasters have sufficient leverage over the MSO's to charge significant rates [for retransmission consent].").

42. *Bernstein Report* at 1.

43. *Bernstein Report* at 1.

> that its sole revenue stream is driven by viewers and given that cable MSOs account for an average of 60% of distribution and even higher in some markets (i.e., urban markets). Given the fixed cost nature of the TV station business model, the margin on this lost advertising revenue is nearly 100%.[44]

In summary, based on traditional measures of market concentration and entry, and on the specific economic characteristics of bilateral negotiations between broadcasters and MVPDs, there is simply no basis for claims that broadcasters have the ability to impose unreasonable retransmission consent terms on programming distributors. As shown in the section below, the evidence also demonstrates that the outcomes of actual negotiations have not resulted in excessive compensation and that the compensation that has been paid has little or no impact on cable company prices.

## IV. RETRANSMISSION CONSENT, PROGRAMMING COSTS AND RETAIL PRICES

One of cable operators' arguments against retransmission consent is that any compensation paid to broadcasters for their signals is ultimately passed along to consumers in the form of higher retail prices. At one level, this assertion is a truism, equivalent to saying that if steel were free, car companies could charge less for automobiles. The problem, of course, is that if the price of steel were set to zero, no steel would be produced, and there would be no cars in the first place. From an economic and consumer welfare perspective, the correct question is whether prices are set so as to send the right signals to both sellers and buyers. If the price is set too low, sellers will not produce the economically optimal quantity (or quality) of output, and consumer welfare will suffer.

The discussion above demonstrates as a *prima facie* matter that conditions in the market for programming are such that retransmission consent negotiations can be expected to yield prices that closely approximate the social optimum. Nevertheless, cable operators and other

44. *Bernstein Report* at 2.

MVPDs have continued to complain that retransmission consent compensation has "unreasonably" increased their programming costs and resulted in significantly higher prices to consumers. The evidence presented below demonstrates otherwise. First, during the period when cable operators refused to pay monetary compensation, and forced broadcasters instead to accept in-kind compensation (primarily in the form of carriage of affiliated programming), the evidence does not support cable operators' claims that resulting increases in programming costs had any significant effect on their overall costs structures or on the retail prices they charged consumers. Second, during the more recent period when broadcasters have begun to receive monetary compensation, the evidence shows that such compensation is extremely modest relative to cable operators' overall revenues, and is likely to remain so.

## A. In-Kind Compensation for Retransmission Consent Has Not Had an Appreciable Effect on Cable Costs or Rates

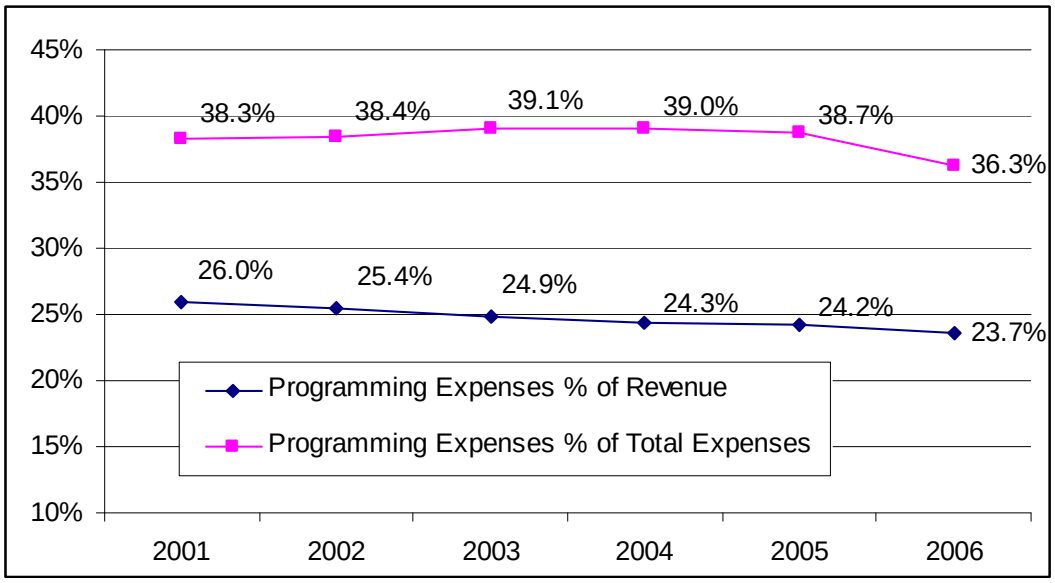
From 1992 through 2004, cable operators refused to pay monetary compensation for retransmission consent, preferring instead to compensate broadcasters, if at all, only in kind. Such compensation primarily took the form of agreeing to carry affiliated broadcast or cable programming. For example, a cable operator might agree to carry a local station's cable-only news and weather channels or to carry a small independent station owned by a broadcasting company in one market where the cable operator had a cable system in return for the right to carry a "big three" network-affiliated station in another market; or to carry a start-up cable network owned by a broadcasting company in return for the right to carry that company's broadcast stations. In either case, it is for practical purposes impossible to place a monetary value on these barter exchanges. It is possible, however, to examine the total costs cable operators paid for programming. As noted above, cable operators allege that retransmission

consent resulted in higher programming costs, and forced them, in turn, to raise prices charged to consumers.

The problem with the cable operators' argument is that programming costs have not risen in relative terms in recent years, even as cable prices have gone up significantly. Whether compared to other elements of cable company costs, to cable company revenues, or to cable company profits, programming costs are relatively small, and their share has been stable or, by some measures, declining. And, the cost of any broadcast retransmission consent compensation is a small fraction of what cable and satellite companies pay for non-broadcast programming.

Figure 6 below shows the relationship between cable operators' programming expenses, on the one hand, and their overall expenses and revenues, on the other, as reported by SNL Kagan. The data show that programming expenses have declined in recent years when compared to both revenue and expenses, falling to less than 24 percent of revenues in 2006. This period coincides with the period when cable operators have complained most aggressively about *rising* programming costs.

FIGURE 6:
PROGRAMMING EXPENSES VS. TOTAL REVENUE AND TOTAL EXPENSES
MAJOR CABLE OPERATORS (2001-2006)

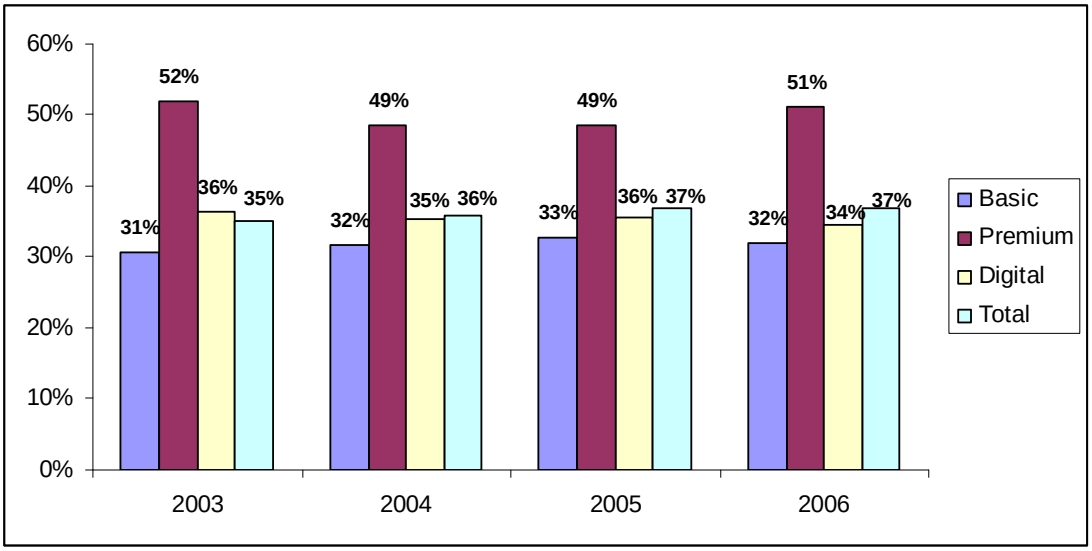



*Source: SNL Kagan, Benchmarking Cable*

The Kagan data is consistent with data reported by other industry analysts. Figure 7 shows the results of an analysis by Morgan Stanley[45] of programming costs in relationship to video revenues (as opposed to all revenues), by category type of programming. As the figure shows, there simply is no evidence that programming costs have increased relative to the revenues cable operators earn from distributing that programming.

45. See Morgan Stanley, *Cable/Satellite: Looking into 3Q06 and 2007; Cautious on the Top Line, Capital Expenditures, and Lofty Valuations* (Oct. 25, 2006) [hereafter *Morgan Stanley*].

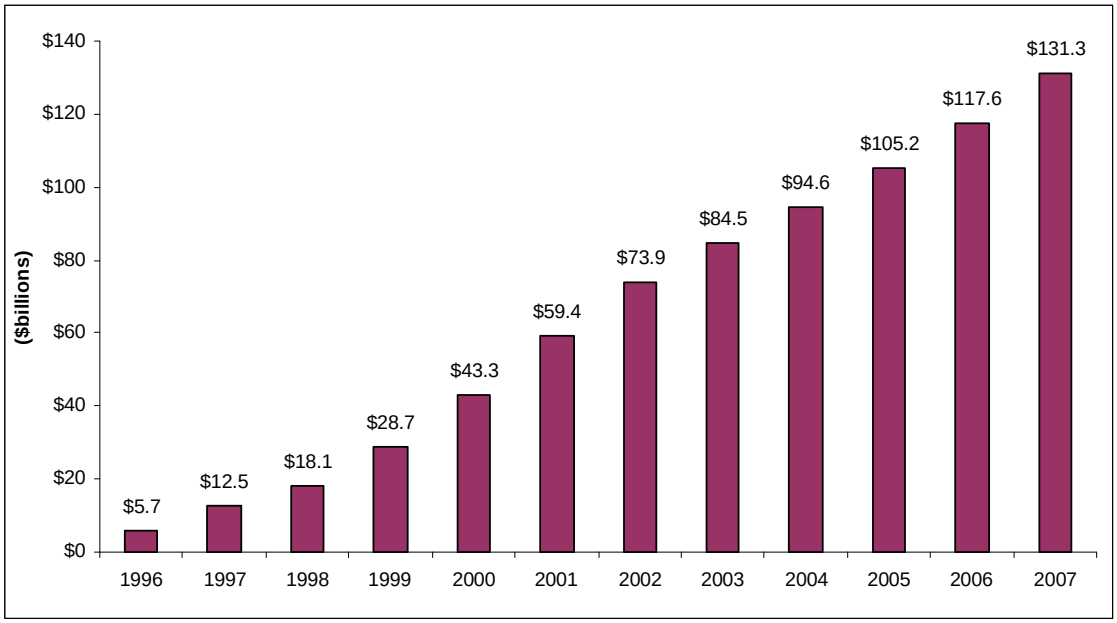
FIGURE 7:
CABLE OPERATORS' PROGRAMMING COSTS AS A PROPORTION OF VIDEO REVENUES, BY CATEGORY OF PROGRAMMING, 2003-2006




*Source: Empiris LLC, Morgan Stanley*

The operating expense figures discussed above do not include the large infrastructure investments made by cable operators in recent years. As shown in Figure 8, the National Cable and Telecommunications Association (NCTA) reports that cable operators have invested more than $131 billion since 1996 to replace coaxial cable with fiber optic technology and to install new digital equipment in homes and system headends, allowing them to provide digital signals, broadband services, telephony services, high-definition television (HDTV), and video-on-demand services.

FIGURE 8:
CUMULATIVE INVESTMENT IN PLANT BY CABLE OPERATORS 1996-2007 ($BILLIONS)

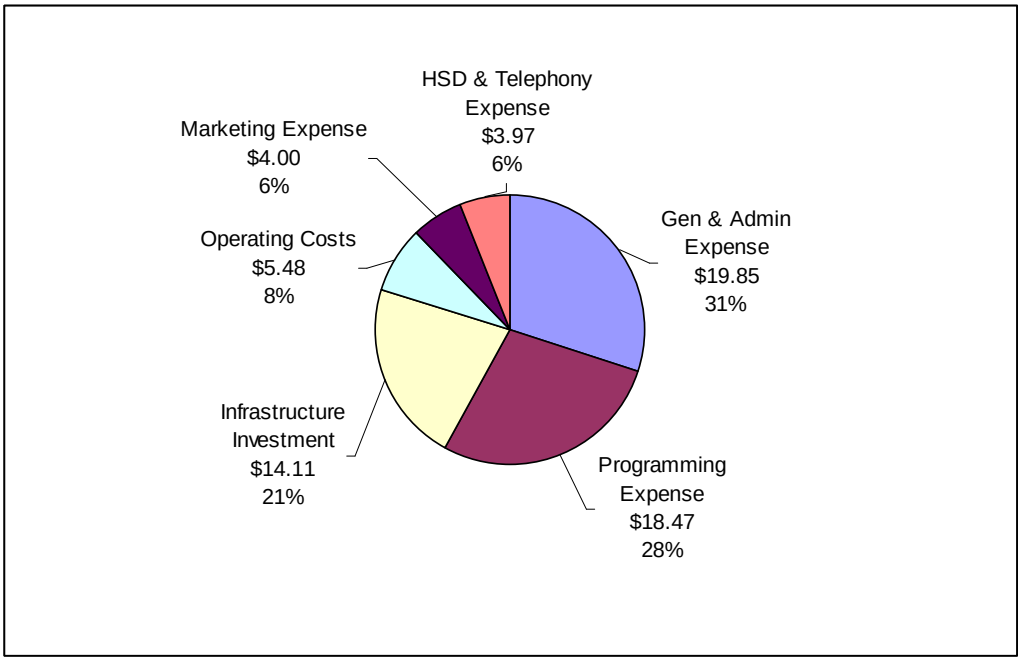



*Source: National Cable and Telecommunications Association*

As Figure 9 shows, when cable operators' investments in infrastructure are taken into account, the proportion of their total expenditures accounted for by programming falls to 28 percent.

FIGURE 9:

CABLE OPERATORS EXPENSES PER SUBSCRIBER PER MONTH
(INCLUDING INFRASTRUCTURE SPENDING), 2006




*Source: Empiris LLC, Morgan Stanley*

It is also useful to compare programming costs to cable operators' profits, which have increased substantially in recent years. If programming expenses were significantly contributing to the cable operators' costs, then one would expect, other things equal, that profits would decline as programming expenses increased.[46] The evidence suggests otherwise.

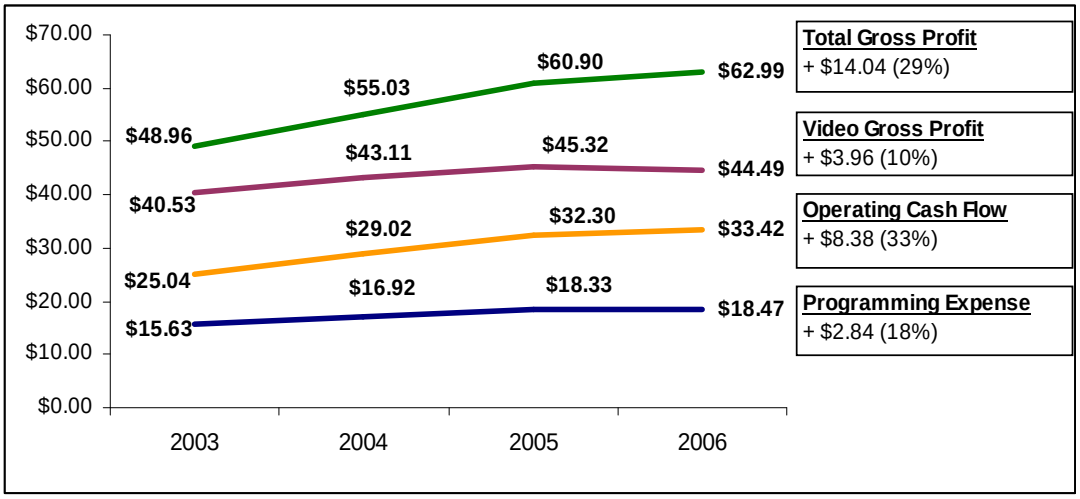
Figure 10 shows the change in programming expenditures (per subscriber, per month) compared with three measures of profitability – total gross profit, video gross profit, and operating cash flow, for 2003 through 2006 for four leading cable operators.[47] Total gross

46. In general, some portion of an increase in the cost of an input will be passed through to consumers, with the precise effect depending on several factors, including the share of the input's contribution to the production of the overall service, changes in the quality of the input (and resulting changes in quality of the output), and the competitive structure of the industry. Firms in a perfectly competitive industry pass on 100 percent of a cost increase to end users, whereas a firm with monopoly power absorbs a certain percentage of a cost increase. See, e.g., P.R.G. Layard and A.A. Walters, *Micro-Economic Theory* (1978), esp. Ch. 9-10.

47. Based on data reported by Morgan Stanley for Cablevision, Charter, Comcast and Time Warner.

profits increased from $48.96 per subscriber per month in 2003 to $62.99 per subscriber per month in 2006, an increase of $14.03, or 29 percent. During the same period, programming expenses per subscriber per month increased from $15.63 to $18.47, an increase of $2.84 per subscriber per month, or 18 percent. Thus, the increase in gross profits per subscriber for these cable operators was approximately five times as large as the increase in programming expenses per subscriber (and, in percentage terms, nearly twice as large). As the figure shows, on a percentage basis, three of the four metrics grew more rapidly than programming expenses; the fourth, video gross profits, still grew by more than programming expenses in absolute terms.

FIGURE 10:
GROWTH IN PROGRAMMING EXPENSES VS. MEASURES OF PROFITABILITY,
MAJOR CABLE OPERATORS (PER SUBSCRIBER PER MONTH, 2003-2006)




*Source: Empiris LLC, Morgan Stanley.*

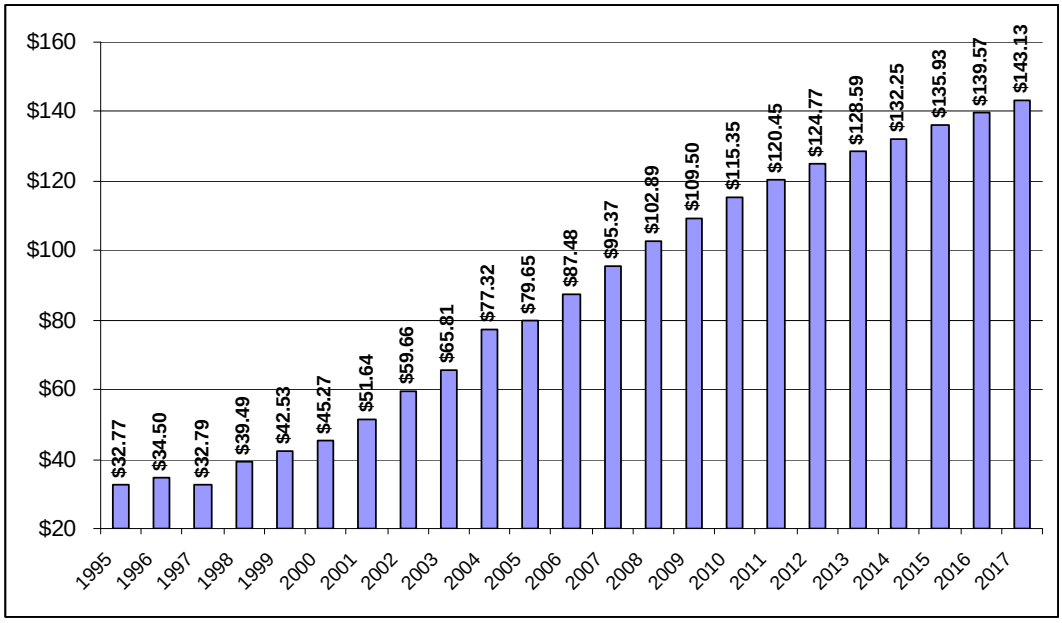
In summary, there simply is no evidence that the in-kind compensation cable operators have paid to broadcasters for retransmission consent has resulted in increased programming expenses relative to cable operators' revenues, other expenses, or profits. Accordingly, there is no basis for cable operators' claims that retransmission consent has had any appreciable effect on cable subscription rates paid by consumers.

## B. Monetary Compensation for Retransmission Consent is *De Minimus* and Likely to Remain So

As noted above, cable operators have resisted paying monetary compensation for retransmission consent and argued that the recent trend in favor of monetary compensation will cause them to raise prices to consumers still further. The evidence shows, however, that monetary compensation represents a tiny fraction of cable operators' revenues, and – even if nearly all broadcasters are successful in winning monetary compensation – will remain a tiny fraction in the future.

Figure 11 shows actual and projected revenue per residential cable subscriber, as reported by SNL Kagan, for 1995 through 2017. As the figure indicates, cable operators have seen dramatic increases in their monthly subscriber revenues (average revenues per unit, or ARPU) in recent years, with ARPUs more than tripling (from $32.77 to $102.89) between 1995 and 2008. Cable operators have seen increases in revenues from basic and enhanced video services, from high-speed data services, and, most recently, from cable telephony. All of these revenues, however, are ultimately attributable in some measure to the basic cable programming that forms the core of cable operators' new triple-play offerings: Without video, their entry into these new markets would be vastly more difficult, if not impossible.

FIGURE 11:
ACTUAL AND PROJECTED AVERAGE REVENUE
PER RESIDENTIAL CABLE SUBSCRIBER (1995-2017)

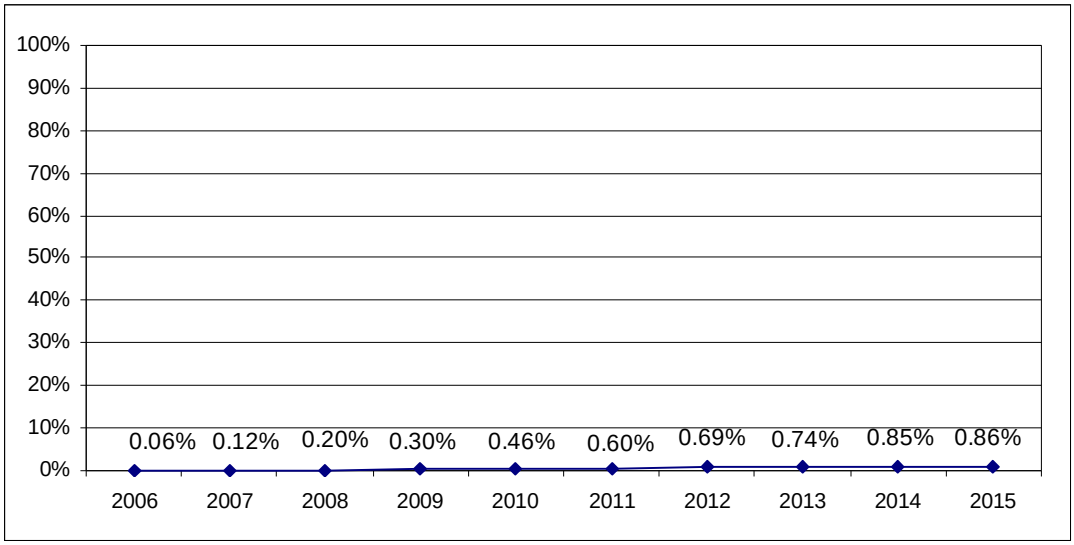



*Source: SNL Kagan, Cable Futurecast*

Monetary retransmission consent compensation represents, and is expected to continue to represent, only a tiny fraction of the cable companies' exploding revenue base. While retransmission consent agreements are typically confidential, broadcasters do provide reports on overall revenues, including data that can be used to estimate retransmission consent fees. Figure 12 below shows SNL Kagan's estimates for retransmission consent fees as a proportion of cable company revenues from 2006 through 2015, assuming that (a) the proportion of cable subscribers covered by monetary compensation agreements for retransmission consent increases from 18 percent in 2006 to 95 percent in 2012 and beyond, and (b) the number of broadcast stations in each market that receive monetary compensation increases from 1.5 in 2006 to 4.0 in 2014 and beyond; that is, the figures assume that virtually all major broadcast stations receive monetary compensation for retransmission by the end of the period. As the figure shows, Kagan estimates that monetary compensation accounts for only 0.2 percent (that is, two tenths of one

percent) of cable company revenues today, and that, even under very liberal assumptions about the trend towards monetary retransmission consent fees in the future, will never reach one percent of cable revenues.

FIGURE 12:
ACTUAL AND PROJECTED RETRANSMISSION FEES AS A PERCENTAGE OF CABLE REVENUES
2006-2015




*Source: Empiris LLC, SNL Kagan*

These figures are perhaps even more stark when expressed in dollars and cents. Kagan estimates that the average total retransmission consent fee paid by cable companies in 2015 will be $1.14 (for four broadcast channels), while at the same time cable companies will be charging the average subscriber about $136 per month. Put still another way, monetary retransmission consent fees are projected to increase by $1.08 per subscriber per month in the next decade; during the same period, cable revenues per subscriber will go up approximately 45 times as much, by $48.38. Retransmission consent fees, in other words, simply cannot be responsible for any significant portion of cable operators' increasing monthly fees.

## V. NEGOTIATING IMPASSES ARE RARE, AND HAVE A NEGLIGIBLE IMPACT ON CONSUMERS

As noted above, cable operators have resisted the move towards monetary retransmission consent fees. Despite the fact that both DBS operators and, more recently, telephone companies that provide video services have paid monetary fees for retransmission, cable companies have fought hard to hang on to the "in kind" compensation regime they successfully imposed in the wake of the 1992 Act. One symptom of this resistance has been the willingness of cable companies temporarily to forego carriage of broadcast stations rather than accede to monetary compensation. In addition, as DBS operators' market shares have increased during the 1990s, and as they have increasingly sought to increase their ability to transmit local broadcast stations into local markets (local-into-local carriage), they too have grown more likely temporarily to forgo carriage of some broadcast stations when retransmission consent agreements are not reached.

As noted above, negotiating impasses that result in carriage interruptions are costly for program distributors and cable companies alike. Consumers also incur a cost, as they may be inconvenienced (e.g., by having to purchase and install antennas, or learning to download some of their favorite programs over the Internet), or even decide to forego watching some programming. Concerns about the impact of negotiating impasses on consumers have raised questions in the minds of some about whether retransmission consent should be weakened or reformed.[48]

This section presents evidence demonstrating that carriage interruptions resulting from retransmission consent impasses are extremely rare, typically brief, and have a negligible impact on consumers.

Two points should be noted at the outset. First, the right to not agree is fundamental to any negotiation. As indicated above, this is the posture Congress took in passing the 1992 Cable Act (when it indicated it would not "dictate the outcome" of negotiations), and it has been faithfully upheld by the FCC on the occasions when cable and DBS operators have sought its intervention. Second, the alternative to permitting free negotiations is to force companies to engage in binding arbitration. Ultimately, however, the purpose of arbitration is to set prices and terms, i.e., to engage in price controls, even if on a case-by-case basis. Given the complexities and higher differentiated circumstances associated with retransmission consent negotiations, the probability of mandatory arbitration achieving anything approaching socially optimal prices and terms is low.

If carriage interruptions were imposing large costs on the U.S. economy, or even on a substantial proportion of consumers, some might argue that mandatory arbitration, despite its inherent inefficiencies, should be considered. The evidence, however, shows that this is not the case.

Between January 2006 and December 2008, *Broadcasting and Cable* reported a total of eight instances in which retransmission disputes led to carriage interruptions.[49] As shown in Table 2, four of these involved a DBS operator (Dish Network), while the other four involved cable companies (Mediacom, Suddenlink, and Time Warner). The number of stations involved ranged from as few as one to as many as 24, while the duration of the interruption ranged from as

48. See, e.g., *CRS Report* at 1-2.

49. *Broadcasting and Cable* is the leading trade magazine covering the broadcasting and cable industries and it is reasonable to assume that it covered every instance in which a negotiating impasse led to an interruption in carriage.

few as five days to as many as 415.[50] The simple average duration of the disputes was 91 days, but this average is heavily affected by the single-station dispute between KAYU and Time Warner: The average of duration of the other seven disputes was approximately 44 days.

TABLE 2:
RETRANSMISSION DISPUTES RESULTING IN CARRIAGE INTERRUPTIONS, 2006-2008

| Parties | Dates | Duration (Days) | Number of Stations Affected | List of Stations Affected | Total Households in Affected DMAs |
|---|---|---|---|---|---|
| **Fisher Communications/Dish Network** | 12/18/08-present | 14 (through 12/31/08) | 10 | KBAK, KBFX, KBCI, KVAL, KIDK, KATU KOMO,KUNS, KIMA, KUNW | 4,061,880 |
| **Young Broadcasting/Dish Network** | Mid-December 2008 | 5 | 10 | KRON , WLNS, WKRN, WTEN, WRIC, WATE, WBAY, KLFY, KELO, KWQC | 6,650,980 |
| **Lin TV/Time Warner Cable** | October-November 2008 | 31 | 17 | KXAN, KNVA, KBVO, WIVB,WNLO, WWHO, WUPW, WDTN, WISH, WNDY, WIIH, WTHI,WANE, WLUK,WALA,WBPG,WWLP | 5,914,950 |
| **Citadel/Dish Network** | August-September 2008 | 37 | 4 | WOI , WHBF, KLKN, KCAU | 1,178,200 |
| **Barrington/Dish Network** | July-September 2008 | 72 | 1 | KRCG | 179,010 |
| **Lin TV/Suddenlink** | December 2007 – March 2008 | 90 | 2 | KXAN, KBIM | 1,356,790 |
| **KAYU/Time Warner Cable** | December 2006 – February 2008 | 415 | 1 | KAYU | 416,630 |
| **Sinclair/MediaCom** | December 2007 – February 2008 | 60 | 24 | KDSM , KGAN,WEAR, WFGX , WYZZ , WLOS, WMYA , WDKY, WMSN, WZTV, WUXP, WNAB, WUCW, KBSI, WDKA, WICS WICD, KDNL, WTWC, WTTO, WABM, WTVZ, WCGV, WVTV | 10,726,520 |
| **Averages/Totals** | NA | 91 | 9 | | 30,484,960 |

It would be incorrect, however, to conclude that all of the households in these DMAs – or even a significant fraction of them – were affected by these carriage interruptions. First, these

50. One dispute, between Fisher Communications and Dish Network, is still ongoing; for purposes of the calculations below, which are based on 2006-2008 viewing data, only the 14 days in 2008 for which carriage was interrupted are counted.

interruptions affected (at most) only the households subscribing to the MVPD involved in the dispute. Thus, only Dish subscribers (not cable subscribers, and not DirecTV subscribers) were affected by the Dish disputes; and, only subscribers of the affected cable company (not DBS subscribers or subscribers of other cable companies operating in these DMAs) were affected by the disputes involving cable companies. Of course, none of the households which receive their television exclusively over the air (i.e., which do not subscribe to pay TV at all) were affected at all.

Second, among households which do subscribe to the affected cable or DBS provider, not all households would have watched the affected channels at all during the duration of the interruption. Nationally, the typical household only tunes in to about 17 television channels each month.

Third, even among households that would otherwise have tuned in to a particular channel during the period of the interruption, it is reasonable to believe that many of them were able to find another channel offering acceptable programming. For example, a viewer who might have tuned in to the local nightly news on the channel for which carriage was interrupted in order to see the weather forecast might well have found local weather news on another channel.

Taking these three factors into account, it is clear that many of the households in a DMA where a carriage interruption occurs would be *completely unaffected by that interruption*, as they did not subscribe to the MVPD involved in the interruption, would not have watched the affected channel anyway, or found the programming they were seeking on a different channel.

For some households, however, it is reasonable to believe that the interruption did have at least some effect. One way of measuring that effect is to estimate how many hours those households would have spent viewing the affected station in the absence of the interruption. It is

possible to arrive at such an estimate by combining data on the number of households affected by a particular carriage interruption (i.e., the number subscribing to the affected MVPD) with ratings data for the interrupted stations.

Table 3 presents estimates of the impact of the eight carriage interruptions during 2006-2008 on household viewing hours, both in the aggregate and as a proportion of total viewing hours. Columns (1) and (2) show the number of markets affected by each interruption, and the total number of TV households in those markets. Column (3) shows the estimated proportion of households in the affected markets which subscribe to the MVPD for which service was interrupted – i.e., the proportion of households *potentially* affected by the interruption. Column (4) shows, for potentially affected households only, the average number of daily viewing hours affected by the interruption, i.e., the hours those households would have spent watching the station that was made unavailable by the interruption, and Column (5) shows affected viewing hours for those households divided by total daily viewing hours, i.e., the proportion of daily television viewing time affected by the interruption. Column (6) shows affected viewing hours as a proportion of total annual viewing hours for potentially affected households; Column (7) shows affected viewing hours as a proportion of total viewing hours for all households in the affected markets (including those subscribing to an unaffected MVPD, or which receive television only over the air). The bottom row in the table shows national totals and averages.

TABLE 3:
ESTIMATED EFFECT OF SERVICE INTERRUPTIONS ON VIEWING HOURS

| Parties | (1) Affected Markets | (2) Total TV HHs in Affected Markets | (3) % TV HHs Subscribing to Affected MVPD | (4) Daily Affected Viewing Hours (Affected HHs) | (5) % Daily Viewing Hours Affected (Affected HHs) | (6) % Annual Viewing Hours Affected (Affected HHs) | (7) % Annual Viewing Hours Affected (All TV HHs) |
|---|---|---|---|---|---|---|---|
| **Fisher Communications/Dish Network** | 7 | 4,061,880 | 13% | 0.39 | 4.7% | 0.27% | 0.03% |
| **Young Broadcasting/Dish Network** | 10 | 6,650,980 | 13% | 0.80 | 9.7% | 0.10% | 0.01% |
| **Lin TV/Time Warner Cable** | 11 | 5,914,950 | 38% | 0.55 | 6.7% | 0.67% | 0.25% |
| **Citadel/Dish Network** | 4 | 1,178,200 | 15% | 0.40 | 4.8% | 0.46% | 0.07% |
| **Barrington Broadcasting/Dish Network** | 1 | 179,010 | 20% | 0.88 | 10.7% | 2.12% | 0.43% |
| **Lin TV/Suddenlink** | 2 | 1,356,790 | 22% | 0.40 | 4.8% | 0.92% | 0.20% |
| **KAYU/Time Warner Cable** | 1 | 416,630 | 10% | 0.28 | 3.4%* | 3.83% | 0.38% |
| **Sinclair/MediaCom** | 16 | 10,726,520 | 7% | 0.32 | 3.9% | 0.95% | 0.07% |
| **National Averages/Totals** | **47*** | **30,484,960** | **16%**** | **0.47**** | **5.7%**** | **0.21%**** | **0.0089%***** |

* Rows to not add to total since some markets were affected by more than one dispute. ** Average across affected markets. *** Based on 100% of U.S. TV HHs.

The data shown in Table 3 demonstrate that the impact of retransmission consent-related carriage interruptions on television viewing in the U.S. is infinitesimally small. For example, the bottom row of columns (4) and (5) shows that households subscribing to MVPDs affected by service interruptions were unable to view their "first choice" television station for about 30 minutes during each day of the interruption, representing less than *six percent* of the average household's total daily viewing time of 8.2 hours; the highest proportion of viewing time affected, in the Barrington/DISH dispute, was less than an hour, or about 10.7 percent of daily viewing time. Of course, these figures assume none of these households had access to those channels over-the-air, and that none were able to find equally acceptable programming on other stations.

Overall, as shown in the bottom row of column (7), the eight service interruptions that occurred in 2006-2008 affected just *0.0089 percent* – that is less than one one-hundredth of one percent – of annual television viewing hours in the United States. To put this figure in perspective, on average, U.S. households experienced an average annual service interruption – that is, the inability to tune in to their first-choice television channel – of about 16 minutes during this period. To put this figure in further context, the average North American household experiences annual electricity outages of about 381 minutes – during which time, they are, of course, unable to watch *any* TV channels. Thus, the average household is about 24 times as likely to be without electricity at any given time during the year than it is to be deprived of its first-choice television channel as a result of a retransmission-related carriage interruption.

Another benchmark worth considering is this: The *aspirational* standard for cable system reliability is 99.97%, implying average annual system outages of 158 minutes per year.[51] Assuming (conservatively) that cable systems meet this aspirational target, the typical U.S. household is about ten times as likely to be without any cable service at all as a result of a cable system outage than it is to be unable to watch its favorite broadcast channel as a result of a retransmission dispute.

## VI. CONCLUSION

Cable operators seek to weaken the retransmission consent regime, thereby strengthening their leverage in negotiations with broadcasters. They argue broadcasters have market power, that they have used this power in the past to impose unreasonable in-kind compensation arrangements, and that they will use it in the future to force payment of excessive monetary compensation. They wrap all of their arguments in the notion that retransmission consent

increases the cost of programming, which must then be passed through to consumers in the form of higher cable rates – thereby explaining why cable rates are rising so rapidly.

Each and every one of the cable operators' assertions is incorrect. Broadcasters do not have market power in the national market for MVPD programming, and they do not have the ability to impose uneconomic terms of any kind on MVPDs at the local level. Programming expenses do not explain a significant portion of rising cable rates. Moreover, the move towards monetary compensation for broadcast signals – which cable operators have successfully resisted for 15 years – is likely to increase economic efficiency and enhance consumer welfare, as it provides another means (in addition to barter) for broadcasters and distributors to reach efficiency-enhancing bargains. Finally, concern about the impact on consumers of carriage interruptions resulting from impasses in retransmission negotiations is misplaced, as such impasses are rare and typically brief, and do not affect a significant proportion of household television viewing.

More broadly, retransmission consent is achieving precisely what Congress intended it to achieve when it passed the 1992 Cable Act: Establishing a market based mechanism to ensure that broadcasters receive the economically efficient level of compensation for the value of their signals. Such compensation ultimately benefits consumers by enriching the quantity, diversity, and quality of available programming, including local programming. Thus, proposals to repeal or weaken the existing system are misguided, and would harm consumer welfare.

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51. See Walter Ciciora, et al, *Modern Cable Television Technology 2d* (Amsterdam: Morgan Kaufmann, 2004) p. 720. Cable operators do not publicly report their actual outage rates.