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Retransmission Consent and Other Federal Rules Affecting Programmer-Distributor Negotiations: Issues for Congress

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Retransmission Consent and Other Federal Rules Affecting Programmer-Distributor Negotiations: Issues for Congress

Summary

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

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

The small cable companies have argued that some of the existing statutory and regulatory requirements were implemented at a time when cable was a monopoly and were intended to protect broadcasters. Now that the market dynamics have changed, they argue, some of these rules should be changed to allow for more even-handed negotiations. At the same time, however, as a result of consolidation and clustering in the cable industry there are a few very large cable companies, which primarily serve major markets, as well as the two national satellite operators, that appear to have sufficient market strength to be able to withstand many of the demands of the programmers with must-have programming and to place small independent programmers at a negotiating disadvantage. This report will be updated as warranted. For a condensed version of this report, see CRS Report RL34079.

Contents

Overview 1

Market Changes Affecting the Programmer-Distributor Relationship 11
- More Distribution Options 11
- Consolidation and Clustering of Cable Operators 13
  - Negotiating with a cable program network 18
  - Negotiating with a national broadcast network 19
  - Negotiating with a local broadcast station or non-network broadcast group 20
- More Program Networks/Fragmented Audiences 20
- Cable System Revenue is Growing From High Speed Internet Access and Telephone Services 29

Specific Examples of Programmer-Distributor Conflicts 31
- Nexstar: The First Broadcaster to Aggressively Seek Cash Payments for Retransmission Consent 31
- CBS: The Only Major Broadcast Network to Aggressively Seek Cash Payments for Retransmission Consent 35
- DISH Network/Lifetime/Hearst-Argyle: An Example of the Complexity of Programmer-Distributor Negotiations 36
- Sinclair's Negotiations with Various MVPDs: A Case Study of Factors Affecting Negotiating Strength 40
  - Sinclair-Mediacom 40
  - Sinclair-Suddenlink 45
  - Sinclair-Time Warner 50
  - Sinclair-Comcast 51
  - Sinclair-Charter 53
  - Measuring Retransmission Consent Revenues 53
- Time Warner: A Large Cable Company Demands Cash Payments from Broadcasters to Retransmit Their Non-Primary Signals 54

Issues for Congress: Proposals for Statutory and Regulatory Change 56
- Economic Factors Relevant to Analysis of the Proposals for Statutory and Regulatory Change 57
- Specific Proposals to Modify Current Statutes and Regulations 60
  - Proposal: Allow the importation of distant signals when a retransmission consent impasse develops 60
  - Proposal: Require broadcasters to publish rate cards that would apply to all MVPDs 62
  - Proposal: Require parties to submit to binding arbitration to resolve leased access, program carriage, or retransmission consent disputes 62
  - Proposal: Strengthen the FCC test for what constitutes "good faith" retransmission consent negotiations 64
  - Proposal: Prohibit tying carriage of popular programming to carriage of less popular programming 66

Proposal: Require programmers to offer their broadcast and cable networks to distributors on an à la carte basis 67
Proposal: Prohibit programmers from requiring their networks to be placed on the expanded basic service tier 69
Proposal: Prohibit the ownership or control of more than one television station in a market or prohibit a "duopoly" owner from tying retransmission consent for one station to another 70
Proposal: Place set-top boxes in customer premises that pick up local broadcast station signals off the air without requiring MVPDs to retransmit broadcast signals 72
Proposal: Close the "terrestrial loophole" exception to the requirement for nondiscriminatory access to programming in which a cable operator has an attributable interest 73
Proposal: Clarify the definition of a regional sports network 73

List of Tables

Table 1. Consolidation in the National Market for the Purchase of Video Programming (Percentage of MVPD Subscribers), 2002-2005 14
Table 2. The 25 Largest Cable Operators as of December 2006 15
Table 3. Cable Television System Clusters Serving More Than 100,000 Subscribers, as of December 2005 16
Table 4. Cable Program Networks with the Largest Number of Subscribers, as of December 2006 19
Table 5. Nielsen Data on Total Television Households, Time Spent Viewing Per Household, and the Average Number of Video Channels Received Per Household, 1985-2006 21
Table 6. Estimated Share of U.S. Television Home Set Usage by Program Source (%) 23
Table 7. The Average Weekly Cumulative Audience Reach of the Largest Broadcast and Cable Program Networks, First Quarter 2007 24
Table 8. The Individual Television Programs with the Largest Audience Ratings, 2005-2006 Television Season 25
Table 9. The Advertiser-Supported Cable Networks with the Highest Average License Fees Per Subscriber Per Month, 2005 27
Table 10. Cable Company Revenues, by Service, 1996-2005, in Millions of Dollars 30
Table 11. Estimated Number of Television Program Sources Viewed per Adult, 2005 59

Retransmission Consent and Other Federal Rules Affecting Programmer-Distributor Negotiations: Issues for Congress

Overview

Virtually all U.S. households have a television and almost 86% of these television households get their video programming by subscribing to a multichannel video programming distributor (MVPD) — in most cases a cable operator or a direct broadcast satellite (DBS) operator — rather than relying upon "free" over-the-air broadcast television signals.[1] As a result, when conflicts arise between programmers and MVPDs about the carriage of particular video programming, the price for that programming, or the tier on which the programming is to be offered to the end user (for example, on a basic or premium tier, on a "top 60" or a "top 120" tier, or on an analog or digital tier), many consumers can be affected.

Recently, there have been several incidents in which a negotiating impasse between a programmer and an MVPD has resulted in the programmer refusing to allow the MVPD to carry, or the MVPD choosing not to carry, a program network, forcing the MVPD's subscribers to choose between foregoing that program network or switching to a competing MVPD that does carry the program network.[2] There also have been a number of situations in which programmer-distributor negotiations have been resolved without any disruption in program carriage, but only after the negotiations played out in public, with subscribers and public officials being warned of the danger of losing access to particular programming and being encouraged by

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

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

each side to contact the other side in order to place pressure on them to compromise. Often these public negotiations have occurred when the programming at risk included upcoming sports events that some subscribers placed a high value on viewing.[3] Also, there have been incidents in which an MVPD has announced a price increase to subscribers shortly after the conclusion of contentious negotiations with a programmer, with the MVPD attributing the price increase to higher programming costs, and the programmer denying the causal connection.

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

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

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[3] See, for example, Peter Grant and Brooks Barnes, "Channel Change — Television's Power Shift: Cable Pays for 'Free' Shows; Broadcasters Want Cash to Carry Their Signal; Super Bowl is Hostage," *Wall Street Journal*, February 5, 2007, at p. A1.

[4] For a detailed discussion of many of these statutory provisions and regulatory requirements, see Federal Communications Commission, *Retransmission Consent and Exclusivity Rules: Report to Congress Pursuant to Section 208 of the Satellite Home Viewer Extension and Reauthorization Act of 2004* (FCC Retransmission Consent Report), September 8, 2005, available at [http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-260936A1.pdf], viewed on June 28, 2007.

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

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

[7] Section 614(b)(3)(A) of the Communications Act states that "A cable operator shall carry

(continued...)

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

- a number of Federal Communications Commission (FCC or Commission) **exclusivity rules**[8] that give local broadcasters the exclusive right to distribute certain programming (the network program non-duplication rules[9] and syndicated exclusivity protection rules[10]) or that protect a sports team's or sports league's distribution

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

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

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

[10] With respect to non-network programming, cable systems that serve at least 1,000 subscribers may be required, upon proper notification, to provide syndicated protection to broadcasters who have contracted with program suppliers for exclusive exhibition rights to certain programs within specific geographic areas, whether or not the cable system affected is carrying the station requesting this protection. However, no cable system is required to
(continued...)

rights to a sporting event taking place in a local market (the sports programming blackout rules[11]). These rules, which tend to mirror the terms found in most network-affiliate contracts and station-syndicator contracts, limit the ability of a cable operator that has not been able to reach a retransmission consent negotiation with a local broadcaster that transmits network or syndicated programming to import the same programming from a more distant broadcaster.

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

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[10] (...continued)
delete a program broadcast by a station that either is significantly viewed or places a Grade B or better contour over the community of the cable system.

[11] A cable system located within 35 miles of the city of license of a broadcast station where a sporting event is taking place may not carry the live television broadcast of the sporting event on its system if the event is not available live on a local television broadcast station, if the holder of the broadcast rights to the event, or its agent, requests such a blackout. The holder of the rights is responsible for notifying the cable operator of its request for program deletion at least the Monday preceding the calendar week during which the deletion is desired. If no television broadcast station is licensed to the community in which the sports event is taking place, the 35-mile blackout zone extends from the broadcast station's licensed community with which the sports event or team is identified. If the event or local team is not identified with any particular community (for instance, the New England Patriots), the 35-mile blackout zone extends from the community nearest the sports event which has a licensed broadcast station. The sports blackout rule does not apply to cable television systems serving less than 1,000 subscribers, nor does it require deletion of a sports event on a broadcast station's signal that was carried by a cable system prior to March 31, 1972. The rule does not apply to sports programming carried on non-broadcast program distribution services such as ESPN. These services, however, may be subject to private contractual blackout restrictions.

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

- cable-related statutory **copyright provisions**, which set specific terms, conditions, and rates, including mandatory licenses, for certain uses of programming.[13] For example, cable systems enjoy a royalty-free permanent compulsory copyright license — that is, do not have to pay copyright fees — for the carriage of broadcast signals of stations located in their local market areas (called "designated market areas" or DMAs). But cable systems are required to pay royalties under a congressionally granted compulsory copyright license for the carriage of the signals of broadcasters located outside the DMA within which the cable system is located. The royalty-free license extends to the secondary transmission of out-of-DMA broadcast stations, however, if it can be shown that those out-of-DMA signals are "significantly viewed" by those households within the cable system's service area that only receive their television signals over-the-air.

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

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

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

- the **program carriage provisions** in section 616 of the Communications Act directing the FCC to establish regulations governing program carriage agreements and related practices between cable operators or other MVPDs and programmers that would prevent an MVPD from requiring a financial interest in a program service as a condition for carriage, from coercing a programmer to grant exclusive carriage rights, or from discriminating against an unaffiliated programmer in a fashion that unreasonably restrains the ability of that programmer to compete, when the programming is distributed over satellite.[15]

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

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[14] (...continued)
Assignors, to Time Warner Cable Inc. (subsidiaries), Assignees; Adelphia Communications Corporation (and subsidiaries, debtors-in-possession), Assignors and Transferors, to Comcast Corporation (subsidiaries), Assignees and Transferees; Comcast Corporation, Transferor, to Time Warner Inc., Transferee; Time Warner Inc., Transferor, to Comcast Corporation, Transferee, Memorandum Opinion and Order, adopted July 13, 2006, released July 21, 2006, at paras. 109 and 181.

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

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

apply to all cable program networks as broadband fiber optic cable becomes more widely deployed. This exception has been termed by some the "terrestrial loophole."

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

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

In addition to these federal rules, there sometimes is informal government intervention into programmer-distributor negotiations because of political sensitivity to consumers losing access to programming — and especially local programming. Parties involved in negotiating impasses, or consumers affected by those impasses, often will seek intervention by an elected official or regulatory agency, even where there is no formal process for such intervention. In some instances, political pressure

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

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

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

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

can be placed on a party to resolve a contractual conflict in a fashion that it would not agree to in a strictly private negotiation.[21] In at least one situation in which a cable company and broadcast station reached an impasse in retransmission consent negotiations and the local broadcast signal was removed from the cable company's offering, a city attorney threatened legal action against the cable company unless the broadcast signal were restored, claiming that not providing the signal was a violation of the franchising agreement between the city and the cable company.[22]

Recently, there have been more frequent incidents of programmers and MVPDs failing to reach contractual agreements, and in several instances one or the other party — or end users who were affected by the impasse — have sought federal government intervention either at the FCC or with Congress. The parties seeking intervention often propose modification of existing statutory provisions or regulatory requirements that allegedly favor one side in the negotiations or undermine the successful consummation of negotiations.[23] Although these impasses have involved a number of different issues, the most controversial (and widely publicized) conflicts have involved unresolved retransmission consent negotiations or agreements that would award a single distributor exclusive rights for sports programming or that would require that high-priced sports networks be placed on the expanded basic tier.

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

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[21] Some cable companies have complained that although, once a broadcast station has chosen the retransmission consent option rather than the must-carry option, there is no statutory requirement for a cable company to reach a retransmission consent agreement with the broadcast station if it is not in the cable company's interest to do so, in practice the political pressure placed on the cable company can force it to accept a detrimental contract. See, for example, the lengthy interview of Fred Dressler, executive vice president of programming, Time Warner Cable, presented as "Past, Present and Future: An Oral History; Fred Dressler reflects on his career, the industry and its future," *An Advertising Supplement to Multichannel News*, December 18, 2006, at pp. 18a-36a.

[22] See Anne Veigle, "Cox Maneuver Puts TV Stations Back on Cable," *Communications Daily*, February 3, 2005, at pp. 4-5.

[23] There is precedence for changing regulations affecting the programmer-distributor relationship as market conditions change. For example, in 1970, prior to the development of cable and satellite television, when the then-three major broadcast networks (CBS, NBC, and ABC) captured approximately 90% of television viewers, the FCC implemented Financial Interest and Syndication Rules (Fin-Syn Rules) that prohibited the networks from holding a financial interest in the television programs they aired beyond first-run exhibition and from creating in-house syndication arms. Consent decrees executed by the Department of Justice in 1977 solidified the rules and limited the amount of prime-time programming the networks could produce themselves. In 1991, based in part in the decrease in major broadcast networks' audience market share to approximately 65%, the FCC relaxed the Fin-Syn Rules. Appeals courts later relaxed the rules even further, in effect eliminating the rules by November 1995.

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

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

Despite all these complexities, the relationships among content producer, programmer, and distributor are characterized by mutual need — both the content producer and the programmer need distributors that have direct contact with the potential audience; the distributor needs content producers and programmers with good content to attract subscribers. At the same time, there is an inherent tension as each seeks to capture the lion's share of the value that consumers place on the content. Each must weigh the potential loss if an impasse occurs and the programmer refuses to permit the distributor to carry the programming or if the distributor chooses not to carry the programming. For example, for the programmer that potential loss could take the form of foregone compensation from the MVPD

and/or foregone advertising revenues as advertisers respond to a reduced audience,[24] both of which could be substantial if the MVPD's subscribers represent a significant portion of the programmer's total audience and if those subscribers do not switch to another MVPD that does carry the programmer's network. For the distributor, that potential loss could take the form of foregone subscriber revenue if, without the programming as part of its offering, some end users shift to a competing MVPD, as well as foregone advertising revenues. The losses could be substantial if many subscribers switched to a competing MVPD. Given these risks, negotiating impasses usually are avoided. Over time, market forces have led to the adoption of business models that serve content providers, programmers, and distributors.

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

There is one critical business practice that tends to hold for the contractual relationships at all levels — the practice of including a strict non-disclosure provision that prohibits the parties from revealing the terms, rates, and conditions in the contract. This practice limits the information publicly available to the negotiating parties and thus tends to favor the larger parties (whether programmers or distributors) who are involved in more negotiations and thus privy to more confidential information. This practice also severely limits public policy makers' access to information, since even parties that would be willing to make such information available to government agencies are prohibited from doing so.

This report first analyzes the changing programmer-distributor market dynamics for non-sports programming that are threatening to undermine traditional business models.[25] It then provides examples of recent programmer-distributor conflicts that

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

[25] This report does not directly address sports programming because there are a number of factors that are unique to sports programming — such as vertical integration by the content

(continued...)

reflect these market changes. Finally, it discusses proposals made by various parties to modify current statutory and regulatory rules in light of the market changes.

Market Changes Affecting the Programmer-Distributor Relationship

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

More Distribution Options

The most significant structural change in the video market is the increase in the number of program distribution options. Today, programmers can distribute their product not only through traditional broadcast television stations and cable operators, but also through direct broadcast satellite operators and other satellite companies, the new multichannel video offerings of the major telephone companies, cable "overbuilders,"[26] on-line video streams, and even cellular telephones. As a result, programmers have more options available to them to reach audiences and are able to negotiate with distributors from a position of strength, often demanding terms, conditions, and rates that are more favorable to themselves and less favorable to distributors than those that have prevailed in the past.[27] The market implications are greatest for "must-have" programming, such as major sports programming and the programming of the four major broadcast networks, for which a significant portion of subscribers have a sufficiently strong intensity of demand that they consider carriage of that programming a prerequisite for subscribing with an MVPD. An MVPD that does not offer must-have programming may find itself at a significant competitive disadvantage in the market. By contrast, the prevailing business model was developed — and some of the programmer-distributor contracts that are

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[25] (...continued)
providers into distribution, the unique demand characteristics of sports fans, the lack of close substitutes for major sports leagues, and the seasonal nature of sports — that yield viable business models that do not apply to non-sports programming. Sports programming is addressed in this report to the extent it represents "must-have" programming that affects programmer-distributor negotiations that affect non-sports as well as sports programming.

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

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

currently expiring were negotiated — in the early and mid 1990s, when cable operators typically were the monopoly MVPD in their service area and therefore had countervailing market power when negotiating with programmers, including those programmers with must-have programming.

One group of distributors — small and mid-sized cable companies — has been placed in a particularly difficult position by this structural market change, while a second group of distributors — the newly-entering telephone companies — has hastened this change. And both, in turn, have had an impact on all distributors.

Small and mid-sized cable companies often face direct competition from the two major satellite companies, DirecTV and DISH Network. These cable companies have far fewer subscribers than the major satellite companies and thus when negotiating with programmers typically do not pose a serious risk to the programmers if there is an impasse and the programming is not carried; a programmer's foregone per subscriber fees from these cable companies and foregone advertising revenues would not be substantial. By contrast, a programmer's revenues could be significantly reduced if one of the satellite companies discontinued carriage, since each of the satellite carriers have more than 13 million subscribers.[28] Moreover, many of the smaller cable companies have limited or no ability to offer telephone and broadband access services and therefore limited ability to offer bundled video/telephone/broadband services that tend to foster customer retention even when favored programming is no longer carried. Thus, if an impasse were to occur, a smaller cable company would face significant risk of losing subscribers to satellite companies. In fact, where a smaller cable company has had an impasse with a programmer, sometimes the programmer — or a satellite operator that has an agreement with the programmer and is competing with the cable company — has offered a "bounty" of upwards of $200 to households to switch to the satellite service, with these offers marketed over the programmer's network while the programmer-cable company negotiations are still on-going.[29]

The telephone company entrants, which are starting to offer multichannel video service and therefore must offer a wide array of programming to attract consumers away from incumbent cable and satellite providers, also have very limited leverage

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

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

in their negotiations with programmers. But this situation may not be particularly harmful to the telephone companies' business plans for several reasons. First, they may be less resistant to a higher per subscriber charge for access to programming than has previously prevailed in the market because they currently have very few subscribers and thus this cost represents a very small portion of their market entry costs. Their costs for programming, even if paying a premium, pale in relation to the capital investments and operating costs associated with truck rolls to customer premises needed to bring fiber or other wireline broadband technologies close to the home. Moreover, in contrast with the smaller cable companies, the telephone companies have significant revenues streams from telephone and broadband access services that contribute toward the fixed costs of their infrastructure.

The willingness of the telephone companies to pay more than the previously prevailing rates for programming and the inability of many smaller cable operators to withstand programmer demands for higher payments have adversely affected the ability of the large incumbent MVPDs — cable and satellite — to resist less favorable terms for programming, despite the countervailing market strengths that they bring to their negotiations. Although these large MVPDs have rarely had an impasse in negotiations that resulted in carriage of particular programming being disrupted, the trade press has noted very contentious negotiations and (despite contractual language requiring all parties to keep all terms confidential) evidence that the cash payments that the large cable and satellite companies are paying for popular programming are increasing.[30]

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

Consolidation and Clustering of Cable Operators

At the same time that additional distribution options have become available to video programmers, consolidation (acquisitions resulting in a small number of large firms serving an increasing portion of total subscribers, nationwide) and clustering (acquisitions resulting in individual firms serving an increasing portion of subscribers in a particular local market) are occurring among cable operators and the two major satellite operators are growing, so that the largest video distributors are serving a higher share of total MVPD subscribers than they have in the past and the large cable operators' serving areas have become increasingly concentrated into a small number of very large clusters. These trends are the result of acquisitions by the large cable

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[30] The very large cable companies appear to have been more successful than the two large satellite companies in resisting cash payments, for several reasons. Their strategy to cluster their systems in a limited number of local markets has given them high subscriber penetration in those markets, which helps in negotiations with local broadcast stations. Also, their ability to offer bundles of video, voice, and data services reduces the likelihood that subscribers will change provider based solely on the loss of a particular video program. Finally, they are negotiating from a history of not making cash payments (at least to broadcasters), and this has created an inertia that takes greater effort for the programmers to overcome.

companies of smaller cable companies, swaps among cable systems of local cable systems that have allowed single companies to become the dominant cable provider in metropolitan statistical areas or beyond, and successful market growth by the two large DBS operators, DirecTV and DISH Network. As shown in **Table 1**, which reproduces data provided in the FCC's most recent report on the status of competition in the market for the delivery of video services, since 2002 the percentage of total MVPD subscribers served by the largest MVPDs has grown and concentration in the market for the purchase of video programming, as measured by the Herfindahl-Hirschman Index,[31] has increased. These figures do not reflect the 2006 purchase by the two largest cable companies, Comcast and Time Warner, of the cable operations of Adelphia, which had been the fifth largest cable operator but fell into bankruptcy. Thus concentration is even greater today, although it is likely that the trend will be reversed as the two major telephone companies, AT&T and Verizon, continue to roll out their video service offerings, which currently are available in only a few geographic markets.

Table 1. Consolidation in the National Market for the Purchase of Video Programming (Percentage of MVPD Subscribers), 2002-2005

Largest MVPDs	2002	2003	2004	2005
Top 1	14.75%	22.69%	23.37%	22.99%
Top 2	29.04%	35.01%	35.47%	38.71%
Top 3	41.03%	46.63%	47.34%	50.99%
Top 4	50.48%	55.98%	57.97%	62.67%
Top 10	84.44%	81.95%	84.72%	88.39%
Top 25	90.26%	87.45%	90.41%	94.00%
Top 50	92.05%	89.29%	92.32%	95.73%
HHI	884	1031	1097	1201

Source: Federal Communications Commission, *In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, Twelfth Annual Report, adopted February 10, 2006 and released March 3, 2006, at p. 119, Table B-4.

Table 2 lists the 25 largest cable operators, which are often referred to as multiple system operators or MSOs, and the number of subscribers they had as of December 2006. It is noteworthy that the largest MSO, Comcast, had almost as many subscribers as numbers 3 through 25 combined.

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[31] The Herfindahl-Hirschman Index (HHI) is the most commonly accepted measure of market concentration. It is calculated by squaring the market share of each firm and then summing the resulting numbers. The higher the HHI, the more concentrated the market. The HHI can range from close to zero for a market of many tiny firms to 10,000 for a monopoly. The Department of Justice and Federal Trade Commission use the HHI when evaluating mergers. They consider a market with an HHI of 1,000 to 1,800 to be moderately concentrated and a market with an HHI of 1,800 or greater to be highly concentrated. As a general rule, if a merger in an already-concentrated market would increase the HHI by more than 100 points, that would raise antitrust concerns.

Table 2. The 25 Largest Cable Operators as of December 2006

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

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

Had the satellite operators, DirecTV and DISH Network, been included in this list, they would have ranked second and fourth, respectively.[32] But satellite operators have a somewhat different market impact because they have subscribers dispersed all around the country, while cable companies tend to cluster their systems in a limited number of geographic areas. (An individual cable cluster most likely consists of multiple cable franchises negotiated with many local jurisdictions.) In the early years of the cable industry, most of the larger firms bidding for cable franchises did not focus their efforts on narrow geographic regions. As a result, the larger cable operators tended to have cable franchise that were widely scattered geographically. Subsequently, many of these large firms traded franchises, to develop clusters in a smaller number of geographic areas. Clustering provides economies of scale in operations, marketing, and customer service. It also strengthens a cable operator's retransmission consent negotiating position with broadcasters, who are less likely to risk the foregone subscriber fees and advertising revenues from an impasse with (and discontinued signal carriage by) a cable operator if that operator serves a large portion of the broadcaster's viewing area.

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

As shown in **Table 3**, there are 113 cable clusters serving at least 100,000 subscribers. But reviewing this table in conjunction with **Table 2**, it is notable that 102 of those clusters are owned by the five largest cable operators and only two are owned by cable operators that are not among the 10 largest.

Table 3. Cable Television System Clusters Serving More Than 100,000 Subscribers, as of December 2005

Rk	Company	Basic Subs	Rk	Company	Basic Subs
1	Cablevision, New York Area	3,026,994	58	Charter, Georgia	298,900
2	Comcast, Boston, MA	1,937,802	59	Charter, Los Angeles Metro	292,500
3	Time Warner, Los Angeles	1,928,340	60	Charter, North Wisconsin	292,100
4	Comcast, Philadelphia	1,916,460	61	Charter, Northwest	286,900
5	Comcast, Chicago	1,800,000	62	Time Warner, Syracuse, NY	280,100
6	Comcast, San Francisco Area	1,654,358	63	Insight, Louisville, KY	276,400
7	Time Warner, New York	1,400,000	64	Comcast, Richmond-Petersburg	272,821
8	Comcast, Seattle, WA	1,032,013	65	Comcast, Indianapolis, IN	270,755
9	Bright House, Tampa Bay, FL	1,021,281	66	Time Warner, Rochester	264,603
10	Comcast, Washington, DC	1,000,000	67	Cox, Northern Virginia	262,000
11	Comcast, Detroit, MI	962,059	68	Comcast, Ft. Myers-Naples	259,752
12	Time Warner, Cleveland-Akron- Canton, OH	833,223	69	Time Warner, Portland-Auburn, ME	252,630
13	Bright House, Central FL	777,428	70	Charter, West Virg.	247,300
14	Cox, Middle America Cox	776,000	71	Comcast, Salt Lake City, UT	244,680
15	Cox, Arizona	773,000	72	Charter, No. Car./Virginia	239,000
16	Time Warner, Houston, TX	754,611	73	Charter, Southern Wisconsin	229,100
17	Comcast, Atlanta, GA	733,691	74	Cox, West Texas	219,000
18	Comcast, Miami, FL	740,274	75	Charter, Mid America	217,200
19	Mediacom, South Central	723,000	76	Comcast, Fresno-Visalia	208,386
20	Comcast, New York	705,736	77	Comcast, Tampa/Sarasota	203,947
21	Mediacom, North Central	698,000	78	Cox, Omaha, NE	203,000
22	Comcast, Denver, CO	666,012	79	Comcast, Memphis, TN	201,201
23	Comcast, Baltimore, MD	649,366	80	Charter, Northern Michigan	199,600
24	Comcast, Pittsburgh, PA	607,574	81	Comcast, Wheeling-Steubenville	197,660
25	Comcast, Hartford-New H, CT	546,814	82	Charter, Easter Michigan	195,700
26	Comcast, St. Paul-Minneapolis	539,627	83	Charter, Central California	190,600
27	Cox, San Diego, CA	538,000	84	Charter, West Michigan	188,900
28	Comcast, Sacramento, CA	535,294	85	Comcast, Albuquerque-Sante Fe	186,533

Rk	Company	Basic Subs	Rk	Company	Basic Subs
29	Cox, Oklahoma	501,000	86	Cox, Baton Rouge, LA	180,000
30	Charter, Tennessee/Kentucky	487,700	87	Charter, Louisiana/Miss.	168,400
31	Time Warner, Raleigh-Durham	470,809	88	Cox, Gulf Coast/Florida	168,100
32	Cox, New England	456,000	89	Charter, Ft. Worth, TX	164,700
33	Charter, St. Louis Metro, MO	452,900	90	Time Warner, Columbia, SC	163,455
34	Time Warner, Charlotte, NC	426,507	91	Comcast, Eugene, OR	161,308
35	Cox, Hampton Roads, VA	415,000	92	Comcast, Salisbury, MD	159,192
36	Time Warner, Milwaukee, WI	412,517	93	Comcast, Knoxville, TN	157,693
37	Cox, Las Vegas	410,000	94	Time Warner, Green Bay	146,501
38	Comcast, Portland, OR	398,996	95	Charter, Nevada	145,100
39	Time Warner, Hawaii	393,280	96	Atlantic Broadband, Western PA	142,935
40	Time Warner, Cincinnati, OH	388,592	97	Charter, Inland Empire	138,900
41	Time Warner, San Antonio	384,400	98	Comcast, Colorado Spr.-Pueblo	137,121
42	Time Warner, Albany, NY	380,319	99	Comcast, Chattanooga, TN	126,859
43	Comcast, Harrisbrg-Lncstr-Leb-York, PA	370,267	100	Buckeye Cable, Toledo, OH	126,150
44	Comcast, W. Palm Beach-Ft. Pierce, FL	370,216	101	Comcast, Burlington-Plattsburgh	126,013
45	Time Warner, Columbus, OH	364,608	102	Insight, Peoria, IL	123,000
46	Comcast, Gand Rapids-Kalamazoo-B.Cr, MI	362,231	103	Comcast, Roanoke-Lynchburg, VA	121,520
47	Comcast, Jacksonville, Brunswick	357,707	104	Insight, Northern Illinois	117,000
48	Charter, New England	356,200	105	Insight, Northeast Indiana	116,900
49	Charter, Alabama	350,200	106	Comcast, Orlando, FL	116,081
50	Time Warner, Greensboro, NC	348,290	107	Time Warner, Wilmington, NC	115,905
51	Comcast, Nashville, TN	327,920	108	Comcast, Savannah, GA	112,113
52	Charter, Minnesota/Nebraska	327,800	109	Insight, Springfield, IL	111,600
53	Time Warner, Austin, TX	316, 911	110	Comcast, Charleston, SC	109,506
54	Cox, Kansas	307,000	111	Time Warner, Waco-Temple-Bryan, TX	108,714
55	Charter, South Carolina	302,600	112	Comcast, Johnstown-Altoona, PA	107,800
56	Time Warner, San Diego, CA	301,656	113	Comcast, Augusta, GA	106,343
57	Time Warner, Kansas City, MO	300,317			

Source: Kagan Research, *Broadband Cable Financial Databook*, 26th edition, 2006, at pp. 27-28.
Note: Pro forma Comcast/Time Warner acquisition of Adelphia Communications.

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

Negotiating with a cable program network.

Cable program networks get approximately half their revenues from per subscriber fees imposed on MVPDs and half from advertising.[33] And those advertising fees depend on the number of subscribers reached, so the more subscribers an MVPD reaches, the more valuable that MVPD is to the program network. Cable program networks that fail to achieve substantial penetration on MVPD systems face financial peril. In recent proceedings at the FCC, parties have filed comments asserting that in order to generate the advertising revenues necessary for success, a national program network must reach between 40 and 60 million, and perhaps as many as 75 million, subscribers.[34] Carriage on the major MVPD systems — Comcast, Time Warner, DirecTV, and DISH Network — therefore is key to cable program network success. Cable program network business strategies therefore focus on obtaining and retaining such carriage. For a new cable program network, that might involve giving one of the major MVPDs an equity interest in exchange for carriage. For an established cable network with a strong brand identity, that might involve creating a sister network and demanding MVPDs to carry the new network in lieu of cash for carriage of the established network. But even an established program network is unlikely to risk a negotiating impasse that results in discontinued carriage by any of those large MVPDs.

As shown in **Table 4**, the 20 most widely distributed advertiser-supported cable program networks each are available to more than 90,000,000 households vias MVPD subscription. Comparing **Table 2** to **Table 4**, it is clear that the cable program networks that have achieved penetration rates of 90,000,000+ enjoy carriage on each of the four largest MVPD systems — the systems of the two largest cable operators as well as on the systems of the two major DBS operators.[35] As shown in **Table 2**, subscriber reach falls quite quickly beyond those large MVPDs. While cable program networks will seek carriage on all MVPDs, as the subscriber reach of

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[33] See footnote 24 above.

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

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

the MVPD falls, the financial risk to a cable program network provider of failing to reach a carriage arrangement with the MVPD falls. This may make it easier for the cable network provider to push harder for a high per subscriber fee from a smaller MVPD. From the perspective of a small or mid-sized cable operator, however, failing to reach a carriage arrangement for a relatively popular cable program network that is carried by DirecTV and/or DISH Network can be risky. Thus, a cable operator's negotiating position vis-a-vis cable network programmers will be strengthened by consolidation.

Table 4. Cable Program Networks with the Largest Number of Subscribers, as of December 2006

Rank	Network	Subscribers	Rank	Network	Subscribers
1	Discovery	92,500,000	10	A&E	91,800,000
2	ESPN	92,300,000	12	TBS	91,700,000
2	CNN	92,300,000	12	Learning Channel	91,700,000
4	TNT	92,100,000	12	Spike TV	91,700,000
4	Lifetime	92,100,000	15	CNN Headline News	91,500,000
4	USA	92,100,000	16	ABC Family Channel	91,300,000
7	Weather Channel	92,000,000	16	MTV	91,300,000
8	Nickelodeon	91,900,000	18	Home and Garden	91,200,000
8	History Channel	91,900,000	19	Food Network	91,100,000
10	ESPN2	91,800,000	19	Cartoon Network	91,000,000

Source: Table prepared by National Cable and Telecommunications Association based on data from Kagan Research, LLC, available at [http://www.ncta.com/ContentView.aspx? contentId=74], viewed on June 28, 2007.

Negotiating with a national broadcast network.

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

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

The negotiating dynamic may be quite different when a broadcast station is conducting its own negotiations with MVPDs — which appears to be happening more often these days. In this situation, the broadcaster's reach is limited to the local market (DMA) in which its station is located or, in the case of a station that is part of a non-network broadcast group, the local markets in which the group has stations. Its concern will not be with the total subscriber reach of the MVPDs with which it is negotiating, but rather with the subscriber reach of those MVPDs within the local markets in which the group has stations. DBS operators are likely to offer service in many or all of those markets, but an individual cable company, even one as large as Comcast or Time Warner, is unlikely to operate in all those local markets. What becomes most important, then, is whether the cable company is clustered in the market or markets in which the broadcaster has stations. Comparing the subscriber reach of cable clusters presented in **Table 3** to the populations of the markets covered by those clusters, it is clear that there are many cable clusters that serve a substantial portion of the households in the local broadcast markets in which they are located. In these situations, the local broadcasters are less likely to risk a negotiating impasse with the clustered cable company and therefore likely to face constraints on the demands they can make for retransmission consent compensation.

Charter Communications CEO Neil Smit has stated that actions it has taken to increase the densities of its existing clusters have strengthened its position in retransmission consent negotiations, making it more difficult for station groups to play hardball given that they would put greater portions of their ad revenues at stake.[36] One industry observer has described this negotiating situation as follows:

> Cable operators have more clout than telcos and even DBS. Cable operators are big enough in major markets to take a broadcaster dark in 60%-80% of local homes overnight. That would guarantee immediate pain as major advertisers cancel. But a DBS operator might serve just 10%-20% of local homes so it can inflict far less pain. Telcos are in the weakest position.[37]

More Program Networks/Fragmented Audiences

Another major structural market change has been the dramatic expansion in the number of program networks (sometimes referred to as channels) available to consumers, with a resulting fall in average audience size per channel. As shown in **Table 5**, the number of video channels received by the average U.S. household increased from 18.8 channels in 1985 to 104.2 channels in 2006, but neither the number of television households nor the average household viewing time per day increased nearly so dramatically during that period. Thus the average audience size

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

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

per program network has fallen substantially. Although the rapid growth in the number of channels received by the average household has slowed in recent years, channel availability continues to grow faster than total viewing hours. Moreover, even the largest MVPD networks, which offer customers more than 200 channels, cannot carry all available cable networks, which now number more than 500 national networks as well as numerous regional networks.[38]

Table 5. Nielsen Data on Total Television Households, Time Spent Viewing Per Household, and the Average Number of Video Channels Received Per Household, 1985-2006

Year	Average Number of Video Channels Received	Television Households in the U.S. (millions)	Time Spent Viewing Television, Per Day, Per Household
2006	104.2	110.2	8 hrs 14 mins
2005	96.4	109.6	8 hrs 11 mins
2004	92.6	108.4	8 hrs 01 mins
2000	61.4	100.8	7 hrs 35 mins
1995	41.1	95.4	7 hrs 17 mins
1990	33.2	92.1	6 hrs 53 mins
1985	18.8	84.9	7 hrs 10 mins

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

This proliferation in program networks has had two general market implications. On the one hand, the typical program network has an audience share of less than 1%, and unless its programming has very strong appeal to a subset of subscribers who would be willing to pay separately for that programming, is not likely to command much compensation from MVPDs for carriage rights. It may well be that if such a program network is not affiliated with an MVPD or with a major programmer it will have to rely on the commercial leased access rules and pay to gain access to an MVPD.[39]

On the other hand, the relatively few program networks that attract larger audiences are valuable to MVPDs for two reasons. First, a program network that attracts a larger audience is, other things equal, likely to have more viewers who

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[38] National Cable and Telecommunications Association, *2007 Industry Overview*, at p. 7, available at [http://i.ncta.com/ncta_com/PDFs/NCTA_Annual_Report_04.24.07.pdf], viewed on June 27, 2007.

[39] See footnote 14.

might choose among competing MVPDs based on the availability of that network's programming; there is greater business risk to MVPDs not to carry that program network. Second, larger audiences tend to attract more advertising revenues for the MVPD.

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

Some program networks, however, remain extremely valuable to MVPDs and, in fact, in some ways network proliferation has increased the value of these networks, even if their audience share has shrunk over time. **Table 6** shows that although the major broadcast networks' share of U.S. television household usage has fallen substantially over time, they continue to capture relatively large audiences. More than 25% of all television usage (including usage to watch VCRs and to play video games) is spent viewing the national programming offered by the four major broadcast networks and the local and syndicated programming offered by those networks' local broadcast station affiliates, and that is projected to continue to approach 25% of all usage at the end of the decade. Since both the national programming and the local programming offered by these major network affiliates attract such relatively large audiences, an MVPD in a market where there is competition from other MVPDs could find itself at risk of losing substantial numbers of subscribers if a contract negotiation impasse resulted in it not carrying the programming of one of those affiliates.[41] Interestingly, recent reports that the four major broadcast networks lost 2.5 million viewers during the spring of 2007 specifically raised the impact that this might have on the advertising rates charged by the networks, but did not address the potential impact on the broadcast networks' negotiations with MVPDs.[42]

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

[41] As will be discussed below, where a broadcaster owns or controls two major network affiliated stations in a local market, it is likely to wield significant leverage in retransmission consent negotiations with local cable systems because the latter would not want to risk losing carriage of the programming of two major networks and two local stations.

[42] See, for example, David Bauder, "Data Says 2.5 Million Less Watching TV," Associated Press wire, May 8, 2007.

Table 6. Estimated Share of U.S. Television Home Set Usage by Program Source (%)

Source	Early 1950s	Early 1960s	Early 1970s	Early 1980s	Early 1990s	Early 2000s	Mid 2000s	Late 2000s
ABC/CBS/ NBC	60	58	55	49	31	19	17	15
DuMont	4	—	—	—	—	—	—	—
Fox/WB/ UPN/Paxnet	—	—	—	—	2	4	5	5
Network Affiliates	30	29	25	23	18	10	7	6
Independent Stations	6	11	16	20	16	12	11	10
PBS Stations	—	2	4	3	3	3	2	2
Pay Cable	—	—	—	4	4	5	4	4
Ad-Supported Cable	—	—	1	3	20	38	44	48
Other Cable	—	—	—	—	1	3	4	4
VCR Play	—	—	—	—	5	5	3	3
Video Games	—	—	—	1	1	2	3	3
Average Hours of Set Usage Weekly	35	39	46	51	55	63	65	67

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

The data in **Table 7** on the cumulative weekly reach of various program networks also show the breadth of viewership enjoyed by the major broadcast networks. In any given week *each* of the four major networks is viewed (for at least one ten-minute segment) by more than 70% of all U.S. television households, almost double the viewership of the largest cable network.[43]

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

Table 7. The Average Weekly Cumulative Audience Reach of the Largest Broadcast and Cable Program Networks, First Quarter 2007

Program Network	Average Weekly Cumulative Market Reach
Broadcast Networks	
CBS	74.5%
NBC	72.8%
ABC	72.6%
FOX	70.6%
CW	44.1%
MNT	29.8%
Cable Networks	
USA	37.7%
TBS	37.1%
TNT	36.6%
A&E	29.5%
FX	28.9%
DISCOVERY	28.2%
LIFETIME	27.2%
COMEDY CENTRAL	27.2%
NICKELODEON	26.9%
SPIKE	26.8%
HISTORY	26.7%
AMC	25.9%
ESPN	25.1%

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

Moreover, the four major broadcast networks provide almost all of the most popular television programs. As shown in **Table 8**, during the 2005-2006 television season, the 100 individual television programs with the largest audiences all were major broadcast network programs. Although other broadcast programmers provided shows that ranked among the second one-hundred in ratings, the highest-rated advertiser-supported cable network program was ranked 236, the second highest-rated cable network program was ranked 389. This table slightly overstates the dominance of broadcast programming because it does not include premium cable programming, such as The Sopranos, which despite seeing its audience size fall from

a high of 13 million households for some episodes in 2002 to 9 million household for some episodes in 2006, still would have had some episodes among the 100 most highly watched programs.[44] Nonetheless, and despite the recent fall in the major broadcast networks' audiences, for the foreseeable future those broadcast networks are likely to continue to provide the lion's share of the most popular television programs.

Table 8. The Individual Television Programs with the Largest Audience Ratings, 2005-2006 Television Season

RK	PROGRAM	NW	%	RK	PROGRAM	NW	%
1	SUPER BOWL XL (6:26P)	ABC	41.62	56	WNTR OLYM FRI PRIME 2	NBC	9.74
2	ACADEMY AWARDS	ABC	23.08	57	TWO AND A HALF MEN	CBS	9.73
3	ROSE BOWL	ABC	21.71	58	WNTR OLYM SAT PRIME 3	NBC	9.68
4	FOX NFC CHAMP (6:47P)	FOX	20.77	59	FOX NFC CHAMP-POST	FOX	9.64
5	AMERICAN IDOL-TUESDAY	FOX	17.72	60	DANCING W STARS RSLTS	ABC	9.57
6	AMERICAN IDOL-WEDNESDAY	FOX	17.24	61	DEAL OR NO DEAL-MON	NBC	9.48
7	AFC DIVISIONAL PLAYOFF- SA	CBS	16.14	62	FOX WORLD SERIES GAME 1	FOX	9.47
8	DANCING WITH STARS-2/26	ABC	16.02	63	CSI: THU 8P SPECIAL	CBS	9.47
9	WNTR OLYM THU PRIME 2	NBC	15.77	63	CSI MIAMI SPECIAL	CBS	9.47
10	CSI	CBS	15.68	65	FOX MLB NLCS GAME 6	FOX	9.41
11	AMERICAN IDOL THU SP-3/9	FOX	15.52	66	COLD CASE	CBS	9.36
12	WNTR OLYM TUE PRIME 2	NBC	15.48	67	LOST	ABC	9.29
13	AMERICAN IDOL THU SP-3/2	FOX	15.29	68	BARBARA WALTERS PRES	ABC	9.28
14	CSI - THANKSGIVING	CBS	14.62	69	CSI-THU 8P SPECIAL	CBS	9.26
15	GREY'S ANATOMY SP 2-5/15	ABC	14.23	70	CSI: MIAMI - SPCL	CBS	9.25
16	AFC/NFC PLAYOFF GM2	ABC	13.95	71	CSI: NY	CBS	9.24
17	DESPERATE HOUSEWIVES	ABC	13.86	71	LAW AND ORDER: SVU	NBC	9.24
18	WNTR OLYM MON PRIME 2	NBC	13.59	73	DESTINATION LOST	ABC	9.22
19	WNTR OLYM PRIME 1	NBC	13.46	74	SURVIVOR: PANAMA-EX FIN	CBS	9.21
20	AMERICAN IDOL THU SP-2/23	FOX	13.38	75	SURVIVOR: GUAT REUNION	CBS	9.18
21	WNTR OLYM SUN PRIME 1	NBC	13.3	76	FOX MLB LCS: GMS 1&2	FOX	9.1
22	FOX WORLD SERIES GAME 4	FOX	12.96	77	DEAL OR NO DEAL - WED	NBC	9.04
23	WNTR OLYM MON PRIME 1	NBC	12.86	78	SUGAR BOWL	ABC	8.99
24	WNTR OLYM OPEN CEREM	NBC	12.81	79	60 MINUTES	CBS	8.97
25	GREY'S ANATOMY	ABC	12.58	80	BARBARA WALTERS PRES	ABC	8.96
26	CRIMINAL MINDS PREVIEW SP	CBS	12.48	81	FOX MLB DIV: AL GM 5	FOX	8.95
27	GOLDEN GLOBE AWARDS	NBC	12.46	82	24 PRVW SP-1/15 9P	FOX	8.94
28	WITHOUT A TRACE	CBS	12.38	83	WNTR OLYM CLOSE CEREM	NBC	8.88
29	ORANGE BOWL	ABC	12.25	84	HOUSE SP-2/20 8P	FOX	8.83
30	DANCING WITH THE STARS	ABC	11.98	85	CSI THU 8P-SPECIAL	CBS	8.75
31	WITHOUT A TRACE-THANKS	CBS	11.93	86	TWO AND A HALF MEN SPL	CBS	8.74
32	WNTR OLYM THU PRIME 1	NBC	11.92	87	ABC PREMIERE EVENT-4/10	ABC	8.68

[44] The Television Advertising Bureau, which tabulates these ratings based on data collected by Nielsen, explains that it does not include ratings data for the premium cable programs because those programs are aired multiple times in a week, but the Nielsen data are presented as the average audience, per showing, and therefore fails to measure the audience size for the initial showing of each episode.

RK	PROGRAM	NW	%	RK	PROGRAM	NW	%
33	CSI: MIAMI	CBS	11.88	88	WILL & GRACE CLIP SPCL	NBC	8.57
34	SURVIVOR: GUATEMALA FIN	CBS	11.85	90	RUDOLPH-RED NOSE-RNDEER	CBS	8.57
35	WNTR OLYM SUN PRIME 2	NBC	11.6	90	NCIS 9P SPECIAL	CBS	8.56
37	WNTR OLYM SAT PRIME 2	NBC	11.33	92	EXT MAKEOVER: HOME ED.	ABC	8.56
37	WNTR OLYM WED PRIME 1	NBC	11.27	93	CSI: MIAMI - SPECIAL	CBS	8.55
38	WNTR OLYM FRI PRIME 1	NBC	11.27	93	LOST SP-1/11	ABC	8.53
39	WNTR OLYM TUE PRIME 1	NBC	11.26	95	COLD CASE-SPECIAL	CBS	8.53
40	CBS NCAA BSKBL CHAMP	CBS	11.17	96	CHARLIE BRWN CHRISTMAS	ABC	8.51
41	CMA AWARDS	CBS	11.08	97	24 PRVW SP-1/16	FOX	8.49
42	FOX WORLD SERIES GAME 2	FOX	11.06	98	CROSSING JORDAN 4/16	NBC	8.45
43	FOX WORLD SERIES GAME 3	FOX	11.01	99	DEAL OR NO DEAL 12/21	NBC	8.4
44	GRAMMY AWARDS	CBS	10.95	99	TWO AND HALF MEN-SPCL	CBS	8.39
45	SURVIVOR: GUATEMALA	CBS	10.87	99	COMMANDER IN CHIEF	ABC	8.39
46	OSCAR COUNTDOWN 2006 PT 2	ABC	10.86	**236**	**NFL REGULAR SEASON L**	**ESPN**	**5.66**
47	HOUSE SP-5/3 8P	FOX	10.6	**389**	**MLB DIVISIONAL SERIES L**	**ESPN**	**4.43**
47	HOUSE	FOX	10.6	**419**	**2006 NBA ALLSTAR GAME**	**TNT**	**4.26**
49	SURVIVOR: GUATE THNKSGV	CBS	10.59	**476**	**STATE OF THE UNION 2006**	**FXN**	**3.8**
49	NFL MON NIGHT FOOTBALL	ABC	10.16	**487**	**S JIMMY TIMMY PWRHR2**	**NICK**	**3.73**
51	24 PRVW SP-1/15 8P	FOX	9.99	**49**	**NBA PLAYOFF-CONF FINALS L**	**ESP**	**3.6**
52	WNTR OLYM WED PRIME 2	NBC	9.79	**526**	**S KIDS CHOICE 06**	**NICK**	**3.51**
53	NCIS	CBS	9.77	**562**	**WWE ENTERTAINMENT**	**USA**	**3.28**
54	UNIT, THE	CBS	9.76	**569**	**FOP MOVIE FAIRY IDOL**	**NICK**	**3.21**
55	SURVIVOR: PANAMA-EXILE IS.	CBS	9.75	**586**	**NBA ALLSTAR SAT NIGHT**	**TNT**	**2.94**

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

Table 8 highlights another key factor in programmer-distributor negotiations. There often is a timing element to must-have programming that programmers can use strategically in their negotiations with distributors. Television households are far more likely to switch MVPD providers if they fear the loss of particular time-sensitive programming, such as the Super Bowl, the Olympic Games, the National Football League season, or the finale of American Idol or some other extremely popular series. Some programmers have effectively timed their negotiations with distributors to take advantage of such program schedules.[45] In some cases, programmers with the rights to sports events have agreed to month-to-month extensions of lapsed agreements with MVPDs until a time when a key sports event was imminent and then used the threat of lost access to that sports event as leverage to complete a more favorable distribution agreement with the MVPDs.[46]

Table 7 shows that, despite the dominance of the four major broadcast networks, at least a dozen cable networks have succeeded in attracting more than

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

[46] Id.

25% of all television households for at least one 10-minute segment each week. Not surprisingly, these cable networks generally have been able to command larger than average per subscriber fees from MVPDs, as shown in **Table 9**. Those networks commanding high per subscriber license fees that did not have broad reach into households tended to fall into one of two categories — sports networks or news networks — that have unique demand characteristics.[47]

Table 9. The Advertiser-Supported Cable Networks with the Highest Average License Fees Per Subscriber Per Month, 2005

Network	Monthly Fee	Network	Monthly Fee
ESPN	2.60	Discovery	0.24
Fox Sports	1.68	ESPN2	0.23
TNT	0.86	AMC	0.22
Disney Channel	0.78	ABC Family	0.22
USA	0.45	A&E	0.21
CNN	0.44	Golf Channel	0.21
Nickelodeon	0.40	Independent Film	0.21
NBA TV	0.34	Lifetime	0.21
Sundance	0.29	Fox Soccer	0.20
TBS	0.29	E!	0.19
Turner Classic Movies	0.28	NFL Network	0.19
MTV	0.28	Natl. Geographic	0.19
FX	0.27	Spike TV	0.18
Fox News	0.25	History Channel	0.18
CNBC	0.25		

Source: Kagan Research, *Economics of Basic Cable Networks, 2006*, 12th Annual Edition, 2005, at p. 58.

The proliferation of program networks may be having another market impact. In the early and mid 1990s, the average U.S. television household received 41 channels; with the lesser audience fragmentation that existed then, a larger proportion of networks could expect to capture enough audience share to be profitable. The key strategic element was to gain a threshold penetration level on basic cable tiers. With such penetration, there was a reasonable chance to become profitable. Thus one strategy attractive to large programmers whose existing programming had already gained some brand identity was to introduce additional program networks under the

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

corporate brand umbrella, such as Disney, Discovery, ESPN, or Fox. Since then, the increase in the number of channels available to households and continued competitive entry by new program networks has resulted in more and more video networks being only marginally profitable; most program networks do not generate revenues in excess of production costs and the likelihood of a new program network proving very popular and profitable is diminishing. This may be constraining the incentive, which has been strong in the past, of large programmers to introduce additional program networks, sometimes even when they can use their entrenched successful networks to cross-market their new networks.[48] Thus, although it has been common for distributors to compensate a programmer for carriage of that programmer's popular programming by agreeing also to carry the programmer's new program networks, that is becoming a less attractive form of compensation unless the programmer has an extremely strong brand identity to exploit. It appears that increasingly a more attractive alternative is for the programmer to extract the value from its popular programming directly, by demanding cash payment from distributors for carriage of that popular programming.

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

> And during the past several years, the "Big Four" networks have renegotiated affiliate deals to eventually eliminate once-lucrative network compensation fees paid to stations to carry programming from ABC, CBS, Fox, and NBC.
>
> Perhaps not coincidentally, those fees began to decline precipitously in 2005, right around the time that retransmission consent revenue [for the affiliate stations] began to rise. For example, in 2005, network compensation at Hearst-Argyle fell 35.9% from $28.8 million to $19.1 million and dipped another 48.7% in 2006 to $9.8 million.
>
> At Nexstar, network compensation dipped 22.4% in 2005, to $6.6 million, and fell 36.4% to $4.2 million in 2006. At Sinclair, the drop-off was less dramatic — 7% in 2005, from $14.3 million to $13.3 million (the company has not yet

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[48] However, despite the fact that most advertising-supported cable network are not able to command substantial per subscriber fees from MVPDs, in *The Economics of Basic Cable Networks, 2006*, 12th Annual Edition, 2005, at p. 3, Kagan Research concluded:

> There's no question why so many want to enter this business — the economics are very attractive if one is successful. The industry posted an estimated $9.0 billion in cash flow in 2004, with an enviable margin of 34.1%.

> released 2006 network compensation) — but the station owner expects more dramatic declines in the coming years.
>
> In its 2005 annual report, Sinclair even went so far as to say that retransmission consent fees have "replaced the steady decline in revenues from television network compensation."[49]

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

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

Most cable operators have upgraded their systems over the past decade and now are able to offer a wide array of services over their broadband networks, including high speed data, telephone, and digital video services, as well as traditional analog video services. As shown in **Table 10**, the revenue base of the cable system operators is diversifying, with fastest growth occurring in high speed data, telephone, and digital tier video services. Most subscribers who select these newer services purchase them as part of a bundled package with basic cable service. This trend is helping cable operators in their negotiations with programmers in two ways. First, subscribers who purchase service bundles are less likely to switch to a competing MVPD if their current provider were to lose carriage of a particular program network, even a popular network. This is particularly the case if the competing MVPD cannot offer the full array of services that the cable company does; for example, satellite companies often cannot offer high speed data and telephone services at a price or uplink speed that is competitive with cable companies. Second, if a cable company

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

is enjoying rapid revenue growth from non-video services, it may be more willing to hold the line in its negotiations with programmers because it is easier to absorb a potential loss of video revenues stemming from an impasse and loss of program carriage when other revenues are growing. On the other hand, the additional revenues generated by these "triple play" offerings may allow a cable operator to pay more for programming.

Table 10. Cable Company Revenues, by Service, 1996-2005, in Millions of Dollars

Year	Basic Service	Premium Channels	Digital Tier	High Speed Data	Telephone Service	Net Local Advertising	Miscellaneous
1996	18,249	4,359	0	—	—	1,413	1,894
1997	20,213	4,616	3	—	8	1,636	2,164
1998	21,574	4,858	98	103	26	1,898	2,333
1999	22,732	5,025	443	386	78	2,267	2,850
2000	24,142	5,259	588	751	275	2,447	2,968
2001	26,324	5,756	1,763	1,870	713	2,431	3,049
2002	27,690	5,963	2,693	4,525	1,265	2,800	3,359
2003	29,000	5,891	3,396	6,772	1,499	2,851	4,237
2004	30,080	6,225	3,966	8,965	1,623	3,236	5,091
2005	31,075	6,389	4,563	11,245	2,158	3,381	6,514

Source: Kagan Research, *Broadband Cable Financial Databook*, 26th Edition, 2006, at p. 8. Miscellaneous revenues include commercial revenue, pay-per-view, advanced analog, home shopping, equipment charges, home networking, pay installation, NVOD, VOD/SVOD, interactive, games, DVRs, and high definition services.

There has been an interesting market response to the growth in cable system revenues from non-video services. As these new revenue sources have increased the average revenue generated per subscribing household (known in the industry as average revenue per unit, or ARPU), the value of existing cable systems has grown and this has been reflected in the price per subscriber at which cable systems have been sold. This, in turn, has affected at least one programmer-distributor negotiation. On July 1, 2006, Suddenlink Communications completed the purchase from Charter Communications of cable systems in West Virginia with 240,000 subscribers, 200,000 of whom live in the Charleston, WV service area of a Sinclair Broadcast Group-owned television station (WCHS, an ABC affiliate) and another television station (WVAH, a Fox affiliate) for which Sinclair has a local marketing agreement. The retransmission consent agreement between Charter and Sinclair had expired prior to the Suddenlink purchase,[50] so Suddenlink entered retransmission consent

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[50] See Mike Farrell, "Suddenlink, Sinclair in Retrans Clash," *Multichannel News*, July 5, 2006, available at [http://www.multichannel.com/index.asp?layout=articlePrint (continued...)

negotiations with Sinclair before the purchase was completed. Sinclair had sought $4 million in cash payments over three years. But when Sinclair learned that the purchase price was $800 million, it raised its demand to more than $42 million. Sinclair's vice president and general counsel reportedly stated that, "If they're paying $3,200 per sub[scriber], why shouldn't a piece of that be coming to us?"[51] This raises an interesting issue. To the extent the high cable system valuation is a function of the programming provided by Sinclair, Sinclair would seem to have a strong claim for larger cash payments. But to the extent the valuation is not related to Sinclair's programming, if Sinclair were nonetheless able to command larger cash payments that might suggest that the current retransmission consent process may be allowing programmers to siphon off funds that might, from a public policy perspective, be better left to cable operators to expand their broadband infrastructure capabilities.

Specific Examples of Programmer-Distributor Conflicts

As early as 2005, broadcasters announced their intentions to receive cash payments from MVPDs for retransmission of their broadcast signals that are comparable to the payments MVPDs make for cable program networks.[52] It generally has not been the mega-programmer broadcast networks (that also own cable networks) that have been most aggressive in the pursuit of cash payments; rather it has been the larger non-network station groups (such as Sinclair, Nexstar, and Belo) and the lone broadcast network that no longer has cable network interests (CBS was spun off from Viacom in 2005, with the latter retaining such cable networks as MTV). In the past two years, despite the confidentiality under which contracts are negotiated, parties have frequently reported to the trade press the difficulties they were having in their on-going negotiations. This section does not attempt to provide an exhaustive recitation of recent programmer-distributor conflicts. Rather, it presents five exemplary cases in an attempt to reflect how the market currently is operating and explore the factors (including federal rules) that tend to influence negotiations.

Nexstar: The First Broadcaster to Aggressively Seek Cash Payments for Retransmission Consent

In January 2005, Nexstar Broadcasting Group, which owns and operates 27 stations in medium sized markets, and provides management, sales, and other services to an additional 15 stations owned by Mission Broadcasting, sought a monthly 30 cents per subscriber cash payment fee from Cox Communications and

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[50] (...continued)
&articleID=CA6349903], viewed on June 27, 2007.

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

[52] See, for example, Linda Moss, "MSOs See Rough Road to Retransmission Deals," *Multichannel News*, July 25, 2005, at p. 1, and Tania Pancyk-Collins, "Viacom Plans Carriage Fees for CBS Programming," *Communications Daily,* September 16, 2005, at p. 7.

Cable One (the fourth and tenth largest cable operators, respectively), for the right to retransmit the signals of each of the Nexstar/Mission broadcast stations in the Cox and Cable One franchise areas. Cox filed a complaint with the FCC on January 19, 2005, alleging that Nexstar and Mission refused to budge from their cash demands and therefore had not negotiated in good faith.[53] Cox alleged that Nexstar was demanding that Cox pay $8.9 million for the next three years "for the privilege of retransmitting the signals of 5 television stations that are free over-the-air in these communities." Cox sought an expedited Commission order setting relief and sanctions and requiring that the parties resume negotiations.[54] Nexstar responded that Cox was refusing to consider making any cash payments.[55]

When it filed the petition, Cox had already been required to discontinue carrying KLST, the CBS affiliate in San Angelo, TX, and KRBC, the NBC affiliate in Abilene, TX, on Cox cable systems with 72,500 customers, and if there were no agreement by the end of January 2005, Cox systems with 45,230 customers would be forced to stop carrying KSNF, the NBC affiliate in Joplin, MO, KODE, the ABC affiliate in Joplin, and KTAL, the NBC affiliate in Shreveport, LA-Texarkana, TX. When it had to discontinue carriage of the broadcast stations, Cox provided the HBO Family networks in their place.

Nexstar had grown rapidly through acquisitions earlier in the decade, but lost more than $140 million between 2001 and 2005 and was trying to pay down $600 million in debt, which was greater than its revenues over those four years.[56] Nexstar's chief operating officer, Duane Lammers, reportedly stated that his company faced costs associated with the digital transition and if cable companies take his stations' signals and resell them to viewers, "it's only fair we get a piece."[57]

On February 2, 2005, Cox prevented the loss of carriage of the two Joplin, MO broadcast stations for which the retransmission agreement had expired by using a "management reorganization" that combined the Missouri systems with Kansas systems and folded them into a retransmission agreement for its Kansas cable systems.[58] But Cox did lose carriage of Nexstar's KTAL station in Shreveport-Texarkana on February 1, 2005. Moreover, Bossier City, LA City Attorney James

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[53] After the fact, the Nexstar position was described in *Broadcasting & Cable* as "a take-it-or-leave-it demand: Pay 30¢ monthly per subscriber, or we'll yank our signals." See John M. Higgins, "Cable, Broadcast Battles End," *Broadcasting & Cable,* February 6, 2006, available at http://www.broadcastingcable.com/index.asp?layout=articlePrint&articleID=CA6304947], viewed on June 27, 2007.

[54] Anne Veigle, "Cox Asks FCC to Order Nexstar to Retransmission Negotiating Table," *Communications Daily*, January 21, 2005, at pp. 4-5.

[55] "Mass Media Notes," *Communications Daily,* February 2, 2005, at p. 9.

[56] "Texas broadcaster pulls stations off cable," *BroadcastEngineering*, January 23, 2005, available at [http://broadcastengineering.com/news/texas-cable-broadcaster-20050123/], viewed on June 27, 2007.

[57] Id.

[58] Anne Veigle, "Cox Maneuver Puts TV Stations Back on Cable," *Communications Daily*, February 3, 2005, at pp. 4-5.

Hall sent Cox a letter threatening legal action unless KTAL were restored to cable carriage, claiming that not providing KTAL "is a violation of the franchise agreement between the City of Bossier City and Cox Communications."[59]

The dispute in Joplin also involved Cable One, which lost carriage of the two Nexstar broadcast stations on January 1, 2005. The dispute benefitted satellite operators, who reported a big upsurge in service orders; Express Cellular & Satellite in Joplin reported an increase from approximately four installations a day to 20.[60]

Both Cable One and Cox responded to the lost carriage of the Nexstar broadcast stations by holding special events at which they gave away old fashioned "rabbit-ear" television antennas that would allow their subscribers to receive the Nexstar signals free over-the-air. Cox said it handed out 800 antennas in Abilene, TX, and 2,800 in San Angelo, TX. Cox also said that it had lost 1,000 subscribers (out of a total of 105,000 subscribers) during the period the Nexstar stations — all affiliates of major broadcast networks — were removed from its cable systems.[61]

According to the trade press, with the loss of cable carriage, Nexstar stations' ratings plunged and their advertising revenues fell accordingly.[62] Nexstar acknowledged losing several million dollars in revenues. With all three parties harmed by the impasse, after 10 months, on October 20, 2005, Cox, Nexstar and Mission signed a retransmission consent agreement for analog and digital carriage rights, covering 12 Nexstar and 9 Mission station serving Abilene-Sweetwater, San Angelo, Lubbock, Amarillo, Odessa-Midland, and Beaumont-Port Arthur, TX, Shreveport, LA, Fort Smith, Little Rock, and Monroe-El Dorado, AK, Springfield and Joplin, MO, and Pittsburg, K[63]S. The agreement allowed Cox to again carry KLST/CBS in San Angelo; KTAL/NBC in Bossier City and Minden, LA, and in Magnolia, AK and Mt. Pleasant, TX; and KRBC/NBC (a Mission station) in Abilene, Sweetwater, and Snyder, TX. These stations had been removed from the Cox lineup in January 2005.

The FCC did not act upon the Cox complaint during the 10 months that the negotiating impasse resulted in the Nexstar stations not being carried on the Cox systems. When the new retransmission consent agreement was reached, the FCC dismissed the complaint as moot.

The terms of the retransmission consent agreement between Cox and Nexstar were not disclosed, but industry executives say Cox and Cable One did not pay the straight license fees Nexstar was demanding; rather they agreed to buy a certain

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[59] Id.

[60] Id.

[61] "Cox Tries a Rabbit Punch," *Broadcasting & Cable*, February 21, 2005, at p. 8.

[62] John M. Higgins, "Cable, Broadcast Battles End," *Broadcasting & Cable*, February 6, 2006, available at [http://www.broadcastingcable.com/index.asp?layout=articlePrint&articleID=CA6304947], viewed on June 28, 2007.

[63] "Cox Communications, Nexstar Broadcasting and Mission Broadcasting Reach Retransmission Consent Agreement," *Business Wire*, October 20, 2005.

amount of advertising on the Nexstar broadcast stations.[64] But smaller cable operators appear to have capitulated to Nexstar's willingness to go dark. At the end of 2005, Nexstar reached a number of retransmission consent agreements with these smaller cable operators that Nexstar said included cash payments. DBS operators already had agreed to make cash payments because they needed the local broadcast signals to be able to compete with cable. In February 2006, Nexstar CEO Perry Sook said the company expected to collect around $12 million per year from its recent round of negotiations with cable and DBS operators.[65] It was estimated that 15 to 20% of those revenues came from satellite companies and about 30% of those revenues were in the form of payments for advertising.

Nexstar reported a huge increase in retransmission consent revenues from cable and satellite companies in 2006. CEO Sook reportedly said these revenues were $13.7 million in 2006, nearly five times the $2.8 million the broadcaster recorded in 2005.[66] Of that 2006 revenue, $8.7 million was cash compensation and $5 million was from advertising agreements. The revenues came from agreements struck with 150 cable operators, DISH Network, DirecTV, and all the overbuilders in its territories. Sook said the company expects these revenues to increase in 2007 from agreements with telephone companies, the expansion of the satellite local-into-local service, and escalator clauses in existing agreements with cable operators. He said many existing Nexstar retransmission consent agreements expire in 2008 and 2009, which will provide an opportunity to further increase retransmission consent revenues then.

Nexstar appears to have succeeded in its strategy of suffering short-term advertising revenue losses in order to create the precedent of obtaining cash payments from MVPDs for carriage of its broadcast signals. It is possible that this strategy could work because there was little overlap between the mid-sized cities it served and the generally larger cities served by the two most formidable cable companies — Comcast and Time Warner.

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[64] John M. Higgins, "Cable, Broadcast Battles End," *Broadcasting & Cable*, February 6, 2006, available at [http://www.broadcastingcable.com/index.asp?layout=articlePrint&articleID=CA6304947], viewed on June 28, 2007.

[65] John M. Higgins, "Cable, Broadcast Battles End," *Broadcasting & Cable*, February 6, 2006, available at [http://www.broadcastingcable.com/index.asp?layout=articlePrint&articleID=CA6304947], viewed on June 28, 2007.

[66] Mike Farrell, "Nexstar: Retrans Revenues Up," *Multichannel News*, March 1, 2007, available at [http://multichannel.com/index.asp?layout=articlePrint&articleID=CA6420695], viewed on April 20, 2007.

CBS: The Only Major Broadcast Network to Aggressively Seek Cash Payments for Retransmission Consent

In 2005, when it still owned the CBS and UPN networks but had already announced plans to spin off its broadcast assets, Viacom publicly announced its intention to obtain the same retransmission fees from cable operators for carriage of its broadcast networks as it received for carriage of its USA cable network; this would have made it the first broadcast network owner to receive cash payments.[67] Industry observers indicated that CBS might be able to do this because in its retransmission consent negotiations, post-spin off, when it no longer had cable program networks, it would not have to consider the impact of pushing for cash payments for its broadcast network on its ability to obtain carriage and cash for its cable networks. (During the period, it was public knowledge that MTV, which is owned by Viacom, wanted to introduce several new MTV-branded cable networks.) Industry observers also indicated that if CBS were to succeed, this might set a precedent that would help non-network station groups, such as Gannett, Tribune, and Belo, in their retransmission consent negotiations, but would have less impact on the negotiations involving the other major broadcast networks, which still have cable networks.

A number of larger cable operators — Charter, Cox, Insight, and Time Warner — publicly responded that they would not pay cash for broadcast carriage, though some did not rule out the possibility of non-cash payments.[68] (The largest cable operator, Comcast, had signed a long-term carriage contract with Viacom at the end of 2003, and thus would not have been affected by the Viacom proposal.) The cable operators argued that the broadcast networks continue to lose audience share and therefore could not demand cash payments, and also that broadcasters were given spectrum for free and that cable companies should not have to pay for broadcast signals that customers can get off the air for free. CBS argued that its broadcast network audience share continued to far exceed that of any cable network and MVPDs should pay for any programming that they provide their subscribers.

In early March 2006, CBS president Leslie Moonves predicted that CBS would eventually get "hundreds of millions of dollars" from retransmission consent agreements covering the 60 million households reached by the CBS and CW stations owned and operated by CB[69]S. Later that month, CBS successfully negotiated its first retransmission consent agreement involving cash payments — with Verizon, the new telephone company entrant into the MVPD industry, for carriage of CBS's owned-and-operated stations. Although the terms were not announced, industry sources said they were "similar to Hearst-Argyle's recent breakthrough agreement with DBS

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[67] See, for example, "Mass Media Notes," *Communications Daily*, June 7, 2005, at p. 9, and Tania Panczyk-Collins, "Viacom Plans Carriage Fees for CBS Programming," *Communications Daily*, September 16, 2005, at p. 7.

[68] Jonathan Make, "Cable Won't Pay Cash for Carriage, Despite Viacom Demands," *Communications Daily*, September 19, 2005, at pp. 3-4.

[69] John Eggerton, "Moonves Sees Nine-Figure Retrans Pot," *Broadcasting & Cable*, March 6, 2006, at p. 27.

service Echostar" under which Echostar (DISH Network) paid 50 cents per month for each of its subscribers in the station group's markets.[70]

In February 2007, CBS announced that it had successfully negotiated retransmission consent agreements with cash payment provisions with nine small cable operators, covering a total of one million cable television subscribers who can watch CBS owned-and-operated stations.[71] But CBS provided no public confirmation of the exact amount of cash being paid by the cable companies, or even of the identities of the cable companies, citing confidentiality provisions in the agreements. Industry observers had differences of opinion on the terms of the agreements; some thought CBS was receiving 50 cents per subscriber per month ($6 million per year), or even more, while others thought some of the compensation was in the form of barter advertising time. Wall Street analysts estimated that cash payments of 50 cents per subscriber per month could generate between $155 million and $240 million in annual revenues for CBS. A Bank of America report, however, stated that "the market value for broadcast retransmission rights won't really be determined until CBS's agreements with the largest cable operators come up for renewal starting in '09-'10."[72]

DISH Network/Lifetime/Hearst-Argyle: An Example of the Complexity of Programmer-Distributor Negotiations

DISH Network has attempted to differentiate itself from other MVPDs in part by being the low-price provider, offering packages at lower prices than its competitors, though sometimes not offering on its more basic tiers certain high-cost networks that are provided on its competitors more basic tiers.[73] (In contrast, DirecTV has differentiated itself in part by having the most sports programming, including some sports programming for which it is the exclusive provider.) Given

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[70] John M. Higgins, "Money Talks: CBS Braces for Cable Showdown," *Broadcasting & Cable*, March 27, 2006, at p. 10. See the discussion of the DISH Network/Lifetime/Hearst-Argyle negotiations in the next section of this report.

[71] Linda Moss, "CBS Eyes New Deals," *Multichannel News*, February 26, 2007, at p. 3.

[72] See Linda Moss, "CBS Eyes New Deals," *Multichannel News*, February 26, 2007, at p. 3, and also Michael Malone, "CBS Demands — And Gets — Cash," *Broadcasting & Cable,* February 26, 2007, at p. 43.

[73] One of the key elements in programmer-distributor negotiations is the tier that the network(s) will be placed on. Most MVPDs offer several tiers — a most basic tier with perhaps 60 program channels, and progressively higher-priced tiers with perhaps 120 and 180 program channels. Programmers, of course, typically seek placement of their networks on the most basic tier, which will be purchased by the most households and thus generate higher revenues in the form of greater per subscriber fees and more advertising revenues. Industry analysts and the trade press often report the subscriber levels for each of these tiers, but rarely agree on those particular levels. The discussion in this section cites a number of different sources with inconsistent subscriber figures and thus there are some inconsistencies about the gain or loss in subscribers as a particular network is moved from one tier to another. This section seeks to show the general impact of a change in tier, not to present a quantitative impact calculation, and thus accepts those inconsistencies.

its business strategy, DISH Network has had more carriage disputes than other MVPDs with programmers that have sought to raise per subscriber charges.[74]

On December 31, 2005, DISH Network removed the Lifetime and Lifetime Movie networks, which target women audiences, from the DISH Network "top 60" package (its most basic package, variously estimated to have 11 million or 12 million subscribers) over a carriage dispute. DISH Network and Lifetime each alleged that the other was making unreasonable demands in their negotiations and then publicly distorting and mischaracterizing the other's most recent offer.[75] Lifetime's press release included quotes of concern from non-profit organizations that serve women and partner with Lifetime. DISH Network claimed that its contractual arrangements with 180 networks had been scheduled to expire on December 31, 2005, but it only experienced an impasse in re-negotiations with Lifetime.[76] DISH Network also claimed that it wanted to return the Lifetime network to DISH Network, but not at the 76% price increase it alleged Lifetime was seeking. Lifetime claimed it was seeking a much smaller price increase. Lifetime was the fourth-most-viewed advertising-supported cable network in the fourth quarter of 2005.

To replace the Lifetime networks, DISH Network temporarily carried Cablevision's WE:Women's Entertainment network on the channel it had used for Lifetime and the Encore Love Movie network on the channel it had used for the Lifetime Movie network. In mid-January 2006, DISH Network worked out a carriage arrangement with Oxygen Media, another network targeting women audiences, to fill the channel slot previously held by Lifetime Movie network on DISH Network's "top 120" package, which is received by an estimated 9 or 10 million DISH Network subscribers. This appeared to be a straight-forward contractual impasse between an MVPD and a cable programmer — with DISH Network risking losing subscribers

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[74] For example, in addition to the dispute with Lifetime described in this section, DISH Network has had a highly publicized dispute with Court TV. When renegotiating carriage terms for the period beginning January 1, 2007, DISH Network sought to move Court TV from its "top 60" tier, which one observer estimated to have 11 million subscribers, to its "top 120" tier, which was estimated to have only 8 million subscribers. Court TV responded by seeking a 70% increase in its per subscriber fee. DISH Network refused to pay the higher fee and removed Court TV from its tier, replacing it with The Biography Channel. On February 9, 2007, DISH Network and Court TV announced a new carriage agreement under which Court TV was carried on DISH Network's "top 120" tier, but other terms of the agreement were not disclosed. See Linda Moss, "Dish Drops Court TV from Lineup," *Multichannel News*, January 8, 2007, at p. 40, and Linda Moss, "Court TV Returns to Dish Network," *Multichannel Newsline*, February 9, 2007, available at [http://www.multichannel.com/index.asp?layout=articlePrint&articleID=CA6415345], viewed on June 28, 2007. In recent years, DISH Network has also been involved in carriage disputes with OLN (now Versus) and Viacom. See Linda Moss and Mike Reynolds, "Dish Sets a Date: Feb. 1," *Multichannel News*, January 29, 2007, at p. 3.

[75] Anne Becker, "Lifetime, Echostar Carriage Dispute Rages," *Broadcasting & Cable*, January 4, 2006, available at [http:www.broadcastingcable.com/index.asp?layout=article Print&articleID=CA6296491], viewed on June 28, 2007.

[76] Adrianne Kroepsch, "EchoStar Pulls Plug on Lifetime After Failed Carriage Negotiations," *Communications Daily*, January 4, 2006, at p. 3.

to DirecTV and cable operators and Lifetime losing revenues as Oxygen takes advantage of the gap in women's networks in the DISH Network line-up.

But, as described in several trade press news analyses, in fact the negotiating mechanics were more complex.[77] Lifetime is 50% owned by Hearst Corp., the controlling shareholder of Hearst-Argyle Television, which owns 28 broadcast television stations. Hearst-Argyle therefore had the right to negotiate retransmission consent agreements with the cable and satellite companies operating in those local broadcast markets; there were about 16 million television households in those local markets, approximately 14 million of which subscribed to MVPDs. But Hearst-Argyle traditionally had made Lifetime its "agent" in the retransmission consent negotiations with the MVPDs, and in those negotiations Lifetime had successfully secured carriage of, and higher cash payments for, the various Lifetime cable networks — rather than seeking cash payments from the MVPDs for carriage of the Hearst-Argyle broadcast signals. In exchange, Lifetime compensated Hearst-Argyle $1.8 million in 2004 and $5 million in the first nine months of 2005, or approximately 4 cents per month for each MVPD subscriber in the local markets served by Hearst-Argyle broadcast stations.

However, instead of continuing to use Lifetime as its retransmission consent agent in its negotiations with DISH Network, just as the December 31, 2005 deadline was approaching, Hearst-Argyle itself undertook retransmission consent negotiations directly with DISH Network, and accepted DISH Network's offer of $11 million a year to carry the Hearst-Argyle broadcast stations to DISH Network's 1.8 million subscribers in the Hearst-Argyle markets.[78] This represented approximately 50 cents per subscriber per month, more than 10 times what Hearst-Argyle had been receiving from Lifetime. But it meant that Lifetime would have to negotiate its own carriage agreement with DISH Network, without the leverage of being able to deny DISH Network access to the Hearst-Argyle broadcast programming if an agreement were not reached.

For its part, DISH Network appears to have believed it was in its financial interest to break tradition and make a cash payment to Hearst-Argyle on the expectation that it would save more than that amount in its negotiations with Lifetime. Presumably it believed that Lifetime, if forced to negotiate carriage on its own outside the context of retransmission consent negotiations, would lack market leverage and would have to accept a lower cash payment, since its programming, although popular, does not represent the sort of must-have programming whose absence would lead to significant desertion by DISH Network subscribers. A

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[77] See John M. Higgins, "Money Talks: Deal of a Lifetime," *Broadcasting & Cable*, January 16, 2006, at p. 17, and Mike Reynolds, "Hearst Key to Lifetime-Dish," *Multichannel Newswire*, February 2, 2006, available at [http://www.multichannel.com/index.asp?layout=articlePrint&articleid=CA6303719], viewed on June 28, 2007.

[78] This apparently had not been announced publicly, but rather reported in a December 30, 2005 8-K filing that Hearst-Argyle made to the Securities and Exchange Commission. See Mike Reynolds, "Hearst Key to Lifetime-Dish," *Multichannel Newswire*, February 2, 2006, available at [http://www.multichannel.com/index.asp?layout=articlePrint&articleid=CA6303719], viewed on June 28, 2007.

Broadcasting & Cable analyst concluded that if DISH Network could succeed in obtaining a reduction of 8 cents per month in cash payments to Lifetime for all 11 or 12 million DISH Network subscribers that would more than make up for a net increase of 46 cents per month in cash payments to Hearst-Argyle for the 1.8 million DISH Network subscribers located in local markets served by Hearst-Argyle broadcast stations.[79] But this raised a strategic market question that was widely discussed in the trade press: would DISH Network lose, nonetheless, because it had set the precedent of paying cash for carriage of a broadcast network?

In any case, DISH Network could not accomplish its objective if it made cash payments to Hearst-Argyle and also agreed to a higher — rather than lower — payment to Lifetime, so an impasse with Lifetime may have been inevitable, even if Lifetime only sought a nominal price increase.

A month later, on February 1, 2006, Lifetime was back on DISH Network's "top 60" tier.[80] In an amended submission to the Securities and Exchange Commission, dated January 31, 2006, Hearst-Argyle stated that it had revoked its December 2005 agreement with DISH Network and instead signed a "replacement agreement" that was "substantially similar to the previous contract," except that DISH Network would not pay Hearst-Argyle cash consideration. Hearst-Argyle also indicated that it amended its compensation agreement with Lifetime — apparently with Lifetime (instead of DISH Network) compensating Hearst-Argyle for the value of the retransmission consent rights in the negotiations, around $11 million. That is, DISH Network would pay Lifetime an unstated amount for carriage of the Lifetime cable networks and Hearst-Argyle broadcast networks, and then Lifetime would pay Hearst-Argyle $11 million. In this fashion, DISH Network could claim it was no longer making cash payments to Hearst-Argyle, even though in effect it was paying Hearst-Argyle for carriage of the broadcast signals. There was no public announcement of how much DISH Network was paying Lifetime, thus fostering debate in the trade press whether DISH Network had been able to reduce the payment to Lifetime sufficiently to make up for the $11 million payment that flowed through from DISH Network to Lifetime to Hearst-Argyle.[81]

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[79] John M. Higgins, "Money Talks: Deal of a Lifetime," *Broadcasting & Cable*, January 16, 2006, at p. 17.

[80] Mike Reynolds, "Hearst Key to Lifetime-Dish," *Multichannel Newswire*, February 2, 2006, available at [http://www.multichannel.com/index.asp?layout=articlePrint&articleid=CA6303719], viewed on June 28, 2007. As explained earlier, there is inconsistency in the trade press about the number of subscribers receiving the various DISH Network packages. The Reynolds article refers to unnamed sources that estimated that the "top 60" package only reaches 8.5 million subscribers, but given that it is the most basic DISH Network offering, that the same sources estimated there are 7.8 million subscribers to DISH Network's "top 120" offering, and that DISH Network has in total 13 million subscribers, the 8.5 million estimate appears to be low.

[81] See John M. Higgins, "Money Talks: Cable, Broadcast Battles End," *Broadcasting & Cable*, February 6, 2006, at p. 10, and Linda Moss, "DirectTV's Turn to Fork Over Documents," *Multichannel Newswire*, November 29, 2006, available at [http://www.multichannel.com/index.asp?layout=articlePrint&articleid=CA6395717], (continued...)

Although DISH Network again carried the Lifetime Movie Network, it was placed in the "top 180" package, with an estimated 4.5 million subscribers, rather than the "top 120" package, with an estimated 7.8 million subscribers. Also, as a result of the dispute, Oxygen, Lifetime's strongest competitor in the market for women's programming, was able to secure long-term carriage on DISH Network's "top 120" package.

It appears that neither DISH Network nor Lifetime benefitted from this retransmission consent impasse. Despite the modified agreement, DISH Network gave the appearance of setting a precedent by paying cash for broadcast signals and also reinforced its image as an MVPD that periodically failed to reach a carriage agreement without first removing programming from its tiers. Lifetime, by letting its networks be removed from a major MVPD's tier, gave its closest competitor, Oxygen, an opening onto that major MVPD's tier.

This dispute, and its resolution, had another market impact. In 2006, DirecTV filed a breach of contract suit against Lifetime, alleging that Lifetime reneged on a deal to pay $200 to DISH Network subscribers who switched over to DirecTV during the Lifetime-DISH Network impasse.[82] Lifetime subsequently filed a countersuit against DirecTV, which had been withholding license fees from Lifetime. In this panoply of suits, DirecTV alleged that Lifetime violated a most-favored-nation clause in their carriage contract in that DISH Network ultimately paid what amounts to a lower license fee, or effective rate, for Lifetime programming than DirecTV. Thus, the DISH Network-Lifetime dispute eventually affected DirecTV-Lifetime negotiations.

Sinclair's Negotiations with Various MVPDs: A Case Study of Factors Affecting Negotiating Strength

Sinclair Broadcast Group perhaps has been the most aggressive of all broadcast companies seeking cash payments for retransmission consent. Its negotiations with a number of MVPDs have received wide coverage in the trade press.

Sinclair-Mediacom.

This has been the "poster child" of difficult retransmission consent negotiations played out in public, and has involved federal regulatory agencies, state legislatures, courts, and Members of Congress. Sinclair Broadcast Group owns or is otherwise involved in the operations[83] of 58 television stations (more than any other U.S.

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[81] (...continued)
viewed on June 28, 2007.

[82] Linda Moss, "DirectTV's Turn to Fork Over Documents," *Multichannel Newswire*, November 29, 2006, available at [http://www.multichannel.com/index.asp?layout=articlePrint&articleid=CA6395717], viewed on June 28, 2007.

[83] By providing programming and operating services pursuant to local marketing agreements or by providing sales services pursuant to outstanding agreements.

broadcast company) in 36 markets, with a mid-size market focus.[84] It owns and operates two or more stations in 11 of those markets. Nineteen of its stations are affiliated with Fox, 17 with MyNetworkTV, 10 with ABC, 9 with the CW, 2 with CBS, and 1 with NBC. Sinclair's stations reach approximately 13% of all U.S. households. Mediacom, the eighth largest cable television company in the U.S., served 1.38 million basic cable subscribers in 23 states, and 105,000 telephone customers, as of December 31, 2006.[85] It primarily serves non-metropolitan areas.

Retransmission consent negotiations between Sinclair and Mediacom began in the fall of 2005, while the two companies were still operating under an existing month-to-month retransmission consent agreement that allowed either party to terminate the agreement at any time upon 45 days prior written notice.[86] It appears that under that old contract Mediacom did not have to make any cash payments to Sinclair for carriage of its signals, but that in the negotiations Sinclair was demanding substantial cash payments for all of its signals.

On October 11, 2006, Mediacom filed an antitrust suit in U.S. District Court in Des Moines, Iowa, seeking a court injunction against Sinclair's alleged attempt to tie retransmission consent agreements for carriage of its popular ABC, NBC, CBS, and Fox affiliates to the payment of retransmission consent fees for some of its less-watched CW and MyNetworkTV affiliates.[87] Mediacom claimed that it was interested in entering into retransmission consent agreements for the carriage of signals of 13 Sinclair "major network stations" (that is, stations that are affiliated with one of the four major television networks) located in 12 designated market areas (DMAs) where Mediacom operates cable systems, but not interested in entering into retransmission consent agreements for the carriage of signals of 9 "other network stations" owned or operated by Sinclair located in DMAs where Mediacom operated cable systems, if such agreements required cash payments. Mediacom alleged that Sinclair maintained a single and non-negotiable demand that Mediacom consent to a global agreement encompassing all 22 Sinclair stations located in DMAs where Mediacom provided cable service, that Sinclair required Mediacom to pay the same carriage rates for the 9 Sinclair stations that Mediacom did not want to carry as for those it did want to carry, that Sinclair rejected alternative arrangements proposed by Mediacom, and that Sinclair issued a terminating notice on September 28, 2006,

[84] Sinclair Broadcast Group, Inc. Form 10-K, received by the United States Securities and Exchange Commission March 9, 2007, at p. 5.

[85] Mediacom Communications Corp. Form 10-K, dated March 8, 2007

[86] *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*, CSR-7058-C, Memorandum Opinion and Order by the Chief, Media Bureau, Federal Communications Commission (hereinafter "FCC Mediacom-Sinclair Order"), adopted and released January 4, 2007, at para. 19.

[87] See Josh Wein, "Stop Sinclair Retransmission Consent Tactics, Mediacom Urges," *Communications Daily*, October 10, 2006, at pp. 5-6.

which ended Mediacom's right to carry the stations effective December 1, 2006.[88] Mediacom also alleged that Sinclair chose to pull the signals during football season, when Mediacom would be most vulnerable to losing subscribers to competing satellite providers if it no longer carried the football games aired on Sinclair's broadcast signals. In addition, Mediacom alleged that an unnamed satellite operator agreed to pay Sinclair a "bounty" for any customers it gained if and when Sinclair pulled its stations' signals off of Mediacom, which according to Mediacom represented a conspiracy in restraint of trade.

Sinclair responded that it had negotiated in good faith and was open to individual carriage arrangements for its stations in Mediacom's operating area, but had not negotiated on a station-by-station basis because it did not know that Mediacom sought an alternative to a group deal.[89] Sinclair publicly provided a list of prices it wanted for each station in Mediacom's service area — 35-38¢ a month per subscriber for its CBS, ABC, NBC, and Fox affiliates and 9-11¢ for CW and MyNetworkTV affiliates this year, as part of a three-year contract with some prices reaching 42¢ in 2008. Sinclair also filed motions in court to dismiss Mediacom's complaint on technical grounds.

The court denied Mediacom's injunction motion on October 24, 2006. Mediacom appealed to the U.S. Court of Appeals for the Eighth Circuit, but dropped the appeal on December 13, 2006.

On October 31, 2006, Mediacom filed at the FCC an Emergency Retransmission Consent Complaint and Complaint for Enforcement for Failure to Negotiate Retransmission Consent Rights in Good Faith against Sinclair, requesting that the Commission find Sinclair in violation of its obligations to negotiate in good faith for retransmission consent, direct Sinclair to immediately commence negotiations in good faith for retransmission consent, and impose appropriate relief and sanctions.[90] Sinclair filed an Answer and Mediacom filed a Reply and both parties also filed numerous pleadings, motions, and *ex parte* presentations. In its complaint, Mediacom argued that because Mediacom's systems represented less than 3% of Sinclair's aggregate audience, but approximately 50% of Mediacom's systems were located in a DMA served by a Sinclair station, Sinclair was in the position to impose uncompromising and harsh proposals that represented a substantial departure from the retransmission consent terms and conditions that Sinclair has offered other similarly-sized cable operators or that Mediacom had been offered by other

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[88] Id. Mediacom alleged that Sinclair strategically timed its termination notice to coincide with a Mediacom effort to sell $300 million in debt, in order to undermine Mediacom's access to capital. See Peter Grant and Brooks Barnes, "Channel Change — Television's Power Shift: Cable Pays for 'Free" Shows; Broadcasters Want Cash to Carry Their Signal; Super Bowl Is Hostage," *Wall Street Journal,* February 5, 2007, at p. A1.

[89] Josh Wein, "Sinclair Rebuts Mediacom Antitrust Claim, Discloses Subscriber Fee Demands," *Communications Daily*, October 17, 2006, at p. 6.

[90] FCC Mediacom-Sinclair Order at para. 1.

broadcasters in these same markets.[91] This information was intended to demonstrate that Sinclair enjoyed great leverage in the retransmission consent negotiations because it would lose very little from an impasse but Mediacom would be very vulnerable, and thus Sinclair did not have the incentive to negotiate in good faith.

As the December 1, 2006 deadline approached, Sinclair gave Mediacom a short-term extension to continue carrying its stations, while negotiations continued, after the CEOs of the two companies met with FCC Commissioner McDowell.[92] The companies agreed to a new January 5, 2007 deadline. At the same time, both companies attempted to strengthen their negotiating positions — Mediacom by sending antennas to subscribers who stood to lose Sinclair station signals if the carriage agreement were terminated, so they could continue to receive the Sinclair signals over-the-air; Sinclair by offering viewers a $100-$150 rebate to switch to DirecTV (with which Sinclair had a retransmission consent agreement). One industry analyst wrote that Mediacom would be vulnerable to subscribers switching over to satellite service if it lost carriage of the Sinclair stations because it had low penetration for VoIP and broadband services that might help retain subscribers.[93] Mediacom responded to this weakness by introducing a six-month $60 per month cable, broadband, and VoIP promotion in areas where Sinclair has television stations, though it did not publicize the promotion but rather offered it to customers who contacted Mediacom about the potential loss of the Sinclair signals.[94]

On January 4, 2007 the FCC Media Bureau (acting on delegated authority from the full Commission) denied the Mediacom complaint, concluding that the dispute arose from a fundamental disagreement between the parties over the appropriate valuation of Sinclair's signals, which is not indicative of a lack of good faith.[95] It strongly encouraged the two parties to engage in hard bargaining to achieve an agreement. It recognized the cost to consumers if Mediacom and Sinclair failed to reach an agreement by January 5th, but stated that the Commission does not have the authority to require the parties to submit to binding arbitration. It could only "strongly encourage them to submit to binding arbitration,"[96] either through the Media Bureau or through the American Arbitration Association. Although Mediacom sought such binding arbitration, Sinclair refused to arbitrate.

On January 5, 2007, Sinclair pulled 22 stations' signals from Mediacom's cable systems, affecting 700,000 subscribers. Mediacom continued distributing antennas

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[91] FCC Mediacom-Sinclair Order at para. 9.

[92] Josh Wein, "Sinclair May Extend Mediacom Carriage," *Communications Daily*, December 1, 2006, at pp. 3-5.

[93] Id.

[94] Josh Wein, "Mediacom Woos Sinclair-Market Customers with $60 Bundle," *Communications Daily*, December 8, 2006, at p. 5.

[95] FCC Mediacom-Sinclair Order at para. 24.

[96] FCC Order at para. 25.

to its affected customers, who were primarily in Iowa and Florida.[97] Media analysts did not agree about the long-term consequences to Mediacom of the loss of carriage. One analyst, Jason Bazinet of Citigroup, reportedly did not expect it to have significant impact, but Rich Greenfield of Pali Research thought Mediacom would be harmed because it would have to reach agreement with Sinclair to retain subscribers, but those subscribers had been inconvenienced and that would make it difficult for Mediacom to recover its higher payments to Sinclair by raising subscriber rates.[98]

On January 11, 2007, the Iowa congressional delegation — two senators and five representatives — asked Mediacom and Sinclair to end the carriage dispute, supporting the FCC Media Bureau's recommendation that they submit to binding arbitration.[99] But Sinclair responded by letter that it was not ready to submit to binding arbitration. Mediacom also took its case to the Iowa General Assembly's Joint Government Oversight Committee. Reportedly, some Iowa legislators were critical of Sinclair, but at least one agreed with Sinclair that the dispute was a private contractual issue.[100] FCC Chairman Martin also stated that he supported binding arbitration. But when Mediacom filed an emergency petition at the FCC, citing comments made by Senator Inouye in 1992 (when he was manager of the 1992 Cable Act that included the retransmission consent provisions in current law) that the FCC does have the authority to require binding arbitration, the Commission did not modify the Media Bureau opinion that the FCC does not have such jurisdiction.[101] On January 30, 2007, Senators Inouye and Stevens, chair and co-chair of the Senate Commerce Committee, urged the FCC to take action to resolve the Sinclair-Mediacom dispute, stating that the FCC had the authority to intervene and arguing that at a minimum carriage of the signals should be continued while the parties continued to negotiate.[102] They expressed concern that the on-going impasse would keep some households from viewing the Super Bowl. Sinclair reportedly rejected their position in a letter in which it stated that "Any suggestion, such as the one contained in your letter, that government intervention will be forthcoming has had a chilling effect on the ability of the parties to reach a mutually acceptable agreement on their own."[103]

On February 2, 2007, just before the airing of the Super Bowl, Sinclair and Mediacom finally reached a retransmission consent agreement, in which Mediacom

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[97] Josh Wein, "Comcast Doesn't Want to Pay to Carry Sinclair Stations," *Communications Daily*, January 9, 2007, at pp. 5-6.

[98] Id.

[99] Untitled article, *Communications Daily,* January 12, 2007, at p. 12.

[100] Linda Moss and Mike Farrell, "Sinclair Settles with TWC," *Multichannel News*, January 29, 2007, at p. 3.

[101] Although Chairman Martin tried to get the Commission itself to vote in support of the Media Bureau opinion, no item ever came up for a formal vote.

[102] Josh Wein, "Martin Should Facilitate Mediacom Customer Relief, Say Inouye, Stevens," *Communications Daily,* February 1, 2007, at pp. 3-5.

[103] Id.

reportedly paid cash fees for carriage of Sinclair's stations, which were restored to the cable company's tiers.[104] Mediacom agreed to drop all FCC and legal matters and to pay for Sinclair's legal fees from the dispute. Mediacom CEO Rocco Commisso reportedly admitted that he "caved in"; Mediacom lost 7,000 subscribers in the fourth quarter of 2006 (before losing carriage of the Sinclair signals) and is expected to report even greater subscriber losses for the period when it lost the carriage.[105]

Sinclair-Suddenlink.

Suddenlink Communications is the eighth largest cable television company in the United States, with 1,377,000 subscribers and operations in more than 20 states, primarily in suburban, small town, and rural communities. On July 1, 2006, Suddenlink completed an $800 million purchase from Charter Communications of cable systems in West Virginia with 240,000 subscribers, 200,000 of whom are located in the Charleston, WV designated market area of a Sinclair-owned television station (WCHS, an ABC affiliate) and another television station (WVAH, a Fox affiliate) for which Sinclair has a local marketing agreement. The remaining 40,000 subscribers are located in the neighboring Bluefield-Beckley-Oak Hill, WV and Parkersburg, WV designated market areas. The transaction represented a strategic decision on the part of both cable operators to cluster their systems — it allowed Suddenlink to expand its presence in the West Virginia-Ohio-Kentucky-Virginia region and allowed Charter to divest itself of systems that were distant from its larger holdings in the northeast and west, as well as receive $800 million to buy down its debt.

The retransmission consent agreement between Charter and Sinclair had expired prior to the Suddenlink purchase.[106] Suddenlink began negotiating a retransmission consent agreement with Sinclair in May 2006, before its purchase was completed. On June 30, 2006, Sinclair announced that it had not been able to reach an agreement with Suddenlink to continue carrying WCHS and WVAH, claiming that Suddenlink's retransmission consent offer included no compensation and that there had been no response to a Sinclair counteroffer.[107] Without a retransmission agreement, WCHS and WVAH would no longer be carried by any Suddenlink cable system when the transfer was completed. Suddenlink's subscribers in Charleston would no longer receive the ABC and Fox programming provided over those stations. Suddenlink's subscribers in Beckley would continue to get ABC

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[104] Linda Moss, "Sinclair's Retrans Cash Rises 90%," *Multichannel News*, February 19, 2007, at p. 40.

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

[106] See Mike Farrell, "Suddenlink, Sinclair in Retrans Clash," *Multichannel News*, July 5, 2006, available at [http://www.multichannel.com/index.asp?layout=articlePrint&articleID=CA6349903], viewed on June 28, 2007.

[107] Sarah K. Winn, "Spat imperils city TV viewing," *Charleston Gazette*, July 1, 2006, available at [http://www.tmcnet.com/usubmit/-spat-imperils-city-tv-viewing-/2006/07/01/1702516.htm], viewed on June 28, 2007.

programming from the local ABC broadcast affiliate located in Beckley, but would lose the Fox programming that Charter had been importing from the Sinclair station in Charleston (in the absence of any local ABC broadcast affiliate in Beckley). Similarly, Suddenlink's subscribers in Parkersburg would continue to get Fox programming from the local Fox broadcast affiliate located in Parkersburg, but would lose the ABC programming that Charter had been importing from the Sinclair station in Charleston (in the absence of any local ABC broadcast affiliate in Parkersburg). A letter was posted on Sinclair's WCHS and WVAH websites asking viewers to contact Suddenlink or to switch to a satellite provider, but although the satellite providers carried Sinclair's ABC and Fox programming in Charleston (as part of their local-into-local service), they did not provide those stations' signals to their subscribers in Beckley or Parkersburg.[108]

On July 5, 2006, Suddenlink filed an Emergency Retransmission Consent Complaint with the FCC, alleging that Sinclair had violated its duty to negotiate retransmission consent in good faith for the two Charleston stations and that Sinclair had demanded that Suddenlink terminate retransmission of the stations during the Nielsen Media Research rating "sweeps" week ending July 26.[109] On July 6, 2006, Sinclair filed an Emergency Petition for Declaratory Ruling and for Immediate Injunctive Relief with the FCC, arguing that Suddenlink had no authority to carry the signals of the Charleston stations and requesting that the Commission order Suddenlink to immediately cease its carriage of those signals. Suddenlink then filed a supplement to its complaint stating that Sinclair informed it in an e-mail that continuing to carry the two stations constituted an acceptance by Suddenlink of Sinclair's retransmission consent offer.[110] Both parties made subsequent filings with the FCC.

Suddenlink alleged that one week prior to the closing of the Charter purchase, Sinclair had asked for $4 million in fees over the three-year life of the retransmission consent agreement, but when Sinclair subsequently learned how much Suddenlink had paid for the cable systems it instead demanded a one-time up-front fee of $200 per subscriber ($40 million for the 200,000 Suddenlink subscribers in those broadcast areas) plus a $1 per month subscriber fee ($2.4 million annually) for the right to carry the stations. Suddenlink alleged that Sinclair threatened to pull the stations from Suddenlink and notified Suddenlink customers that the stations would not be available after July 1, 2006. Reportedly, Suddenlink provided the FCC with an e-mail from Sinclair stating, "Without the right to carry these stations, at least 25% of recently acquired subscribers will discontinue service, resulting in loss of value of more than $150 million.... Paying $40 million to ... avoid such a loss seems to us a

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[108] Fred Pace, "No NFL, Simpsons or 24?," *The Register-Herald*, July 2, 2006.

[109] FCC Public Notice DA 06-1454, released July 20, 2006.

[110] Mike Farrell, "Sinclair E-mail Fires up Suddenlink," *Multichannel News*, July 6, 2006, available at [http://www.multichannel.com/index.asp?layout=articlePrint&articleID=CA6350010], viewed on June 28, 2007.

reasonable price to pay."[111] (The $40 million+ fee would be more than double the total company retransmission consent revenues Sinclair reported in 2005.)

Suddenlink also claimed that when it informed Sinclair that it was obligated to carry the stations at least through the Nielsen sweeps (an FCC requirement that Sinclair disputed was applicable), Sinclair responded that another MVPD had agreed to pay $200 per defecting Suddenlink subscriber. But Sinclair disputed that Suddenlink was obligated to maintain its carriage and it may well be that Sinclair's reference to another MVPD being willing to pay for defecting Suddenlink subscribers was intended to support its view that the sweeps requirement was created to protect broadcasters during sweeps week, not MVPDs, and that such a requirement would not be binding if the affected broadcaster did not seek such protection.

Sinclair alleged that in the negotiations Suddenlink had proposed payments that were lower than those Sinclair received from Suddenlink in other markets. Sinclair also claimed that before the Charter-Suddenlink sale was completed, but while Suddenlink-Sinclair retransmission consent negotiations were occurring, it had received a letter from Charter stating that a lack of a retransmission consent agreement could jeopardize the Suddenlink purchase, indicating the value of the Sinclair signals; when Sinclair learned how much Suddenlink had paid for the Charter systems, it reconsidered upward the value of its broadcast signals to Suddenlink.[112] Sinclair vice president and general counsel Barry Faber was quoted as stating, "If they're paying $3,200 per sub, why shouldn't a piece of that be coming to us?"

Sinclair pulled the WCHS and WVAH signals from Suddenlink's cable system in Beckley on July 3, 2006,[113] but did not pull the signals from Suddenlink's Charleston cable system, presumably in deference to the FCC rule about discontinuing service during a Nielsen ratings sweep, despite its claim that the rule did not apply in this situation.

Barry Faber, Sinclair vice president and general counsel, reportedly said that he was prepared to take the two Charleston stations off Suddenlink's cable systems "forever" if his company did not receive adequate compensation.[114] He also reportedly said that Suddenlink made a bad deal with Charter because retransmission consent for Sinclair's two stations was not covered in the transfer of assets and Suddenlink stands to lose more than $125 million of its investment if 20% of its subscribers defect to DBS providers because Sinclair withholds the signals of its two major network affiliated stations.

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[111] Peter Grant and Brooks Barnes, "Channel Change — Television's Power Shift: Cable Pays for 'Free' Shows; Broadcasters Want Cash to Carry Their Signal; Super Bowl is Hostage," *Wall Street Journal*, Feb. 5, 2007, at p. A1.

[112] Id.

[113] Joe Morris, "Cable, WCHS at odds: Broadcast dispute might go to court," *Charleston Gazette,* July 7, 2006.

[114] Josh Wein, "Suddenlink, Sinclair Prepare for Long Retransmission Consent Fight," *Communications Daily,* July 7, 2006, at pp. 4-5.

Robert Prather, president of Gray Television, the owner of the NBC affiliates in the Charleston and Parkersburg markets, reportedly stated that if Suddenlink ended its dispute with Sinclair by paying cash for carriage, Suddenlink would have to give Gray's Charleston station the same terms because "We've got a most favored nation clause in our deal. If they pay them, they would have to pay us, too."[115] Nexstar COO Duane Lammers said that Suddenlink is particularly vulnerable to broadcasters seeking to extract cash for carriage because it had recently borrowed a lot of money to acquire rural systems that are "not big enough to be able to sustain a protracted battle."[116]

Suddenlink was especially sensitive to subscriber interest in the upcoming Major League Baseball All-Star game to be broadcast over the Fox broadcast network and attempted to make Fox programming available to its subscribers. It did not have any options in the Charleston market, because the combination of retransmission consent, network non-duplication, and syndicated exclusivity rules prohibited it from importing network or syndicated programming without Sinclair's permission. But it was able to continue to provide Fox and ABC programming in the Beckley market. It received permission from the Fox network to retransmit a national Fox station to replace Sinclair's Charleston Fox affiliate.[117] And Suddenlink already had a retransmission consent agreement with WOAY, the local ABC affiliate in Beckley. However, Suddenlink's subscribers in Beckley no longer had access to the local news broadcasts on Sinclair's WVAH and WCHS stations.

In mid-July 2006, Sinclair announced that it made a new negotiation proposal to Suddenlink — a month to month agreement of 47 cents per station with no upfront fee or a three-year agreement for $6 million.[118] Sinclair claimed that Suddenlink had not been responsive and that Suddenlink continued to refer publicly only to the earlier $40 million proposal — which Sinclair said it had made only in response to Suddenlink's proposal that there be no charge — as if that was Sinclair's most recent offer. Sinclair also ran a crawl message during certain broadcasts informing customers that its stations might be unavailable soon on their cable system and providing contact information for DirecTV and DISH Network.

On July 25, 2006, Sinclair and Suddenlink reached an agreement to extend cable carriage of the Sinclair stations through August 7, 2006, while negotiations continued.[119] In an *ex parte* filing at the FCC, Suddenlink stated that it had "steadily increased the overall value of [its] offer." When the extension was announced, Charleston, WV, city council member Harry Deitzler voiced concern that the not-yet-

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[115] Id.

[116] Id.

[117] Fred Pace, "Still no agreement in cable, TV stations' brawl," *The Register-Herald*, July 13, 2006.

[118] Fred Pace, "Sinclair makes offer to settle dispute with Suddenlink cable," *The Register-Herald,* July 19, 2006.

[119] Josh Wein, "Suddenlink, Sinclair Extend Carriage Talks on W.Va. Stations," *Communications Daily*, July 27, 2006, at p. 6.

finalized agreement could include a confidentiality clause that would hide the terms of the agreement.[120]

> The question I want answered is whether or not Suddenlink is paying the channels to put them on the air and, if they are, are they going to absorb the costs or pass it on to customers.
>
> If the cable company and the local television stations enter into an agreement whereby the television stations will effectively be charging the city residents to watch their stations, we are not going to be happy.

On August 7, 2006, Suddenlink and Sinclair reached a three-year retransmission consent agreement. Terms were not disclosed but Michael Keleman of Suddenlink stated that the agreement did not include the $40 million upfront payment and monthly fees that Sinclair had initially sought that would have forced Suddenlink to impose steep monthly rate increases on subscribers.[121] Keleman said the contract terms would not result in any viewer rate increases, although rates might go up over the course of the contract for other reasons. Charleston city councilman Deitzler, chairman of the council's cable television committee, had warned Suddenlink that any rate increase stemming from payments to Sinclair could jeopardize Suddenlink's franchising agreement with the city. With the new agreement, Suddenlink and Sinclair withdrew their FCC petitions on August 8, 2006

On September 12, 2006, West Virginia Media, a station group with four network affiliated stations in the state, including a CBS affiliate (WVNS) in the Beckley designated market area, announced that it was using the multicast capability of that station to start up its own Fox affiliate in Beckley.[122] West Virginia Media said the idea came from the Sinclair-Suddenlink retransmission consent impasse, which threatened to leave Beckley's residents without access to Fox programming. By September 19th, the new station was up and running on digital multicast and was already being carried by most local cable systems, including Suddenlink (on channel 10).[123] West Virginia Media was able to move so quickly because WVNS had previously been a Fox affiliate and Beckley was one of only six designated market areas, nationally, without a Fox affiliate. The new station planned to offer a 10 p.m. local news broadcast daily, the first by a local Beckley station, using the WVNS news team.

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[120] Sarah K. Winn, "Councilman keeps eye on cable deal," *Charleston Gazette*, July 29, 2006.

[121] See Joe Morris, "WCHS, WVAH to stay on cable: Rates won't rise over deal official says," *Charleston Gazette*, August 12, 2006, and Mike Farrell, "Suddenlink, Sinclair Settle Retrans Flap," *Multichannel News*, August 10, 2006, available at [http://www.multichannel.com/index.asp?layout=articlePrint&articleID=CA6361496], viewed on June 28, 2007.

[122] Fred Pace, "Beckley to have its own FOX affiliate," *The Register-Herald*, September 12, 2006.

[123] Fred Pace, "West Virginia Media starts FOX station in Beckley market," *The Register-Herald*, September 19, 2006.

On October 20, 2006, West Virginia Media filed for both non-duplication and syndicated exclusivity protections for the Fox programming on its WVNS Fox digital station in the Beckley designated market area.[124] Under these rules, cable companies could no longer import Fox programming from distant broadcast stations without West Virginia Media's approval. As a result, on December 18, 2006, Suddenlink's Beckley cable system blacked out the Fox programming on Sinclair's WVAH-Fox station out of Charleston, but continued to carry the local news and other programming produced locally by WVAH.[125]

Suddenlink's cable franchise agreement with Beckley expired in December 2006. Since Suddenlink had only recently acquired the franchise from Charter and there had been little time for franchise agreement negotiations, the city and the company agreed to extend the existing agreement for four months.[126]

On February 14, 2007, Suddenlink announced cable system rate changes, most of which were increases, for both Charleston and Beckley area subscribers.[127] Suddenlink spokesperson Keleman stated: "This is the first increase in rates since 2004.... The cost of programming overall has increased as well as labor costs and certainly fuel costs."[128] It also announced that six new high-definition channels would be launched on March 15, 2007 and the implementation of capital upgrades to increase bandwidth capabilities, increase Internet access speeds, and build a platform for telephone service.

Sinclair-Time Warner.

In July 2006, the FCC approved Time Warner's acquisition from the bankrupt Adelphia of cable systems that served 3.5 million subscribers.[129] One million of those subscribers were located in local broadcast markets in which Sinclair owned or operated one or more broadcast television stations. Adelphia's agreement with Sinclair to retransmit those 24 stations' signals expired on December 31, 2006 and therefore Sinclair and Time Warner had to negotiate a new contract. As that deadline

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[124] Fred Pace, "Suddenlink blacks out Charleston FOX," *The Register-Herald*, December 18, 2006.

[125] Id.

[126] Fred Pace, "Franchise agreement with cable company extended," *The Register-Herald*, December 13, 2006.

[127] Fred Pace, "Suddenlink cites higher costs in announcing cable rate hikes," *The Register-Herald*, February 14, 2007.

[128] Id.

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

approached and passed, Sinclair and Time Warner agreed three times to extend carriage while continuing to seek a negotiated agreement.[130] On January 22, 2007, Sinclair and Time Warner reached a three-year agreement under which Time Warner agreed to carry Sinclair's digital signals to most of its customers, to carry Sinclair's HDTV signals as they became available, and to carry Sinclair's MyNetwork TV affiliates in Columbus and Dayton, Ohio, both of which are transmitted as digital multicast stations.[131] The agreement extended beyond the cable systems purchased from Adelphia. According to Sinclair, "The agreement allows Time Warner to carry the analog and digital signals of 35 television stations owned and/or operated by Sinclair in 22 markets to approximately six million of Time Warner's subscribers, many of whom receive two stations owned and/or operated by Sinclair.... Time Warner ... carries our stations to more subscribers than any other cable company."[132]

The financial terms of the agreement were kept confidential and thus it is not possible to determine whether and to what extent Time Warner agreed to make any cash payments for carriage of Sinclair's broadcast signals. But the inclusion of provisions for the carriage of Sinclair's digital and HDTV signals and the digital multicast signals of a non-major broadcast network, as well as Sinclair's silence about cash payments, would suggest that a significant portion of the retransmission consent compensation took the form of carriage of less popular programming or program formats rather than cash payments.

Sinclair-Comcast.

The retransmission consent agreement between Comcast and Sinclair's 37 owned or operated stations (mostly affiliates of Fox, MyNetworkTV, and The CW, in markets as large as Baltimore, Pittsburgh, Minneapolis, Nashville, Richmond, and Tampa), which covered more than 3 million Comcast subscribers in 23 markets, was scheduled to expire on February 5, 2005. Sinclair's stations represented just 15% of Comcast's 24.2 million subscriber footprint, while Comcast's markets represented 30% of Sinclair's total advertising revenue.[133]

Comcast claimed that it was required, by FCC rule, to continue to carry Sinclair's analog broadcast signals through March 1, 2007, the end of the ratings

[130] See, for example, Linda Moss, "TW, Sinclair Keep Talking," *Multichannel News*, January 22, 2007, at p. 2. In contrast, during that same time period, Sinclair refused to continue negotiating with Mediacom beyond an initial extension of time and instead pulled its broadcast programming from Mediacom's cable tiers when the deadline was reached.

[131] Linda Moss and Mike Farrell, "Sinclair Settles with TWC," *Multichannel News*, January 29, 2007, at p. 3.

[132] "Sinclair Announces Analog and Digital Carriage Agreement with Time Warner Cable," Press Release, January 22, 2007, available at [http://www.sbgi.net/press/release_2007122_201.shtml], viewed on June 28, 2007.

[133] Mike Farrell and Linda Moss, "Retransmission — Cash or Not: Sinclair, Comcast Settle Up," *Multichannel News*, March 12, 2007, at p. 8.

sweeps period.[134] When the March 1st date approached, Comcast and Sinclair agreed to extend the existing agreement through March 9, 2007, and finally reached a new four-year retransmission consent agreement the day before that deadline. Under the agreement, Comcast agreed to carry multiple digital channels Sinclair currently is broadcasting in Richmond, VA and Baltimore, as well as certain other multicast channels that Sinclair may broadcast in Comcast markets in the future.[135] The new contract also involved advertising and co-marketing agreements, as well as advertising and cross-promotion opportunities on both companies' properties. The exact terms of the agreement were not disclosed.

As soon as the retransmission consent agreement was announced, however, Comcast and Sinclair sparred publicly about whether Comcast was making any cash payments for carriage of the Sinclair broadcast signals.[136] In a statement and interview, Comcast executive vice president David Cohen said:

> Comcast has achieved its objective of not paying cash for broadcast carriage that would need to be passed on to our customers. Consistent with our existing agreement with Sinclair, and all of our other retransmission consent agreements, comparable value is being exchanged.
>
> We have always been willing to discuss exchanges of value with broadcasters. We have had with Sinclair an existing exchange of value of where we're paying cash but receiving marketing and advertising benefits back from Sinclair that are of comparable value to the payments that we're making. We were able to make a deal consistent with that model.

Sinclair general counsel Barry Faber quickly disputed the Comcast claim that it did not make cash payments, claiming that Cohen had

> seriously mischaracterized the deal.... No way does what we gave them equal the value of what they're giving us. Our policy is that we get paid for retransmission consent, and simply giving us cash in exchange for inventory worth the same amount of cash, I wouldn't have gotten anything.

Faber added that Comcast may have been correct that it did not pay cash that it would have to pass on to its customers through higher rates, but it did pay cash. He also said that Sinclair updated its projections for revenue from retransmission payments from Comcast and other cable operators in 2007 to $53 million from the original

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[134] Josh Wein, "Comcast Doesn't Want to Pay to Carry Sinclair Stations," *Communications Daily*, January 9, 2007, at pp. 5-6. But Comcast said the FCC rule does not cover the small number of Comcast subscribers receiving out-of-market or HD signals from Sinclair stations, which were therefore scheduled to be discontinued on February 5th.

[135] Mike Farrell and Linda Moss, "Cashing In or Out: Sinclair, Comcast Settle," *Multichannel Newswire*, March 9, 2007, available at [http://www.multichannel.com/index.asp?layout=articlePrint&articleid=CA6423098], viewed on June 28, 2007.

[136] See, for example, Mike Farrell and Linda Moss, "Retransmission — Cash or Not: Sinclair, Comcast Settle Up," *Multichannel News*, March 11, 2007, at p. 8, and P.J. Bednarski, "Comcast, Sinclair Agree on Retrans," *Broadcasting & Cable,* March 12, 2007, at p. 22.

projection of $48 million, partly as a result of the agreement with Comcast — but would not state how much of the additional $5 million was attributable to the Comcast agreement.[137]

This war of words was not unexpected. It was widely viewed in the industry that if Comcast agreed to pay cash for the Sinclair signals, it would have represented a fundamental shift in retransmission consent negotiations industry-wide. Thus it was very important for Comcast to claim that it received advertising and marketing services of comparable value to the cash payments it made and for Sinclair to claim that the cash payments far exceeded the value of the advertising and marketing services it provided.

Sinclair-Charter.

In April 2007, Charter Communications became the third major cable company to reach a retransmission consent agreement with Sinclair; the three-year agreement covered the analog and HDTV signals of 28 television stations reaching 1.9 million subscribers, including 19 owned-and-operated Sinclair stations. Although the contract terms were kept confidential, two Wall Street analysts speculated that the terms included some kind of cash payments to Sinclair — perhaps in the range of 15-20 cents per subscriber per month — as well as some form of barter advertising.[138]

Measuring Retransmission Consent Revenues.

In its 2006 10-K annual report, Sinclair reported $25.4 million in retransmission consent revenues for the year, $20.5 million in cash and $4.9 million in local and regional advertising.[139] In February 2007, after negotiating the Mediacom and Time Warner agreements, Sinclair announced that it expected to generate nearly $48 million in retransmission consent revenues in 2007,[140] and then in March 2007, after negotiating the Comcast agreement, increased that estimate to $53 million.[141] But there remained a lot of debate about how these retransmission consent revenue estimates were calculated and, in particular, how to determine the cash portion. Consider, for example, a complex retransmission consent agreement in which the cable company (Comcast) agrees to make a single overall payment to the broadcaster (Sinclair) in exchange for the following package: (1) the right to retransmit Sinclair's broadcast signals, (2) a certain amount of advertising time on Sinclair's broadcast

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[137] See Mike Farrell and Linda Moss, "Retransmission — Cash or Not: Sinclair, Comcast Settle Up," *Multichannel News*, March 12, 2007, at p. 8, and Mike Farrell, "Defining When Cash is Cash — and Isn't," *Multichannel News,* June 28, 2007, at p. 6.

[138] Linda Moss, "Charter Renews with Sinclair," *Multichannel News*, April 16, 2007, at p. 8.

[139] Mike Farrell, "Defining When Cash is Cash — and Isn't," *Multichannel News*, March 19, 2007, at p. 6.

[140] Linda Moss, "Sinclair's Retrans Cash Rises 90%," *Multichannel News,* February 19, 2007, at p. 40.

[141] Mike Farrell and Linda Moss, "Retransmission — Cash or Not: Sinclair, Comcast Settle Up," *Multichannel News*, March 12, 2007, at p. 8.

stations, and (3) the right to offer Sinclair's broadcast programming as part of its video on demand service. How do you value the advertising and VOD programming? Suppose, for example, that Comcast purchases $100 of advertising time on a Sinclair station. That advertising has a value of $100 to Comcast and Comcast would attribute the full $100 to the advertising. But if, in the absence of the agreement, Sinclair would have sold that advertising time to someone else, then the incremental value to Sinclair of that advertising time would be less than $100, perhaps $30. Sinclair might then attribute only $30 to advertising and $70 to cash payment for retransmission consent.[142] Similarly, Sinclair might place a low value on the video on demand rights to its programming, but Comcast, which is attempting to retain subscribers while competing with satellite by creating a large VOD library, might place a higher value on the programming. For example, it might be important to Comcast that its subscribers have the ability to watch the 6 o'clock local news at 8 o'clock. Thus, a cable company might argue that a $10 million retransmission consent payment consists of $1 million in advertising payments and $9 million in payment for VOD rights, while the broadcaster might attribute all or most of the $10 million to cash payment for retransmission consent.

Time Warner: A Large Cable Company Demands Cash Payments from Broadcasters to Retransmit Their Non-Primary Signals

In retransmission consent negotiations in 2006 with a number of broadcast stations that are located in relatively small markets and affiliated with the CW broadcast network (which is not a major broadcast network), Time Warner, the second largest cable operator, used its strong market position to demand compensation from those broadcasters in exchange for carrying their signals.[143] It could do so because these signals were not the primary signal of the broadcast stations, but rather digital multicast signals. Nonetheless, agreement was reached within the context of retransmission consent negotiations.

In late September 2006, the signals of 20 CW station affiliates either were not carried on Time Warner systems or were being carried on a narrow digital tier not seen by half the subscribers. The markets involved included Palm Springs, CA; Lima, OH; and Waco, El Paso, Corpus Christi, and Wichita Falls, TX. Time Warner said that, in contrast to many other retransmission consent negotiations where broadcasters were trying to demonstrate the value of their programming to MVPDs, these negotiations demonstrated the value created by MVPDs by extending the broadcast network's (and local network affiliate's) reach.

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[142] For a more complete discussion, see Mike Farrell, "Defining When Cash is Cash — and Isn't," *Multichannel News*, March 19, 2007, at p. 6.

[143] The discussion in this section is based on John M. Higgins, "Time Warner Squeezes CW Stations," *Broadcasting & Cable*, October 2, 2006, available at [http://www.broadcastingcable.com/index.asp?layout=articlePrint&articleID=CA6376892.html], viewed on May 30, 2007.

Time Warner succeeded in securing cash payment from one station, WKRC, Cincinnati, owned by a major broadcaster group (Clear Channel Television). Time Warner received $350,000 — $1 per subscriber — for carriage of a digital CW feed on the local cable system's basic tier. The payments were in part for advertising on the Time Warner cable system promoting the broadcast station. Time Warner had a particularly strong negotiating position in Cincinnati because CW officials were worried about the network not being carried in the homes of marketing executives at Cincinnati-based Procter & Gamble who were in charge of purchasing advertising for that company. A CW executive acknowledged that the network was partly reimbursing Clear Channel as part of co-operative advertising efforts with its affiliates. Time Warner said the company was not receiving cash payments for carriage but would not comment on whether it was receiving "launch support" that included buying promotional spots on a cable system, which is common among cable networks but previously unheard of among broadcast networks.

The CW needs wide cable carriage to reach enough audience to attract advertisers. Cable companies do not automatically carry digital broadcast channels such as the CW channel. When they do, they often place those digital programs on a digital tier that is purchased by only 30% to 50% of the cable system's total subscribers. Broadcasters must negotiate to gain carriage on the more valuable basic cable tier available to all cable subscribers. The CW has had reasonably good success in its negotiations with MVPDs, but Time Warner has demanded compensation for carrying the CW signal. Demands have included giving commercial time on the stations to promote Time Warner Cable and rights to offer the station's local news via video-on-demand.

Some industry observers warned that the Time Warner strategy might help the broadcasters in their attempt to gain "digital multicast must-carry." Currently, cable operators are required to carry only the primary signal of each local broadcaster that chooses the must-carry (vs. retransmission consent) option. But as they deploy digital technology, in the transition from analog to digital transmission of broadcast signals, broadcasters are able to transmit multiple signals simultaneously and are seeking to widen the must-carry requirement to cover all of their signals. Cities outside the 100 largest U.S. markets typically have only three or four broadcast television stations and those broadcasters would not drop an affiliation with a major broadcast network to carry the CW network. CW thus was attempting to get those local broadcast stations, which had space on their digital signals for a few additional channels, to carry the CW network on a digital slot. Currently, stations in 49 markets use a digital slot for the CW. Broadcasters might argue that Time Warner's alleged recalcitrance demonstrates the need for multicast must-carry.

Ironically, CW is 50% owned by Time Warner Inc., the parent of Time Warner Cable. But the other 50% of CW is owned by CBS, which has been aggressively seeking cash payments in its retransmission consent negotiations with cable systems, and industry observers viewed Time Warner's actions as a warning that in some circumstances the MVPD enjoys the upper hand. In another irony, at approximately the same time that Time Warner was demanding payment for carriage of CW broadcast network signals, it was in a retransmission consent dispute with KAYU-TV, the Fox affiliate in Spokane, WA, and the broadcaster removed its signal from Time Warner cable systems serving 25,000 subscribers in Pullman, WA, Libby, MT,

and Coeur d'Alene and Moscow, ID, because Time Warner was refusing to make cash payment for carriage.[144]

Issues for Congress: Proposals for Statutory and Regulatory Change

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

It is possible that, as market conditions have changed, statutes or regulations that did not unduly favor one party over another when they were enacted, or that were intended to favor a party that was viewed as being in a disadvantageous position, now affect negotiations in an unintended fashion. For example, the various rules relating to cable carriage of broadcast signals — retransmission consent, network non-duplication, and syndicated exclusivity rules — were developed at a time when the local cable operator typically was the only MVPD in a broadcaster's service area and there was concern that cable operators might refuse to carry local signals or in some other way threaten the viability of local broadcasting. Today, with competitive provision of multichannel video services by satellite and telephone systems, the tables are somewhat turned, and broadcasters with must-have programming often can negotiate from a position of strength, especially with cable systems whose subscribers do not represent a significant portion of a broadcaster's audience.

The earlier discussions of market trends and of specific programmer-distributor disputes showed there is great variability in the negotiating strength of both individual programmers and individual distributors. They also showed that almost all impasses that resulted in MVPDs not carrying particular programming occurred outside major markets. Despite the trend toward greater programmer negotiating strength, in major markets distributors tend to have enough market clout to be able to reach agreements they can live with. This is not the case in smaller markets. In this new market environment, it is possible that the "one size fits all" regulations currently in place may no longer be fostering the public policy objectives they were intended to advance — especially outside major markets. Most of the proposals for modification of the current statutory and regulatory framework have come from

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[144] Anne Becker, "Northwest Station Pulls Signal in Retransmission Battle," *Broadcasting & Cable*, January 1, 2007, at p. 5.

parties that operate in smaller markets. In reviewing these proposals, it is important to consider their potential impact on large markets as well as smaller markets and to try to determine whether any changes should and could be limited to those markets where the current statutory and regulatory framework may be failing to safeguard the public against lost programming or higher prices. Also, it is important to note that the parties that have been proposing statutory or regulatory changes often cite the combined impact of multiple rules — for example, the impact of retransmission consent and program exclusivity rules in markets where a broadcaster owns multiple stations that are affiliated to two or more major broadcast networks. Would changing just one of the existing rules resolve alleged existing problems or create new ones? Would changing multiple rules represent overkill?

Economic Factors Relevant to Analysis of the Proposals for Statutory and Regulatory Change

In addition to the various market trends that were discussed in detail earlier, there are three economic factors that might be relevant to specific proposals that have been made for statutory and regulatory change. These are: the substantial economic rents earned by some factors of program production; how to divide the value of must-have programming — and the rents it generates — among programmers, distributors, and subscribers; and the extent of consumer demand for program diversity.

Successful existing network programs that have demonstrated the ability to generate larger audiences than the average program — hit programs such as *American Idol* and certain sports events — become more expensive to produce precisely because they are successful. Costs increase as the talent associated with those programs (athletes, actors, directors, producers) are able to renegotiate contracts to command a larger portion of the revenues they generate. Popular programming that attracts a large audience (or perhaps attracts a somewhat smaller audience that has a high intensity of demand) typically generates large revenues, either from advertisers or from direct subscriber charges. These higher than average revenues are shared by the owners of the programming and the program distributors, in the form of profits, and by the talent (actors, directors, athletes), in the form of high renegotiated salaries that include what economists call "economic rent." Economic rent, which some view as a measure of market power, is the difference between what a factor of production is paid and how much it would need to be paid to remain in its current use. A star in a successful television program might be paid $500,000 per episode when his next best employment opportunity might be to sign up for a new, untested series for $100,000 per episode. If the ratings for the successful program were to fall, or for some other reason the programmer could no longer command as much compensation from distributors and subscribers as it had been receiving, the star would likely continue to act but his salary would likely fall substantially. Reducing rent does not change production decisions, so economic rent can be reduced without any adverse impact on the real economy.[145]

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[145] See [http://www.economist.com/research/ Economics/alphabetic.cfm?letter=R], viewed on June 28, 2007.

These economic rents become part of the cost of the programming. The costs associated with each episode of a successful network program at the peak of that program's popularity therefore could be many times the average costs of all programming.

From the perspective of the viewing public, the substantial advertising and subscriber fee revenues generated by popular programming — both of which ultimately are passed on to consumers — are beneficial if they generate additional programming of the sort that the public prefers. To the extent these "windfalls" are ploughed back into the production of equally popular programming, or innovative programming that might not otherwise be produced, the public benefits. But to the extent most talent — athletes, writers, directors, producers, etc. — would continue to perform at the same level even if they could not command such high prices for their services, the public does not benefit from a system that fosters extremely high economic rents. For example, whenever a sports league has negotiated a new contract with a broadcast or cable network that substantially increases the revenues flowing to the league, the athletes in those leagues are able to command significantly higher salaries. It is unlikely that the quality of those athletes' performances would fall, or those athletes would choose not to continue to play, if their salaries were $1 million per year rather than $10 million. But the level of these economic rents will affect the prices that subscribers pay for their MVPD service.

It is important to distinguish between economic rents, which if reduced would not affect production, and compensation, profits, or earnings that are needed to attract factors of production. For example, it will be necessary for programmers to earn high profits on their successful programming in order to cover their losses from their unsuccessful programming. This often leads to debate about the amount of revenue that programmers need to generate in order to continue to provide quality programming and, beyond that, when a program is highly popular and can generate large revenues, how those additional revenues should be distributed among the talent (as salaries or other compensation), programmers and distributors (as profits), and subscribers (through charges that are less than their full valuation of the programming). This inevitably has been an area of conflict in retransmission consent negotiations. Broadcast signals typically consist of national network programming, nationally syndicated programming, and locally produced programming. Broadcasters argue that their stations have high audience ratings, are more highly valued than cable networks, and therefore they should receive the bulk of the revenues generated by their programming. MVPDs argue those signals are provided free over-the-air, broadcasters get compensated by the advertising revenues generated, MVPD carriage increases the size of broadcast audiences and therefore increases broadcasters' advertising revenues, and therefore MVPDs should not be required to pay cash to carry the broadcast signals to their subscribers. Subscribers complain to their elected officials about increasing MVPD rates, and may switch to a lower-cost provider, but rarely discontinue service entirely in response to price increases.

There is market evidence about how subscribing households value these broadcast signals. In 1999, Congress enacted the Satellite Home Viewer

Improvement Act (SHVIA),[146] which allowed satellite operators to carry the signals of their subscribers' local broadcast television stations. The two major satellite operators — DirecTV and DISH Network — began offering "local-into-local" service in some markets, charging their subscribers a separate $5 per month to receive the local signals in their market. (That charge is no longer separated out.) The vast majority of their subscribers chose to receive the local broadcast signals — showing a willingness to pay for the combination of network, syndicated, and local programming provided by their local broadcast stations.

That does not answer the question, however, of how to distribute that value of that programming between the broadcaster and the MVPD — or to allow the subscribers to pay less than their full valuation of the programming. Since economic rents do not generate additional productive value, however, it is in the public interest not to generate economic rents, which ultimately are borne by consumers.

There also has been some discussion of the extent to which households value having access to one hundred or more channels when the average household only watches a small portion of those channels. This could be useful information to help assess the impact on consumers of offering programming in tiered service offerings that bundle many networks together or in an à la carte basis. According to Media Dynamics, Inc.,[147] although the average television household can now receive 106 channels, a typical adult watches only 13 to 14 of those channels on a weekly basis. Over longer periods of time, however, the number of program sources the average viewer samples grows significantly. As shown in **Table 11**, the average adult cable subscriber watches at least 10 minutes of programming on 16 to 17 different channels in a week, on 31 different channels in four weeks, and on 43 channels in 13 weeks. These data do not provide information on the value consumers assign to additional choices, but do suggest that they take advantage of the availability of such choices.

Table 11. Estimated Number of Television Program Sources Viewed per Adult, 2005

Program Sources	All Adults 1 Week	All Adults 4 Weeks	All Adults 13 Weeks	Homes with Cable 1 Week	Homes with Cable 4 Weeks	Homes with Cable 13 Weeks
Major Networks	2.0	2.7	2.9	1.7	2.6	2.8
Local Shows on Affiliates	1.0	1.7	2.1	0.9	1.6	2.0
Independent Stations	1.3	1.6	1.8	1.4	1.7	1.9
PBS Stations	0.4	0.6	0.7	0.4	0.6	0.7
Pay Cable	0.5	0.6	0.6	0.7	0.8	0.8
Basic Cable	8.7	19.9	29.2	11.5	23.7	35.1
Total	13.9	27.1	37.3	16.6	31.0	43.3

Source: Media Dynamics, Inc.

[146] P.L. 106-113.

[147] Media Dynamics, Inc., *TV Dimensions 2006*, at pp. 26-28.

Specific Proposals to Modify Current Statutes and Regulations

The first two sections in this report described recent structural market changes that have altered the relative negotiating strength of programmers and distributors and showed that, in general, this has occurred to the detriment of smaller cable companies. Most of the federal statutes and regulations affecting programmer-distributor negotiations were enacted before these recent market changes and, indeed, several were specifically intended to strengthen the negotiating position of broadcasters. Not surprisingly, then, most of the proposals to modify current statutes and regulations have come from small distributors.

Proposal: Allow the importation of distant signals when a retransmission consent impasse develops.

Currently, a cable operator that reaches a retransmission consent impasse with a local broadcaster is prohibited under the network program non-duplication and syndicated exclusivity rules from importing the same network and syndicated programming provided by that local broadcaster from a distant broadcaster without the permission of the local broadcaster. For example, a cable operator experiencing a retransmission consent impasse with its local ABC broadcast affiliate cannot import the ABC network programming transmitted by a more distant ABC affiliate. Thus, even though the network and syndicated programming is not produced by the local broadcaster, that broadcaster has control over its distribution in its designated market area.

Some small cable companies have proposed modifying these exclusivity rules to allow distributors to import distant network and syndicated programming when a retransmission consent impasse develops.[148] This would allow an MVPD to negotiate with multiple providers of network and syndicated programming for the carriage of that programming if the MVPD reaches an impasse with its local broadcaster. Carriage of such distant signals would allow subscribers to continue to receive the network and syndicated programming.[149]

There appear to be two aspects to this proposal: to prohibit broadcast networks and their affiliates from employing exclusive arrangements that do not allow cable

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[148] See, for example, the opinion piece by Rocco Commisso, Mediacom Communications CEO, entitled "Rx for Retransmission," in *Multichannel News*, February 1 2, 2007, at p. 27.

[149] Of course, even if the MVPD were to import distant network and syndicated programming signals, without a retransmission agreement with the local broadcaster, the MVPD would not be allowed to carry the local broadcaster's local programming. Whether or not the MVPD imported those signals, however, subscribers could use "rabbit ear" or rooftop antennas to receive their local broadcaster's signals off the air — and thus receive the network, syndicated, and locally produced programming — and, in fact, in cases where impasses have developed cable operators typically have offered subscribers free rabbit ear antennas. In some situations, however, subscribers are not able to receive the local broadcast station's signal with rabbit ears, or even with a rooftop antenna, because they are too far away from the broadcaster or unusual terrain intrudes blocks signal transmission.

companies to seek alternative sources of broadcast network and syndicated programming and to deny the local affiliates the ability to get a "windfall" from popular network programming. (The proposal's proponents claim that the local broadcaster has not produced the network and syndicated programming but the exclusivity rules allow it to act like a monopoly producer and extract all the economic rents from the programming, which only forces up subscriber rates.)

Although it is true that exclusivity arrangements are intended to allow the broadcast network and its affiliates to maximize their revenues from the network programming, it is not clear that elimination of the FCC's exclusivity rules would have any market impact. Virtually the same exclusivity terms and conditions are included in the contracts that local broadcasters have with their affiliated networks and with their providers of syndicated programming. Indeed, the FCC rules specifically were constructed to mirror the language that already existed in most broadcaster-program owner contracts. So unless such contract terms were prohibited, elimination of the rules would have no practical impact. Similar types of exclusive distribution territories are common throughout the U.S. economy and pass antitrust muster.

With respect to the concern about the exclusivity rules allowing local affiliates to earn "windfalls," it is not clear to what extent recent market changes have created windfalls or simply changed the form of compensation. As was discussed earlier, in the past most local broadcast stations that were affiliated with a major broadcast network made that network its agent to negotiate retransmission consent terms with MVPDs and thus the networks received the bulk of the retransmission consent compensation, often in the form of agreement by the MVPD to carry other (broadcast or cable) program networks produced by the major broadcast network. But in exchange, the major broadcast networks made major cash payments to their local broadcast affiliate stations. In recent years, however, the major networks have agreed to allow their local broadcast affiliates to directly negotiate their own retransmission consent compensation with MVPDs, while substantially decreasing the cash payments from the broadcast networks to their local affiliates. Thus, even if retransmission consent negotiations result in direct cash payments to the local broadcast affiliates, at least some of the compensation received by those local broadcasters is, indirectly, being passed through to the program producers in the form of lower payments to affiliates.

The proposal to allow the importation of distant network and syndicated programming could have an impact beyond an impasse situation. It could strengthen the negotiating position of MVPDs by potentially allowing them to bargain among alternative providers of the same must-have network programming — to the extent that the local broadcast stations' existing network and syndication contracts did not already prohibit this. But giving all MVPDs the ability to negotiate with any network affiliate would strengthen the negotiating leverage of large as well as small MVPDs, and might have the unintended consequence of fostering retransmission consent impasses in larger markets.

Proposal: Require broadcasters to publish rate cards that would apply to all MVPDs.

The smaller independent cable companies complain that, due to their lack of negotiating power, broadcasters have demanded higher per subscriber fees from them than from the large cable and satellite companies in retransmission consent compensation. One has proposed a "nondiscrimination" requirement that broadcasters publish rate cards that would apply to all distributors of a broadcaster's programming.[150] Since the rate would apply to large and small distributors alike, and the broadcaster would have to take into account the negotiating strength of the large distributors when setting its rate, the purpose of this proposal is to give small distributors the same negotiating leverage as the larger ones. This might help keep small cable systems' programming costs down and thus reduce upward pressure on their retail charges to subscribers.

One problem with this proposal, however, is that most retransmission consent negotiations involve a large number of parameters, not just the per subscriber fee. A broadcaster might be willing to accept a lower per subscriber fee from a large distributor in exchange for some other form of compensation, such as the MVPD agreeing to carry the broadcaster's multiple digital signals, but smaller cable companies might not have the capacity on their networks to offer similar carriage. Similarly, a large distributor might partially compensate the broadcaster by purchasing advertising time on the broadcast station, but a small distributor might not be willing or able to do so. In these situations, requiring all distributors to pay the same per subscriber charge would represent discrimination against the larger distributors who also are providing the broadcaster alternative forms of compensation for the programming.

Proposal: Require parties to submit to binding arbitration to resolve leased access, program carriage, or retransmission consent disputes.

In a recent opinion and order relating to a retransmission consent complaint, the FCC's media bureau concluded that the "Commission does not have the authority to require the parties to submit to binding arbitration."[151] The Order "strongly encouraged" the two parties to submit to binding arbitration in recognition of "the cost to consumers if Mediacom and Sinclair do not reach an agreement" by the deadline. But Sinclair refused to do so and the Commission did not choose to take action.

This has led to proposals that, rather than allowing a local broadcast station's signal to be dropped from a cable or satellite system if a retransmission consent negotiation reaches an impasse, the parties should be required to submit to binding

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[150] Id.

[151] *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*, CSR-7058-C, Memorandum Opinion and Order, adopted and released January 4, 2007, at para. 25.

arbitration to resolve the rates, terms, and conditions of carriage. The arbitration might be performed by the FCC staff or by a recognized arbitration organization, such as the American Arbitration Association. This might involve a "baseball-style" winner-take-all process, in which each party submits a complete contract and the arbitrator choose between the two, or some other arbitration process.

Mandatory binding arbitration would assure that subscribers continue to receive the local broadcast programming, consistent with the public policy objective of fostering localism. It also might encourage the negotiating parties to avoid starting negotiations with extreme positions that they know would never survive an arbitration process, which in turn might expedite the negotiations process and discourage impasses. But some have opposed mandatory binding arbitration on the grounds that it represents very intrusive government intervention, and denies a party the right to choose, given the contractual terms demanded by the other party or dictated by the arbitration decision, simply not to make the programming available or simply not to carry the programming.

Although the Commission has chosen not to address the use of mandatory arbitration to resolve programmer-distributor impasses in retransmission consent negotiations, it recently included a commercial arbitration remedy for programmer-distributor disputes as a condition for approving the transfer of licenses from Adelphia to Comcast and Time Warner,[152] and in two separate notices of proposed rulemaking (NPRMs) has sought comment on implementing an arbitration process for resolving programmer-distributor disputes.[153] The Adelphia/Comcast/Time Warner order included a detailed commercial arbitration remedy with explicit arbitration rules. In the first NPRM, the Commission sought comment on whether it should adopt procedures or remedies such as mandatory standstill agreements and/or arbitration to resolve program access complaints, as it has done in the form of conditions to specific mergers. In the second NPRM, the Commission sought comment on the application of arbitration procedures to resolve leased access and program carriage disputes, whether such arbitration procedures should be specific to these types of complaints, what the procedures should be, whether they should be

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[152] See *In the Matter of Applications for Consent to the Assignment and/or Transfer of Control of Licenses: Adelphia Communications Corporation (and subsidiaries, debtors-in-possession), Assignors, to Time Warner Cable Inc. (subsidiaries), Assignees; Adelphia Communications Corporation (and subsidiaries, debtors-in-possession), Assignors and Transferors, to Comcast Corporation (subsidiaries), Assignees and Transferees; Comcast Corporation, Transferor, to Time Warner Inc., Transferee; Time Warner Inc., Transferor, to Comcast Corporation, Transferee*, Memorandum Opinion and Order, adopted July 13, 2006, released July 21, 2006, at Appendix B, pp. 2-4, and Appendix C.

[153] *In the Matter of Implementation of the Cable Television Consumer Protection and Competition Act of 1992; Development of Competition and Diversity in Video Programming Distribution: Section 628(c)(5) of the Communications Act; Sunset of Exclusive Contract Prohibition*, MB Docket No. 07-29, Notice of Proposed Rulemaking, adopted February 7, 2007, released February 20, 2007, at para. 15, and *In the Matter of Leased Commercial Access; Development of Competition and Diversity in Video Programming Distribution and Carriage*, MB Docket No. 07-42, Notice of Proposed Rulemaking, adopted March 2, 2007, released June 15, 2007, at para. 19.

elective or mandatory, who should bear the costs of arbitration, and what standard of review should the Commission employ in reviewing an arbitration decision.

Thus, at this time, the Commission is considering arbitration procedures in leased access and program carriage disputes in which the programmer tends to be the aggrieved party bringing a complaint against a distributor to the Commission but not in retransmission consent disputes in which the distributor — most frequently a cable company — tends to be the aggrieved party bringing a complaint against broadcast programmer. It appears that the FCC believes it has the authority to require arbitration for the former, but not for the latter.

Proposal: Strengthen the FCC test for what constitutes "good faith" retransmission consent negotiations.

The Satellite Home Viewer Improvement Act (SHVIA),[154] enacted in 1999, required the FCC to revise the rules surrounding retransmission consent agreements between television broadcast stations and multichannel video programming distributors (MVPDs), such as cable and satellite companies. The law prohibits a TV station that "provides retransmission consent from engaging in exclusive contracts for carriage or failing to negotiate in good faith." In March 2000, the FCC adopted rules for good faith negotiations for retransmission consent agreements involving broadcast television stations and cable or satellite companies.[155] The FCC established a two-part test for good faith negotiations.

The first part of the two-part good faith test consists of a brief, objective list of procedural standards applicable to broadcast stations negotiating retransmission consent agreements:[156]

- a broadcaster may not refuse to negotiate with an MVPD;
- a broadcaster must appoint a negotiating representative with the authority to bargain;
- a broadcaster must agree to meet at reasonable times and locations and cannot delay the course of negotiations;
- a broadcaster may not offer a single, unilateral proposal;
- in responding to an offer proposed by an MVPD, a broadcaster must provide reasons for rejecting any aspects of the offer;

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[154] P.L. 106-113.

[155] *In the Matter of Implementation of the Satellite Home Viewer Improvement Act of 1999; Retransmission Consent Issues: Good Faith Negotiation and Exclusivity*, CS Docket No. 99-363, First Report and Order, adopted March 14, 2000 and released March 16, 2000.

[156] Id. at Appendix B, pp. 1-2.

- a broadcaster is prohibited from entering into an agreement with any party conditioned upon denying retransmission consent to any MVPD; and

- a broadcaster must agree to execute a written retransmission consent agreement that sets forth the full agreement between the broadcaster and the MVPD.

Under the second part of the good faith test, an MVPD may present facts to the FCC which, even though they are not a specific violation listed above, given the totality of the circumstances constitute a failure to negotiate in good faith.[157]

In its order, the FCC concluded that it is not possible to identify objective competitive marketplace factors that broadcasters must use in negotiating. To provide guidance, the FCC listed some conditions that are potential competitive marketplace considerations and some that are not. For instance, the order notes that any effort to stifle competition through the negotiation process would not meet the good faith negotiation requirement. The order directs the Commission staff to expedite resolution of good faith complaints and notes that the burden of proof is on the MVPD complainant. The order also allows parties to pursue voluntary mediation and the FCC will consider favorably a broadcaster's willingness to participate, but non-participation will not constitute a violation of good faith.

Subsequent to adoption of these rules, several MVPDs have filed complaints against broadcast stations. The Commission, itself, has not acted on any of these complaints, but rather has given the Media Bureau delegated authority to reach determinations. The Bureau generally has not responded quickly to these complaints; in most cases the parties have reached agreement before the Bureau has taken action, and the complaints were then retracted. Where it has made determinations, the Bureau has not found the broadcasters in violation of the good faith rules. Typically the Bureau has found these impasses represented a difference of opinion about the value of the broadcast signals under dispute, not a refusal by the broadcaster to negotiate in good faith.

Since the Commission, itself, has chosen not to get involved in any of these complaints and therefore there has not been any commission-level order identifying what constitutes good faith negotiations, some MVPDs have proposed that the FCC's good faith standards be revisited and strengthened to prohibit any form of discriminatory pricing, abusive practices, and anti-competitive behavior by broadcasters.[158] As explained earlier, retransmission consent compensation often is made in both cash and non-cash form. It therefore often may be difficult, if not impossible, to identify what would constitute discriminatory pricing. Abusive practices and anti-competitive behavior often are subject to antitrust scrutiny. Absent a specific list of actions that would represent bad faith negotiations, it is not possible to fully evaluate the proposal to strengthen the FCC's good faith rules.

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[157] Id. at Appendix B, p. 2.

[158] See, for example, the opinion piece by Rocco Commisso, Mediacom Communications CEO, entitled "Rx for Retransmission," in *Multichannel News*, February 1 2, 2007, at p. 27.

At the same time, the Commission has recently adopted a Notice of Proposed Rulemaking seeking comment on the effectiveness of leased access enforcement and the costs and burdens associated with the complaint process,[159] and also on whether and how its processes for resolving carriage disputes should be modified.[160] It might be reasonable for the FCC to undertake an analogous review of its retransmission consent complaint process.

Proposal: Prohibit tying carriage of popular programming to carriage of less popular programming.

Although most recent retransmission consent impasses have centered on unresolved conflicts about cash payments for carriage, the smaller cable operators have long sought limitations on another form of compensation — the practice of the large broadcast networks that also own cable networks of tying retransmission consent for a particular broadcast station's signal to carriage of an entire suite of cable and broadcast networks.[161] These tie-ins sometimes extend beyond carriage on the local cable system and may require multi-system operators to carry the suite of cable networks on all their cable systems and/or for time periods that extend far beyond the three-year period covered by the broadcast station retransmission consent agreement being negotiated.[162] The American Cable Association (ACA) claims that such tie-ins can result in cable system operators providing programming their customers do not prefer or passing through high programming charges to customers.

The ACA therefore has proposed a prohibition on programmers requiring distributors to carry less popular programming in order to gain access to more popular programming, which it claims would give cable and satellite operators — especially small cable operators whose systems have limited capacity — greater discretion in choosing cable networks that meet their subscribers' tastes, to the benefit of those subscribers, and also would help independent cable networks gain access to cable systems.

The programmers that own broadcast stations have responded that, in some cases, it was cable operators not programmers who initially proposed that their compensation for retransmission consent take the form of carrying the programmers' cable networks (as well as the broadcast signal) at a low charge or no charge, rather than paying a high price for the retransmission rights to the broadcast signal. At the time, the cable operators had available capacity on their systems but not much cash to pay for programming. Now the situation is reversed; many cable operators have limited available capacity for additional cable networks and some would prefer to pay

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[159] *In the Matter of Leased Commercial Access; Development of Competition and Diversity in Video Programming Distribution and Carriage*, MB Docket No. 07-42, Notice of Proposed Rulemaking, adopted March 2, 2007, released June 15, 2007, at para. 7.

[160] Id. at para. 6.

[161] See, for example, the American Cable Association *Petition for Inquiry into Retransmission Consent Practices*, filed with the FCC on October 1, 2002.

[162] Id.

higher prices for the broadcast programming and free up scarce capacity on their systems.

A prohibition on tie-ins would strengthen the negotiating position of distributors and independent networks relative to the large programmers that own multiple cable networks and broadcast networks. But it might have other impacts — or little impact.

Under a prohibition, the large programmers that could no longer tie retransmission consent for their popular broadcast networks to carriage of their other program networks would seek an alternative form of compensation from MVPDs for retransmission consent. The most likely alternative would be to increase the cash payment demanded for carriage of the popular broadcast network, which could lead to an increase in the number of negotiation impasses. In general, the fewer the number of parameters involved in a retransmission consent negotiation, the fewer the areas where compromise can be reached, and the higher the likelihood of unresolved conflict. While many small cable operators have sought a prohibition on tie-ins, the larger MVPDs (many of whom are, themselves, large programmers) have supported that form of compensation, in part because they like to tie their own cable networks but also in part because it provides more opportunity for give and take in the negotiations.

Under a prohibition on tying, several business strategies at the heart of the current cable programmer business model would be constrained. The large programmers have followed the business strategy of creating multiple networks because of the efficiencies they can gain by cross-marketing one network on another and developing a strong brand identity. If distributors can choose not to carry the large programmers' less popular networks, the programmers' efficiencies from cross-marketing and branding would be diminished. At the same time, if their strategy of proliferating their own branded networks were curtailed, it might become easier for new independent networks to enter the market, which might increase the diversity of independent voices.

Proposal: Require programmers to offer their broadcast and cable networks to distributors on an à la carte basis.

A less intrusive and restrictive government intervention would not prohibit programmers from offering their popular networks as part of a tie-in with less popular networks, but would require the programmers also to offer each of their program networks to MVPDs on an à la carte basis. This could include a requirement for nondiscriminatory pricing of the à la carte offerings but, as discussed earlier, carriage agreements often include other forms of compensation or services and therefore it would be difficult to determine what constituted discriminatory pricing.

It is not clear what impact this requirement would have, however, for two reasons. First, tying more popular program networks to less popular ones has been at the core of the cable industry for more than a decade because in most situations it is beneficial to the MVPD as well as the programmer. Consumer demand for a large tier of program networks tends to be far less price elastic — far less sensitive to

increases in price — than demand for individual program networks. Thus in most situations the MVPD is not harmed by having to purchase a bundle of program networks from a broadcast or cable programmer. There are some exceptions — for example, a small cable operator whose system has limited channel capacity or an MVPD with relatively few subscribers demanding sports programming facing a bundle of networks that includes one or several very high-priced sports programming.

Second, it is likely that the large programmers would price an à la carte offering in a fashion that took into account both the lost marketing efficiencies from tying less popular programming to popular programming and the lost revenues if network proliferation had been a successful way to forestall competitive entry. Thus the rates for à la carte offerings are likely to be very high, which might discourage most MVPDs from choosing that option. The exceptions might be small cable operators whose systems have such limited channel capacity that their only viable choice would be the à la carte offerings of at least some programmers and programming for which there is an audience with a high intensity of demand that the MVPD intends to offer on a premium tier — assuming the programmer allowed the MVPD to offer the programming on a premium tier. (See the next proposal.)

Proponents of à la carte pricing of retail MVPD service have been among the strongest proponents of mandatory à la carte pricing at the wholesale level, since they believe the latter would foster the former. These proponents argue that à la carte pricing gives subscribers the greatest control over their video purchases. It allows them to pay only for the programming that they want and also allows them to keep programming that they find offensive out of their home. In addition, noting that subscribers' price elasticity of demand (sensitivity to price increases) tends to be greater for individual networks than for large tiers, they argue that requiring an à la carte option would place downward pressure on both wholesale and retail prices.

Opponents of mandatory à la carte pricing argue that the current system of large tiers allows both programmers and distributors to take advantage of the significant economies in cross-marketing and fosters diverse programming by giving new networks the opportunity to build audiences (how would subscribers even learn about the existence of new networks in an à la carte environment, unless those new networks were owned by one of the large programmers who could continue to cross-market?) and supporting minority and independent networks that might not attract enough subscribers in an à la carte environment to survive. The data in **Table 11**, showing that over a 13 week period most viewers watch programming on far more networks than they do in a week, suggests that there likely are many casual and infrequent viewers of any individual network that now are part of that network's audience but would be unlikely to subscribe to that network in an à la carte environment. This might require the network and MVPD to set high à la carte price for the diminished audience. Of course, as long as subscribers continue to have tiered options as well as the à la carte option they need not change their behavior, but it is likely that many subscribers that currently take advantage of channel surfing would choose the à la carte option.

Proposal: Prohibit programmers from requiring their networks to be placed on the expanded basic service tier.

Often, when a major programmer with must-have programming is negotiating with a distributor, it not only seeks to tie carriage rights to that programming to carriage of its less popular program networks, it also seeks to require the distributor to place the less popular networks on its most widely subscribed to tier — the enhanced basic service tier. That will maximize the number of households receiving the programming and will help in ratings and hence advertising revenues. But the secondary or tertiary networks of that programmer may not be the program networks most sought by subscribers and thus the MVPD sometimes will prefer not to place them on its expanded basic service tier.

The ACA therefore has proposed prohibiting programmers from requiring cable and satellite operators to offer the programmers' cable networks only on the expanded basic service tier and instead allow the MVPDs to determine program placement on their network tiers. In most situations, distributors share the large programmers' preference for a single large expanded basic service tier, and thus the impact of this proposed prohibition might be limited. But there may be situations in which programmer and distributor interests diverge and, more generically, the prohibition could create an opportunity for distributors to experiment with their cable tiers.

For example, while cable programmers receive about half their revenues from advertising and half from per subscriber fees assessed on cable and satellite operators, cable and satellite operators get almost 90% of their revenues from subscribers and only a little more than 10% from advertisers.[163] An optimal tiering strategy for programmers therefore might not be optimal for distributors. Moreover, cable and satellite operators do not have a retail layer to insulate them from subscribers, and therefore may be more responsive to consumer complaints about the placement of specific networks on tiers.

Cable and satellite operators may be more willing than programmers to take particular cable networks off the expanded basic service tier and place them on premium tiers because they only indirectly benefit from the strategies of cross-promotion of networks and network proliferation that directly benefit programmers, which depend heavily on a single large expanded basic service tier.

Cable and satellite operators also may choose to experiment with cable tiers — and even with à la carte pricing — if they perceive that these additional offerings might increase their profits. When the per subscriber license fee for a cable network does not appear to be in equilibrium with subscriber viewing patterns,[164] then the

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[163] See footnote 24 and also **Table 10** in this report.

[164] For example, in 2003 Cox Cable alleged that ESPN represented 18% of Cox's total programming costs but only 4% of Cox's viewing audience. (See Chris Isidore, "Sports' main event: ESPN-cable bout," CNNMoney.com, October 23, 2003, available at [http://money.cnn.com/2003/10/23/commentary/column_sportsbiz/sportsbiz/index.html], (continued...)

operator will have the incentive to either decrease payments to the programmer or increase revenues from end users or both. By placing a high-cost network on a separate tier, the operator might be able to reduce payments to the programmer by only paying for those subscribers who actually desire that network while maintaining (or at least not decreasing by as much) the revenues received from subscribers. If the operator were able to take a high-cost cable network off its expanded basic service tier, place it on a separate tier, and then re-price the expanded basic service tier in a way that did not lower revenues from that tier by as much as it gained revenues from the new separate tier, it would benefit from having the discretion to place cable networks on tiers as it saw fit.

Some observers have questioned whether giving distributors greater control over the tier placement of cable networks would yield lower prices for subscribers. They cite the most recent FCC report on cable industry prices — which found that satellite operators do not provide sufficiently strong competitive constraints on cable operators to restrain prices[165] — and suggest that the shift of control over the placement of networks on tiers from programmers to distributors is less likely to reduce rates to subscribers than to redistribute the profits from programmers to distributors. But even if the price effect were small, distributor control over network placement on tiers would improve the ability of distributors to base placement on their subscribers' preferences rather than the negotiating strength of the programmers.

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

In the earlier section presenting specific examples of programmer-distributor conflicts, it was striking how often the broadcaster involved in a dispute owned or controlled more than one broadcast station in a small or medium sized local market. It appears that where a broadcaster owns or controls two stations that are affiliated with major networks, that potentially gives that broadcaster control over two sets of must-have programming and places a distributor, especially a relatively small cable operator, in a very weak negotiating position since it would be extremely risky to lose carriage of both signals. Alternatively, when a broadcaster owns or controls one station that is affiliated with a major broadcast network and a second station that is affiliated with a weaker broadcast network, it may be able to tie carriage of the major broadcast network to a demand that the cable operator also carry — and perhaps pay for carriage of — the signals of the weaker broadcast network, which otherwise the

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[164] (...continued)
viewed on June 28, 2007.) ESPN responded that Cox fails to take into account additional local advertising revenues Cox receives by carrying the ESPN networks.

[165] *In the Matter of Implementation of Section 3 of the Cable Television Consumer Protection and Competition Act of 1992; Statistical Report on Average Rates for Basic Service, Cable Programming Service, and Equipment*, MM Docket No. 92-266, Report on Cable Industry Prices, adopted December 20, 2006, released December 27, 2006, at para. 14.

cable company would refuse to pay for or only carry for free as part of a must-carry arrangement.

The FCC's media ownership rules, including its local television multiple ownership rule, currently are in flux, as a major order that it adopted on June 2, 2003,[166] modifying five rules was remanded by the United States Court of Appeals for the Third Circuit in June 2004.[167] Thus the rules currently in place are those that existed prior to June 2, 2003, while the Commission completes work on a proceeding to adopt new rules (or provide stronger support for the June 2, 2003 rules) that will meet the Court's concerns.[168] Under current rules, a company can own two television stations in the same designated market area if the stations' Grade B contours[169] do not overlap *or* if only one is among the four highest-ranked (in terms of audience) in the market and at least eight independent television stations would remain in the market after the proposed combination.[170] An existing licensee of a failed, failing, or unbuilt television station can seek a waiver of the rule if it can demonstrate that the "in-market" buyer is the only reasonably available entity willing and able to operate the subject station, and that selling the station to an out-of-market buyer would result in an artificially depressed price for the station.[171] The rule that the FCC had adopted in June 2003 would have provided a lower threshold for such "duopoly" ownership.[172]

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[166] Report and Order and Notice of Proposed Rulemaking, *2002 Biennial Regulatory Review — Review of the Commission's Broadcast Ownership Rules and Other Rules Adopted Pursuant to Section 202 of the Telecommunications Act of 1996,* MB Docket 02-277*; Cross-Ownership of Broadcast Stations and Newspapers,* MM Docket 01-235; *Rules and Policies Concerning Multiple Ownership of Radio Broadcast Stations in Local Markets,* MM Docket 01-317; *Definition of Radio Markets,* MM Docket 00-244; *Definition of Radio Markets for Areas Not Located in an Arbitron Survey Area,* MB Docket 03-130, adopted June 2, 2003 and released July 2, 2003

[167] *Prometheus Radio Project v. Federal Communications Commission,* 2004 U.S. App. LEXIS 12720 (3rd Cir. 2004).

[168] A detailed discussion of the FCC's media ownership rules is provided in CRS Report RL31925, *FCC Media Ownership Rules: Current Status and Issues for Congress*, by Charles B. Goldfarb.

[169] Grade B is a measure of signal intensity associated with acceptable reception. The FCC's rules define this contour, often a circle drawn around the transmitter site of a television station, in such a way that 50 percent of the locations on that circle are statistically predicted to receive a signal of Grade B intensity at least 90 per cent of the time. Although a station's predicted signal strength increases as one gets closer to the transmitter, there will still be some locations within the predicted Grade B contour that do not receive a signal of Grade B intensity.

[170] 47 C.F.R. 73.3555(b).

[171] 47 C.F.R. 73.3555 n. 7.

[172] In markets with five or more TV stations, a company could own two TV stations, but only one of these stations could be among the top four in ratings; in markets with 18 or more stations, a company could own three TV stations, but only one of these stations could be among the top four in ratings; in deciding how many stations are in the market, both commercial and non-commercial TV stations were counted. There was an eased waiver

(continued...)

The FCC record developed when constructing the 2003 rules did not take into account the impact of duopoly control of television stations on retransmission consent because at that time the market changes that were strengthening the negotiating position of broadcasters had not yet occurred — or had not yet been affecting negotiations. Rather the focus of the analysis of the local television multiple ownership rule was on the number of independent voices and competition in the market for advertising. The Commission concluded that the old rule (which is now again in place) could not be justified on diversity or competition grounds. While those remain important bases for analysis, it appears from recent retransmission consent negotiations that in its current proceeding, the FCC might also want to look at the effect of duopoly ownership on retransmission consent negotiations since any impact on broadcaster-distributor negotiations may also affect the availability and price of programming to MVPD subscribers. For example, in comments filed in the current proceeding, Suddenlink argued that common ownership of two or more of the top four stations in a local market places cable operators at a disadvantage in retransmission consent carriage negotiations and therefore should be prohibited.[173]

This may become a more complex issue as broadcast stations begin to use their digital multicast capability to offer multiple signals that may include the signals of more than one network. As explained earlier, tying these secondary or tertiary digital signals to retransmission consent negotiations involving the broadcaster's primary signal might prove the most effective way for smaller broadcast networks to obtain carriage on cable systems. It is unlikely that the local affiliates of these new networks will become one of the four top stations in local markets in the near future, but a multicasting broadcaster may try to tie MVPDs' rights to carry its major network signal to carriage of its multicast signals.

Proposal: Place set-top boxes in customer premises that pick up local broadcast station signals off the air without requiring MVPDs to retransmit broadcast signals.

The cable industry appears to be seeking a technological fix that might allow it to escape retransmission consent requirements, at least in those areas where subscribers are able to obtain broadcast signals off the air. CableLabs says it is developing specification for an interface that would let set-top boxes in a subscriber's

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[172] (...continued)
process for markets with 11 or fewer TV stations in which two top-four stations sought to merge. The FCC would evaluate on a case-by-case basis whether such stations would better serve their local communities together rather than separately. Under the waiver standard that applied for all markets, the FCC would consider permitting otherwise banned two-station combinations or three-station combinations if one station was "failed, failing, or unbuilt." The standard was liberalized by removing the requirement that an applicant for such a waiver "demonstrate that it has tried and failed to secure an out-of-market buyer for the failed station."

[173] See Ted Hearn, "Broadcast-Station Cap Sought," *Multichannel News*, October 30, 2006, at p. 51.

home receive digital broadcast signals off the air.[174] In effect, the set-top box would incorporate the equivalent of the old rabbit-ears or rooftop antenna that allow households to receive broadcast signals free off the air. This technology would allow households to see broadcast television signals alongside cable programming "as an integrated viewing experience." This appears to be an attempt to improve cable systems' bargaining position with broadcast television stations operators by providing set-top boxes to their customers that would receive all the local broadcasters' digital signals "for free" without the cable companies having to pay for the right to retransmit the signals.

Since this could be a threat to the retransmission consent/must-carry regime set up by Congress, and since broadcasters are seeking modification of the must-carry option to require MVPDs to carry local broadcasters' multiple digital signals, not just the primary signal (as currently required by law), it is likely that this technological development will play a role in any attempt to modify the current statute.

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

Section 628 of the Communications Act, which directs the FCC to establish rules to prevent a vertically integrated cable operator from discriminating in the prices, terms, and conditions at which it makes its programming available to non-affiliated MVPDs or have exclusive access to the programming in which it has an attributable interest, applies only if the vertically integrated company's programming is transmitted to distributors via satellite. It does not apply to programming that is transmitted to distributors over terrestrial facilities (for example, over broadband lines), an exception that frequently applies to regional sports networks and potentially could apply to all cable program networks as broadband fiber optic cable becomes more widely deployed. Some parties have proposed closing this "terrestrial loophole." There does not appear to be any basis for treating programming that is transmitted terrestrially differently from programming that is transmitted by satellite.

Proposal: Clarify the definition of a regional sports network.

Based on its concern that Comcast and Time Warner, after acquiring the cable systems of the bankrupt Adelphia and exchanging systems among themselves to increase their cluster sizes, might have the market power to "make or break" unaffiliated regional sports networks (RSNs) by choosing not to carry them, the FCC conditioned approval of the license transfers on allowing unaffiliated RSNs to use commercial arbitration to resolve disputes regarding carriage on Comcast or Time Warner cable systems.[175]

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[174] Todd Spangler, "Trying to Beat Broadcast Over the Ears," *Multichannel News*, March 12, 2007, at p. 6.

[175] See *In the Matter of Applications for Consent to the Assignment and/or Transfer of Control of Licenses: Adelphia Communications Corporation (and subsidiaries, debtors-in-possession), Assignors, to Time Warner Cable Inc. (subsidiaries), Assignees; Adelphia* (continued...)

For the past two years, The America Channel (TAC) has attempted without success to gain carriage of its programming on the cable systems of Comcast, Time Warner, and other large MVPDs, though it has reached carriage agreements with some overbuilders and new telephone company entrants into the MVPD market. Its announced programming format was uplifting programming that would profile ordinary people doing extraordinary things, but it did not have actual programming available. It sought carriage agreements to use as the basis for gaining the necessary financing, reportedly stating that "Without a carriage deal, or at least a placeholder that signifies carriage will be forthcoming upon launch, financial investors are reluctant to commit capital."[176]

After the FCC adopted its order approving the Adelphia/Comcast/Time Warner license transfers, TAC modified its programming format, combining regional broadcasts of more than 600 NCAA Division I women's and men's sports games and matches "with real-life drama about the aspirations, achievements, challenges, adventures, community service, and lifestyles of students and student athletes."[177] In so doing, TAC sought confirmation by the FCC that it met the definition of a regional sports network in the FCC's Adelphia order and therefore could demand arbitration if either Comcast or Time Warner refused to carry its programming.[178]

The right to go to arbitration would not necessarily result in an arbitration decision requiring Comcast and Time Warner to carry TAC. But it would create the possibility of such an outcome, which might in turn encourage other program networks to include in their programming the minimum amount of sports programming needed to meet the definition of an RSN, in order to gain the right to demand arbitration with Comcast and Time Warner. Based on the concern that such an outcome could be expanded to cover other MVPDs, a number of MVPDs have filed at the FCC oppositions to the TAC filing, based on the argument that they do not sign carriage agreements with networks before the networks start programming. TAC has responded by providing examples meant to demonstrate "that it is common industry practice for a network to launch and produce programming only after a foundational carriage agreement" has been reached.[179]

Although parties on both sides of this issue have met with FCC commissioners, the Commission has not yet formally addressed this issue. Some have proposed that

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[175] (...continued)
Communications Corporation (and subsidiaries, debtors-in-possession), Assignors and Transferors, to Comcast Corporation (subsidiaries), Assignees and Transferees; Comcast Corporation, Transferor, to Time Warner Inc., Transferee; Time Warner Inc., Transferor, to Comcast Corporation, Transferee, Memorandum Opinion and Order, adopted July 13, 2006, released July 21, 2006, at para. 181.

[176] See Jonathan Make, America Channel's Carriage Quest Spurs Pay-TV Concern," *Communications Daily,* May 25, 2007, at pp. 3-5.

[177] See [http://www.americachannel.us/overview.php], viewed on June 29, 2007.

[178] See Jonathan Make, America Channel's Carriage Quest Spurs Pay-TV Concern," *Communications Daily,* May 25, 2007, at pp. 3-5.

[179] Id.

the FCC hold a proceeding in which it could review the current definition of regional sports network and make any modifications needed to block a failed program network from demanding arbitration just by offering some minimum amount of sports programming.