Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of	)	
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Annual Assessment of the Status of	)	MB Docket No. 07-269
Competition in the Market for the	)	
Delivery of Video Programming	)	
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REPLY COMMENTS OF FREE PRESS

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REPLY COMMENTS OF FREE PRESS

Free Press respectfully submits these reply comments in response to the Federal Communication Commission's ("FCC" or "Commission") request for comment on the state of the marketplace for multichannel video programming distributors (MVPDs).[1] The following analysis presents a snapshot of the MVPD marketplace and highlights several problems occurring within the MVPD space with regard to pricing competition and customer experience.

As this proceeding makes clear, a litany of issues face the MVPD marketplace. Issues have arisen over vertical and horizontal consolidation, program carriage agreements, a competitive equipment market, wholesale tying or bundling of programming, leased access, terrestrial loophole and discrimination against public, educational, and governmental channels. Free Press takes this opportunity to address what we believe are some of the most pressing concerns. In particular, we highlight increasingly high prices, dwindling network investment, and a lack of consumer choice amongst key aspects of the MVPD market.

Additionally, in light of the D.C. Circuit's recent ruling on cable ownership limits,[2] the Commission should launch a broad inquiry into the various and interrelated consumer issues present in the cable industry. In the Cable Act Congress directed the Commission to promote

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[1] *Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, MB Docket No. 07-269, Supplemental Notice of Inquiry, 24 FCC Rcd 4401 (2009) (*MVPD NOI*).
[2] *See* "Court throws out FCC cable ownership limit," *Reuters*, Aug. 28, 2009.

competition, consumer choice, and a diversity of programming and provided the Commission with a variety of tools to ensure cable customers gain access to the full benefits of this distribution medium. We encourage the Commission to move expeditiously in initiating an inquiry and to develop a comprehensive record on the issues affecting consumers in this market.

I. Despite Increased Profits, Industry Investment Continues to Decline

The Commission requests comment on the whether the industry is "continuing to invest in system upgrades and service improvements."[3] The cable industry has devoted much paper to chronicling its investment in cable infrastructure, and, based on their comments, one would assume the industry was investing at record levels.[4] In fact, when viewed through the appropriate metric – investment as a percentage of revenue – the exact opposite is true. Despite windfall profits, cable operators are *decreasing* their investment levels.[5] For example, Comcast's capital expenditures as a percentage of revenue dropped from 19.8% in 2007 to 16.8% in 2008.[6] For 2009, Comcast expects "full year CapEx will be both lower in absolute dollars and as a percentage of revenue when compared to 2008."[7] Consistent with that statement, Comcast has maintained a 12.8% CapEx level through the first half of 2009.[8]

Moreover, the money allocated to investment does not appear to be committed to system upgrades or service improvements. Rather, cable investments are primarily dedicated to low-risk, growth-responsive outlays of funds – not higher-risk, forward looking investments that spur innovation and competitive markets. Indeed, in a recent earnings call, Comcast stated in that,

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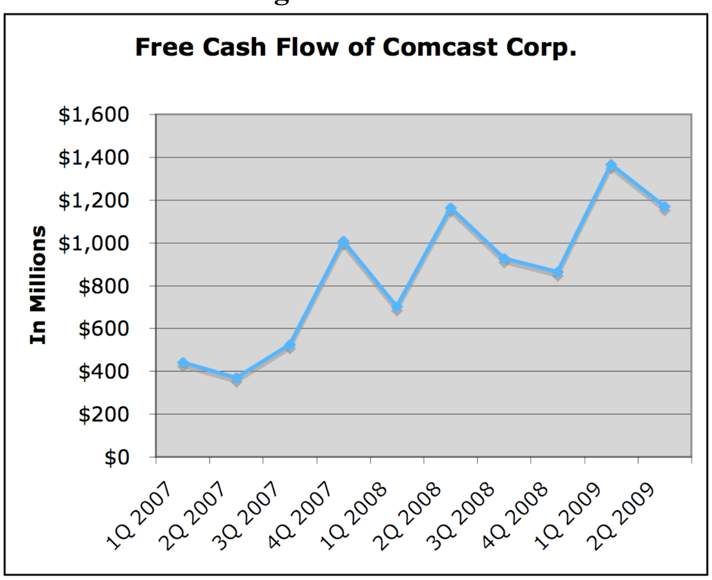
[3] *MVPD NOI* at para. 7.
[4] *See, e.g.,* Comments of National Cable and Telecommunications Association at 17 (May 20, 2009).
[5] *See, e.g.,* Comcast Corporation, Trending Schedules, Aug. 6, 2009, p. 3.
[6] *Id.*; Comcast Corporation, "Comcast Reports Fourth Quarter and Year End Results," Press Release, Feb. 18, 2009.
[7] Comcast Corporation, Q1 2009 Earnings Call Transcript, *Seeking Alpha*, April 30, 2009, p. 3.
[8] *See* Comcast Corporation, Trending Schedules, Aug. 6, 2009.

"consistent with historical trends capital expenditures continues to be predominantly growth oriented with growth CapEx accounting for 71% of cable CapEx for the year."[9] In other words, the nearly all the capital expenditures are "directly tied to revenue generation,"[10] and not to infrastructure upgrades.

II. In Spite Of Increased Industry Revenues Consumers Face Higher Rates and Fewer Choices

While cable industry profits are demonstrating robust margins, the benefits are not being passed onto consumers. Instead, consumers are confronted with mounting costs and diminished choice with regard to programming, set-top boxes, and interactive program guides. Comcast's free cash flow – that is, the amount of money made vs. spent – has increased dramatically in the last two years (see Figure 1).[11]

Figure 1:



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[9] Comcast Corporation, Q4 2008 Earnings Call Transcript, *Seeking Alpha*, Feb. 18, 2009, p. 4 (*Comcast Q4 2008*).

[10] Comcast Corporation, Q2 2008 Earnings Call Transcript, *Thomson StreetEvents*, July 30, 2008, p. 4.

[11] *See 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*, Report on Cable Industry Prices, 24 FCC Rcd 259, at para. 2 (2009) (*Cable Price Survey*).

A. MVPD Subscribers Continue to Face Rising Costs for Service Packages

Based on the claims of MVPD operators commenting in this proceeding, one would expect that the costs to cable subscribers would be decreasing due to competition in the MVPD marketplace. That does not appear to be the case. The latest Commission report on cable industry prices shows consumer bills on the rise – indeed, the Commission has yet to document a decline since it began tracking cable prices in 1995.[12] In 2008, cable subscribers saw the highest year-over-year percentage increase in the previous three years.[13]

The costs of service packages have steadily increased despite claims of "vigorous competition" from wireline and satellite video competitors. While AT&T or Verizon video offer service to more than a quarter of Comcast's footprint,[14] the unfortunate reality is that the emergence of telephone competition has simply offered consumers another avenue to be overcharged.[15] Research suggests that the emergence of a wireline video competitor in a market where there is an incumbent cable provider doesn't guarantee reduced costs for wireline or cable customers. A study by the University of Minnesota on the effect of statewide video franchising legislation in three states found that while prices decreased only marginally in one of the states,[16] in the other two "…prices (corrected for core inflation) grew by 69 and 22 percent."[17] The author's explanation for this counterintuitive result is that oligopolistic competition, as between

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[12] *Id.*

[13] *Id.*

[14] "The RBOCs now have over built 28% of our footprint" Comcast Corporation, Q2 Financial Call Transcript, Aug. 6, 2009.

[15] For instance, the cost of the FiOS "Premier" TV package has increased twice since it was first offered. Ritsuko Ando, "Verizon raises price for FiOS TV service," *Reuters*, Nov. 20, 2007. AT&T is no different. Jeff Richgels, "AT&T hikes U-Verse prices, adds packages," *The Capital Times*, Dec. 31, 2008.

[16] "Statewide Video Franchising Legislation: A Comparative Study of Outcomes in Texas, California and Michigan," University of Minnesota, Prepared for the Minnesota Department of Commerce, March 2009, p. 16.

[17] *Id.*

incumbent cable provides and new wireline entrants, often results in price escalation."[18] As a result of telephone companies' bundling practices "incumbent (cable) providers do not have an incentive to lower their prices, since their rivals are raising theirs."[19] This also suggests that claims by telephone companies that "every year franchise reform is delayed takes more than $8 billion out of consumers' pocketbooks,"[20] should be taken with a grain of salt.

The Commission's most recent cable price survey also found that, despite the existence of a wireline competitor, costs to consumers continue to rise.[21] Nor does competition from direct broadcast satellite (DBS) providers compel price reductions. As the Commission found, "it does not appear from these results that DBS effectively constrains cable prices."[22] As a consequence, the Commission should treat industry claims that "the marketplace for the delivery of video programming is diverse, dynamic and fiercely competitive,"[23] with skepticism – particularly when such competition has not resulted in price relief for consumers.

To justify the undeniable fact that prices have steadily increased despite so-called competition, cable providers often argue that the cost per channel is actually decreasing, but customers are paying more because they are getting more in terms of the number channels available in programming bundles.[24] This argument, while convenient, is ultimately unpersuasive. As a practical matter, most cable customers watch only a fraction of the channels

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[18] *Id.*
[19] *Id.*
[20] Testimony of Verizon Executive Vice President Tom Tauke, Communications, Consumer's Choice and Broadband Act of 2006, Senate Commerce Committee (May 25, 2006).
[21] *See Cable Price Survey* at Chart 1-a.
[22] *Id. at* para. 3.
[23] Reply Comments of the National Cable and Telecommunications Association at 1 (June 22, 2009).
[24] *See, e.g.,* Letter from Kyle McSlarrow, National Cable and Telecommunications Association, *See 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. 02-266, at 2 (Jan. 4, 2007).

they are forced to pay for. As the General Accounting Office (GAO) found in a report to the Senate Commerce Committee, "most people, on average, watch only about 17 networks."[25] However, by and large, cable subscribers are not given the option of subscribing to a smaller package. As a consequence, cable operators force customers to pay more, albeit at a lower rate, for something they didn't want in the first place. Allowing subscribers to purchase smaller bundles at the reduced per channel rate would result in a far more cognizable value to the consumer.

In any event, it's clear that there is no legitimate reason to corral consumers into super-sized channel packages. In the second quarter of 2008 Comcast saw their video programming expenses *decrease* by $8 million compared to the first quarter of 2008 (from $277 million to $271 million). At the same time Comcast raised its customers' average monthly bill by $3.00 (from $106.70 to $109.61). [26] Undoubtedly a portion of these price increases can be attributed to the practice of programmers requiring MVPDs to include the full suite of channels in order to receive more popular programming.[27] We encourage the Commission to act to protect consumers against price gouging by dominant programmers, the costs of which are directly passed onto consumers.

B. The Lack of Competition in the Set-Top Box Market Has Resulted In Higher Prices and Fewer Options for Consumers

Not only are consumers being gouged on the price of service packages, they also face unjustifiably high equipment costs. For example, the average price of set top boxes has risen

[25] *Issues Related to Competition and Subscriber Rates in the Cable Television Industry*, U.S. General Accounting Office, GAO-04-8, p. 37 (October 2003).
[26] *See* Comcast Corporation, Trending Schedules, Aug. 6, 2009.
[27] *See, e.g., Implementation of the Cable Television Consumer Protection and Competition Act of 1992, Development of Competition and Diversity in Video Programming Distribution.* Report and Order and Notice of Proposed Rulemaking, 22 FCC Rcd 17791, 17862-17863, para. 120 (2007).

from $9.95 per month in 2007 to $15.95 per month in 2009.[28] This price increase is not tied to any actual increase in the cost of set-top boxes. In fact, Comcast is generating returns on box rentals that "are even better than the 35% to 40% [Comcast] projected due to reduced box costs, higher revenue per customer and lower churn."[29] Yet, despite these operational savings, Comcast *increased* the monthly cost of DVR service during the same quarter this statement was made.[30] While cable operators continue to make more money, customers are actually charged *more*.

Cable operators can charge exorbitantly high rates for set-top boxes because consumers have few alternatives than to rent equipment from the cable company.[31] Congress has instructed the Commission to "assure the commercial availability"[32] of equipment from manufacturers not affiliated with any MVPD distributor so that "consumers are not forced to purchase or lease a specific, proprietary converter box, interactive device or other equipment from the cable system or network operator."[33] Nevertheless, a viable market for independently manufactured set-top boxes has not emerged. This can be largely attributed to the failure of the Commission's

[28] Carolyn Y Johnson, "Comcast, Verizon raising prices for HD DVR service," *Boston Globe*, Aug. 11, 2007; Comcast Raising Rates," *Satellite TV*, Oct. 6, 2008, available at http://www.dish-television.com/2008/10/06/comcast-raising-rates/.
[29] *Id.*
[30] *Id*.
[31] The ten largest cable operators, serving nearly 90% of cable subscribers in the U.S., have deployed less than 440,000 CableCARDS. As of December 2008, these ten operators have more than 51.5 million subscribers. *See Commercial Availability of Navigation Devices*, Report of National Cable and Telecommunications Association, CS Docket No. 97-80, at 1 (June 26, 2009); National Cable and Telecommunications Association, "Top 25 MSOs," available at http://www.ncta.com/Stats/TopMSOs.aspx.
[32] *Cable Television Consumer Protection and Competition Act*, Pub. L. 102-385 (1992), codified at 47 U.S.C. § 521 *et seq*.
[33] Joint Explanatory Statement of the Committee of Conference, S. Conf. Rep. 104-230, 104th Cong., 2d Sess. at 181 (1996).

"CableCARD" regime and the repeated grant of 629 waivers for set-top box manufacturers.[34] We understand and support the Commission's desire to see cable operators transition to all-digital networks. But the goal of a competitive retail market for set-top boxes that frees consumers of burdensome lease agreements should not be sacrificed along the way.

The failure of the CableCARD regime can also be attributed to incumbent cable industry control over the standard setting process for third party set-top boxes and the lack of incentive for cable operators to ensure functionality of a competitor's equipment. The Commission itself expressed reservations about whether a cable-controlled process would provide sufficient "opportunity for a range of interests to participate."[35] Nevertheless, the cable companies have dominated the standard setting processes and have implemented a poor system of CableCARD deployment and failed to adequately support third-party devices. As a result, those few consumers who purchase an independently manufactured CableCARD-enabled device, such as TiVo, face substantial hurdles in ensuring a fully capable device.[36] Of course, given the huge windfall cable operators derive from renting set-top boxes on a monthly basis, they have little motivation to facilitate a market for third-party equipment.[37] Consequently, consumers continue to be overcharged month after month for a piece of equipment that has already been paid for many times over.[38]

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[34] *See, e.g.,* Comments of TiVo Inc. at 6-9. (July 29, 2009).

[35] *Implementation of Section 304 of the Telecommunications Act of 1996: Commercial Availability of Navigation Devices*, CS Docket No. 97-80, Report & Order, at para. 125 (Feb. 20, 1997). *See also* Comments of Verizon at 5 (May 20, 2009).

[36] *See, e.g.,* Comments of TiVo Inc. at 4-6. (July 29, 2009).

[37] *See, e.g.,* Erica Ogg, "Comcast introduces open-cable platform," *CNET News*, Jan. 8, 2008.

[38] A closely related issue of industry lock-down on technology concerns the design of electronic program guides currently offered to consumers. While many electronic and web interfaces provide consumers with myriad methods to navigate content, MVPDs for years have offered a virtually identical interface. Despite two-way, interactive technology existing for decades the interactive program guide and video on demand features were only recently offered. Multi-tasking consumers move from the intuitive interfaces

(continued on next page)

We urge the Commission to recognize this reality and take swift action on behalf of consumers to ensure they experience the competition Congress intended. History will look back at provider-leased cable boxes in the same way we now view leased rotary telephones from Ma Bell – anachronisms that were characteristic of monopolistic business practices. The sooner the Commission can chart a path away from this situation, the better.

III. Independent Cable Programmers Face Significant Barriers to Entry

Customers are not the only ones suffering from lack of effective competition in the MVPD market. Independent programmers also face substantial hurdles in gaining access to carriage by platform gatekeepers. Vertical integration by studios, networks, and cable operators, and near complete domination by a handful of major companies has pushed many independent programmers off the dial. Unfortunately, this lack of competition has disproportionately affected independent minority-owned and minority-targeted programming.[39]

As one network CEO explained, "Cable and satellite TV companies want to own you before they put you on television."[40] Similarly, a consultant for start-up networks affirmed, '[t]he landscape is intensely difficult right now….you need an equity partner these days among distributors, and there aren't that many guys that will take an equity interest.'[41] For example, the

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(footnote continued)
of iPods and webpages to the archaic experience of the set-top box. This is an area where a competitive market is desperately needed. Without Commission action, consumers will continue to have their home viewing experience defined by an industry that took thirty years to offer customers a single interactive video service. *See e.g.* Thomas R. Eisenmann, "The U.S. Cable Television Industry, 1948-1995: Managerial Capitalism in Eclipse," *The Business History Review*, Vol. 74, No. 1 (Spring 2000), pp. 8-9.

[39] *See* Adam Lynn and Mark Cooper, "Minority Programming: Still at the Back of the Bus," Presented at the 2008 International Communication Association Conference (May 24, 2008). Perhaps most poignantly, the CEO of the Black Family Channel (which has abandoned its efforts to gain distribution from cable operators) has advised,"[t]oday, if you want to start a cable network, it might be easier to schedule a ride to the moon." Bobby White, "TV Channels Move to Web, Think Outside the Cable Box," *Wall Street Journal*, August 10, 2007.

[40] "Blacks Support Congress Bill for Fairness in Television Opportunities," *DogonVillage.com*, 2006.

[41] Shirley Brady, " Are Independents' Days Over?" *CableFAX*, June 20, 2005.

U.S. Olympic Committee sought a partnership with Comcast before launching the cable network.[42] The channel is already available on Comcast's standard digital tier. Less successful is the Horror Channel, who has not partnered with any platform distributor, and has yet to strike a programming deal with a single cable or satellite operator.[43] Conversely, the Comcast-partnered horror channel, FEARnet, enjoys distribution on Comcast's platform.[44]

The lack of diversity in programming sources does not serve the public. We encourage the FCC to initiate further inquiry into the availability of distribution opportunities for independently supplied programming on MVPD platforms, and in particular to address the impact of vertical integration on independent program supply.

CONCLUSION

The promise of rigorous MVPD competition has not come to pass and cable operators maintain a firm grip over consumer choice. Not only should the Commission take these trends into account when crafting its annual report to Congress, the FCC should launch a comprehensive inquiry into competition, consumer choice, and a diversity of programming available to the public.

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[42] According to press reports, the benefits to consumers were not part of the negotiations. *See e.g.* Tripp Mickle and John Ourand, "USOC, Comcast Announce Plans To Launch New Olympic Network," *SportsBusiness Journal*, July 8, 2009. ("USOC COO Norm Bellingham said the financial terms of the Comcast partnership are "confidential," but people familiar with negotiations said the USOC expects up to $30-40M in annual advertising to Comcast in exchange for distribution and support of the channel…Comcast also was swayed by a personal appeal from former USOC Chair Peter Ueberroth, who persuaded Comcast head Brian Roberts that Comcast's support for a non-profit channel focused on the Olympics could offer both political and financial benefits.").

[43] *See* http://www.horrorchannel.com/wheretofind.html

[44] *See, e.g.,* Devin Leonard, "This horror show oozes money," *Fortune*, Sept. 4, 2008.

Respectfully Submitted,

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