Testimony of Hal J. Singer, Ph.D.

BEFORE THE COMMITTEE ON ENERGY AND COMMERCE

SUBCOMMITTEE OF COMMUNICATIONS AND TECHNOLOGY

"THE SATELLITE TELEVISION LAW: REPEAL, REAUTHORIZE, OR REVISE?"

JUNE 12, 2012

Summary of Testimony

- The potential harm presented by vertical integration in the cable industry is a reduction in innovation among independent content providers. The harm manifests itself in the form of fewer programming choices and less *programming diversity*; the harm does not necessarily involve a short-run price increase or output reduction, as one would expect to find from an antitrust violation.
- The Cable Act of 1992 sought to alleviate this potential harm by permitting vertical integration but policing discriminatory conduct on a case-by-case basis.
- A reduction in innovation by independents caused by discrimination may not be cognizable under the antitrust laws, which were designed primarily to prevent the exercise of *pricing power*. Accordingly, antitrust is not the proper framework to adjudicate discrimination complaints. Instead, the FCC should adjudicate these disputes under the public-interest standard.
- With the exception of must-have networks, because few cable customers would be willing to switch video providers due to the loss a single network, complainants should not be required to estimate forgone benefits from broader carriage to prevail in a program-carriage complaint.

Testimony

As the subcommittee on Communications and Technology considers reauthorizing the Satellite Act and possible changes related to the video marketplace, it should also evaluate the non-discrimination protections in the Cable Act and whether they work as intended. The focus of my testimony is the proper regulatory oversight of vertically integrated cable operators, and the role of the Federal Communications Commission (FCC) in that oversight process.

To design the proper regulatory framework, one must first understand the nature of the potential harm presented by vertical integration in the cable industry—namely, a reduction in innovation among independent content providers ("independents"). Why do we care about that potential harm? Because some of the best content has sprung and will likely continue to spring from independents, who are free from the strictures of a clumsy conglomerate when creating artistic expressions. Without any protection against discrimination, independents would be forced to surrender equity in exchange for carriage, and thus would be less willing to take risks, which would result in fewer programming choices and less *programming diversity*. For example, if an independent network knew that five years after its launch, it would be competing for the rights to a major sporting event against a vertically integrated cable operator that could deliver 30 million more viewers for its affiliated sports network at the flip of a "master switch," the independent might abandon the entire enterprise.

There are two schools of thought on how best to deal with this problem of vertical integration. The first, advocated by Professor Tim Wu in his best-selling

book *The Master Switch*, is to ban vertical integration entirely. The second, which was embraced by Congress in the 1992 Cable Act, is to permit vertical integration but to police discriminatory acts on a case-by-case basis. The downside of an outright ban is that is sacrifices potential efficiencies related to vertical integration. The downside of the case-by-case approach is that, if relief from discrimination does not come swiftly, or if the evidentiary burden imposed on an independent cannot be satisfied under any fact pattern, then after-the-fact adjudication affords no protection at all.

Assuming that case-by-case review is the best solution to the problem of vertical integration—and in light of recent proceedings, it is not clear whether that is the case—the policy question turns to which legal framework is best suited for the task: Should the FCC adjudicate these disputes under its public interest standard, or should complaints of discrimination by a vertically integrated cable operator be addressed under the antitrust laws? The problem with the latter approach is that a reduction in innovation by independents—the harm that the Cable Act intended to insure against—may not be cognizable under the antitrust laws, which were designed primarily to prevent the exercise of *pricing power*. As a practical matter, no private litigant would ever risk the resources to bring a discrimination case into an antitrust court unless it could also link the restraint to a short-term price or output effect. Because this will generally be impracticable, antitrust is the wrong framework to address discrimination by a vertically integrated cable operator. To borrow an analogy from labor laws, we do not turn a blind eye toward discrimination in the workplace so long as there is no associated

wage effect; rather, discrimination is pernicious because it denies an equally qualified applicant the opportunity to compete on a level playing field.

The lack of price effects in these cases is also why it makes no sense to interpret the non-discrimination protections of the Cable Act in an antitrust context—even if Congress used the word “unreasonably” in the statute. By seeking to identify harm to an independent programmer rather than harm to competition, Congress meant to fill a *gap* in antitrust protection—namely, the preservation of diversity in the video-programming marketplace. How do we know? At the time the Cable Act was passed, the largest cable operator in the country, TCI, controlled less than 20 percent of national video subscribers. If Congress meant to import antitrust concepts into the Cable Act, as some now argue, then Congress also intended to immunize *all* vertically integrated cable operators, including TCI, from the non-discrimination protections of the Act, as none would have sufficiently high market shares to satisfy the monopoly-power requirement of the antitrust laws. The absurdity of this conclusion—that Congress passed redundant antitrust regulation that was applicable to no one—proves that the Cable Act has nothing to do with antitrust enforcement. It also proves that discrimination by a vertically integrated cable operator is best adjudicated by the FCC under the public-interest standard.

Finally, I would like to speak briefly about the appropriate evidentiary burden imposed on complainants under this FCC-administered approach. The purpose of the Cable Act is to ensure that a vertically integrated cable operator does not consider the benefit to its upstream programming affiliate when making carriage decisions of a similarly situated independent network. There are two

primary ways to establish evidence of this kind of “biased” decision-making. Complainants could show *direct* evidence that benefits to an upstream network were inappropriately considered. In the absence of such direct evidence, complainants could in theory establish that the downstream cable division incurred a loss by carrying the independent network narrowly; this finding would create a presumption that the vertically integrated operator would not have incurred such a loss without there being an offsetting benefit to the upstream network. However, this *indirect* method of proof is often thwarted by the fact that many episodes of tiering do not entail a change from broad carriage to narrow carriage, which could permit estimation of the cable operator’s forgone benefits from broader carriage. Moreover, with the exception of a handful of networks such as ESPN, most independent networks lack “must-have” status and thus would be hard-pressed to demonstrate any forgone benefit from broader carriage. Cable operators generally create value for their customers by offering a *buffet* of choices as opposed to granting access to any particular network. Requiring an independent to estimate forgone benefits with precision would be tantamount to asking a leading columnist for the *New York Times* to estimate what fraction of subscribers would switch to another newspaper if the editorial page excluded that columnist. That the answer might be none—due to the costs of switching newspapers or due to customer loyalty attributable to the paper’s content generally—does not imply that the columnist adds no value to the *Times*. Accordingly, complainants should not be required to estimate forgone benefits from broader carriage to prevail in a program-carriage complaint, as the current law now demands. By making the evidentiary

burdens under the case-by-case approach too extreme, we risk undermining the non-discrimination protections of the Cable Act. And if that's the case, then Professor Wu's suggested remedy of an outright ban is the only remaining policy option to protect against the harm of vertical integration.