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THE SATELLITE TELEVISION LAW: REPEAL, REAUTHORIZE OR REVISE?

before the

SUBCOMMITTEE ON COMMUNICATIONS AND TECHNOLOGY
COMMITTEE ON ENERGY AND COMMERCE

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Good morning Mr. Chairman, Ranking Member Eshoo, and Members of the Subcommittee. My name is Amy Tykeson, and I am President and CEO of BendBroadband. I appreciate the opportunity to appear before you today to consider the reauthorization of the Satellite Television Extension and Localism Act of 2010 ("STELA").

In my testimony, I want to bring to your attention some of the challenges that confront cable operators – particularly smaller operators – in today's video marketplace. The competition that cable operators face from satellite companies with national footprints, from well-funded telco-video providers with established customer bases, and, increasingly, from a host of new Internet-based sources of video programming, is formidable.

But the challenges I want to discuss today are those that cable operators face as they attempt to navigate a path through a marketplace where outdated, unnecessary and often one-sided rules are combined with an increasingly consolidated programming marketplace. This combination of factors is preventing cable operators from giving consumers the video service that they want, at reasonable prices, using the most innovative technologies available.

My testimony today will focus on three examples of how today's video marketplace would benefit from targeted reforms. These three examples are:

1. **The barriers to creating programming packages that respond to consumers' needs and demands;**

2. **The breakdown of the retransmission consent process, which is harming consumers; and**

3. **The unnecessary costs imposed on cable consumers by requiring separable security in set-top boxes.**

BendBroadband: From Community Antenna Service to Provider of Advanced Communications Services.

Let me begin by discussing my experience at BendBroadband, which is a second generation, family-owned business serving the tri-county area of Central Oregon. Our origins trace back more than 50 years to a small community antenna television facility constructed for the purpose of bringing broadcast television signals to viewers in Bend, Oregon. Today BendBroadband is a nationally-recognized independent business that was the first "traditional" cable system in the country to transition to 100 percent all-digital service.

Our system, which has more than 2,000 miles of fiber and coax infrastructure, delivers advanced video, voice and Internet services to approximately 50,000 commercial and residential subscribers in Central Oregon, a region with about 180,000 people. We also operate a Tier III, LEED Gold, colocation data center that serves the regional medical community and is a catalyst for economic development. At BendBroadband, we are proud of our reputation as

a progressive employer and engaged corporate citizen in the local communities we serve. We are the 14th largest employer in the region, with 270 associates.

Our company's evolution from a basic community antenna service to a provider of advanced communications services mirrors the evolution of the cable industry as a whole. When many of today's cable regulations were put into place, traditional cable systems were labeled "monopolies." Today, the nation's cable systems are vying on a daily basis with a host of competitors to attract and retain digital video, voice, and data customers.

The emergence of a robustly competitive communications marketplace and the rapid advancement of technology over the past two decades go hand-in-hand. Advances in technology have enabled competition and competition has spurred advances in technology. The cable industry and BendBroadband have been at the vanguard of this virtuous cycle. The cable industry has invested billions of dollars to upgrade facilities and develop and deploy new services including high-speed broadband, digital video and voice products.

These investments, which ultimately benefit consumers, are not limited to the larger cable operators; BendBroadband has invested $100 million dollars over the past seven years in order to provide our customers with the most advanced and diverse array of services possible.

The Cable Market Has Evolved, But the Laws Governing Cable Have Not.

The cable industry clearly has been moving forward. But the laws and regulations governing the industry have not. A snapshot of the cable market taken in 1992 would have shown a market in which traditional cable systems had a 98 percent market share.[1] But a snapshot of the cable market today shows a much different picture.

Today, virtually every consumer has at least two and sometimes three alternatives to the incumbent cable operator (*i.e.*, the two national satellite providers and, often, a telco-video provider like Verizon FiOS or AT&T U-Verse). As a result, cable's share of the multichannel market has dropped from 98 percent to 56 percent.[2]

In addition, cable operators no longer are the dominant players in the video programming universe. Cable operator ownership of non-broadcast cable networks has declined from more than 50 percent in 1992 to only 14 percent today.[3] At the same time, the "Big Four" broadcast networks have consolidated ownership of cable programming channels and now control at least 60 percent of the non-broadcast cable programming channels.

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[1] *See* Hearing on the State of Video, Subcommittee on Communications, Technology, and the Internet of the Committee on Commerce, Science and Transportation (May 14, 2013) (Testimony of Michael K. Powell, President and CEO, National Cable & Telecommunications Ass'n. ("*Powell Testimony*").

[2] *Id.*

[3] *Id.*

With this background in mind, I want to discuss three examples of areas ripe for reform as Congress considers the reauthorization of STELA.

1. The Barriers to Creating Programming Packages That Respond to Consumers' Needs and Demands.

As noted above, a handful of large programmers, including the Big Four national broadcast networks, have become the dominant providers of video programming. One of the ways that these programmers have achieved their positions of dominance is by engaging in a series of practices that are sharply driving up the cost of programming and adversely impacting consumer choice.

In particular, the major program suppliers each control a dozen or more channels. However, only a few of these channels contain "must have" programming. The rest either are far less valuable to customers (and thus would have difficulty achieving widespread distribution on their own) or they are expensive, niche channels. In the past, cable operators sought to keep the price of basic cable service affordable by providing optional tiers and expanded levels of service.

But programmers, drawing on the market power that they derive from their must have channels, are requiring cable operators to carry all of their channels on broadly available tiers. These practices are costing operators, and ultimately consumers, billions of dollars in increased programming expenses.

Our customers are signaling to us by word and action that they want more choice in the programming they purchase both in terms of the channels offered and the prices charged. Unfortunately, our ability to create such packages is limited by programming contracts. As a result, multichannel video programming distributors (MVPDs) have little control over the input costs of our video offerings or the make-up of the packages that we offer to consumers. In addition, independent programmers are often losing out under this system.

While the major programmers' bundling and tiering practices are a growing problem for all MVPDs and their customers, they present unique difficulties for smaller operators. Because some of our communities have been hit especially hard in the recession, smaller, less expensive packages of programming would be a welcome option for consumers. But small operators lack leverage and are largely presented with take it or leave it offers with little or no room for negotiation.

Smaller operators (and operators with a small footprint in a local market) also can face discrimination in the prices and terms they are offered compared to the prices and terms offered to larger companies. Programmers charge higher prices and offer less attractive terms to cable operators with fewer customers despite the absence of quantifiable cost differences to justify these price

differences. As a result, the impact of rising programming fees is felt more acutely by small cable operators, a finding recently affirmed by industry analysts.[4]

Congress sought to protect smaller operators from discriminatory and unfair programming practices by extending "program access" protections to programming buying groups. However, the regulations adopted by the FCC in 1993, particularly the definition of a "buying group," prevent the nation's largest programming buying group, the National Cable Television Cooperative ("NCTC") from availing itself of the law's protections as Congress intended. The FCC is now considering and should adopt updated rules that would allow a buying group, like the NCTC, to file program access complaints and would also create safeguards to prevent programmers from evading the rules. It is vital that the FCC act now to update the rules applicable to buying groups by making it clear that programmers must treat buying groups comparably to other MVPDs and prohibit the arbitrary exclusion of certain buying group members from joining a master agreement.

Cable operators and other distributors should be able to offer consumers choice and flexibility that 21st Century technology enables. And, we welcome a dialog on these issues.

[4] Moody's, Smaller US Cable Operators to Feel the Brunt of Rising Programming Costs, May 2, 2013 *available at* http://www.moodys.com/research/Moodys-Smaller-US-Cable-Operators-to-Feel-the-Brunt-of--PR_272253.

2. The Breakdown of the Retransmission Consent Process, Which is Harming Consumers.

There is no small irony in the fact that the major broadcast networks are among the largest purveyors of non-broadcast cable channels today. In 1992, more than half of such channels were controlled by cable operators and Congress was concerned that those cable operators had the incentive and ability to threaten the future of local over-the-air broadcasting. Congress' answer was to create a new "retransmission consent" right that was supposed to ensure the "universal availability" of local broadcasting without harming consumers who subscribe to MVPD service.

Today, the retransmission consent process is benefiting the national broadcast networks far more than localism or the viewing public. This is because local stations' retransmission consent rights have been usurped by the major national broadcast networks who demand a share of their affiliates' retransmission consent revenues as "reverse compensation."[5] The resulting diversion of retransmission consent revenues from local stations to national broadcast networks does not help preserve localism as Congress intended. Rather, it provides a subsidy for the national broadcast networks' operations. It also subsidizes the

[5] For example, in May 2011 it was reported that NBC had entered into an arrangement with its affiliates under which NBC would hold its affiliates' proxies and negotiate retransmission consent deals on their behalf, with NBC pocketing as much as 50 percent of the revenues. *See* Harry A. Jessell, *NBC's Affiliate Retrans Plan is 50-50 Split*, TVNewsCheck, May 18, 2011 *available at* http://www.tvnewscheck.com/article/2011/05/18/51322/nbcs-affiliate-retrans-plan-is-5050-split.

national networks' cable channels – channels that siphon off programming and viewers from local over-the-air affiliates.[6] This puts even more pressure on the local affiliates to increase the retransmission consent fees that they demand from cable operators and other MVPDs.

As a result, retransmission consent negotiations are becoming more contentious and demands for retransmission consent fee hikes are spiraling upward at a dizzying pace. In 1992, Congress expected that the rough balance of power that then existed between local stations and cable operators would prevent either side from taking advantage of the other.[7] But the market has changed dramatically and local stations have been able to leverage their monopoly position (protected by government-guaranteed territorial exclusivity arrangements) to play competing MVPDs against each other. According to SNL Kagan, retransmission consent payments, which were all but non-existent in the 1990s, grew from $215 million in 2006 to nearly 2.4 billion in 2012 and are expected to top $3 billion this year.[8] By

[6] For example, after 50 years on CBS broadcast stations, next year the US Open Tennis Tournament will be moved to ESPN (which is vertically integrated with the ABC broadcast network). Such moves are made possible by the national networks using retransmission consent revenues.

[7] *See* S. Rep. No. 102-92 (1991) ("Senate Report") at 1168 (expressing expectation that demands for retransmission consent compensation would be modest because "broadcasters also benefit from being carried on cable systems"). *See also* 138 Cong. Rec. S643 (Jan. 30, 1992) (Statement of Sen. Inouye) ("It is of course in the mutual interests of these parties to reach an agreement: the broadcaster will want access to the audience served by the cable system, and the cable operator will want the attractive programming that is carried on the broadcast signal."); Implementation of the Cable Television Consumer Protection and Competition Act of 1992; Broadcast Signal Carriage Issues, Report and Order, 8 FCC Rcd 2965 (1993) at para. 115 (finding that "there are incentives for both parties to come to mutually beneficial arrangements" in retransmission consent negotiations").

[8] SNL Kagan, Economics of Broadcast TV Retransmission Revenue, May 15, 2013.

2018, retransmission consent fees are projected to double again, to more than $6 billion.[9] In short, obtaining access to "free" local television is becoming increasingly expensive for the tens of millions of homes that subscribe to cable or another MVPD.

This is not what Congress intended. Retransmission consent was never meant to be a subsidy for the national networks. In fact, during the debate over the 1992 Act, Members of Congress repeatedly stated that local stations, not the national networks were the intended beneficiaries of the new retransmission consent right.[10] Yet, despite those statements, and despite assurances by the broadcast industry that the national networks would play no role in retransmission consent,[11] today those networks take the position that they should be the ones benefitting from the retransmission consent rights granted by Congress to local

[9] *Id.*

[10] As Senator Inouye stated, Congress intended for retransmission consent to "permit local stations, not national networks…to control the use of their signals." 138 Cong. Rec. S562-63 (Jan. 29, 1992). Other members of Congress echoed Senator Inouye's statement. *See, e.g.*, 138 Cong. Rec. H6491 (July 23, 1992) (Statement of Rep. Callahan) ("The right to retransmission consent …is a local right. This is not, as some allege, a network bailout for Dan Rather or Jay Leno. Networks are not a party to these negotiations, except in those few instances where they own local stations themselves.") (emphasis supplied); 138 Cong. Rec. H6493 (statement of Rep. Chandler) ("The intent of the [retransmission consent] amendment was to give bargaining power to local broadcasters when negotiating the terms of cable carriage – not to serve as a subsidy for major networks.") (emphasis supplied).

[11] *See, e.g.*, Letter from Edward O. Fritts, President & CEO, NAB, to Jack Valenti, President, MPAA, dated October 7, 1991 ("NAB Oct. 7, 1991 Letter") (stating that retransmission consent was "not a 'network TV' issue, that the networks would not play a role in the negotiations between local stations and local cable systems, and that the networks would have "no right to dictate their terms or to demand any part of the benefits which the local station might obtain from a cable system"). S*ee also* Letter from Edward O. Fritts, President & CEO, NAB, to Rep. Christopher H. Smith, dated August 9, 1991 (stating, in attachment, that characterizations of retransmission consent as a "network plan" are "sheer nonsense" and that "Networks are not involved in any negotiations."). Copies of the documents referred to herein can be found as an attachment to the Joint Comments of Mediacom Communications Corporation, Cequel Communications LLC d/b/a Suddenlink Communications, and Insight Communications Company, Inc. filed in the FCC's retransmission consent reform proceeding, MB Docket No. 10-71, on May 27, 2011.

network affiliates.[12] And as David Smith, CEO of Sinclair Broadcasting Group, has commented, local broadcasters will have to "keep upping" their retransmission consent demands "forever" in order to satisfy the networks' reverse compensation demands.[13]

The pressure to extract payments not only for themselves but also for the national networks has driven local stations to do whatever they can to take advantage of their already considerable bargaining advantage over MVPDs. For example, local broadcasting is becoming increasingly consolidated through station acquisitions or the use of contractual arrangements that allow local Big Four network affiliated stations to coordinate their retransmission consent negotiations and thereby further increase their leverage.[14] One study has found that the retransmission consent fees for Big Four broadcast network affiliates are more than

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[12] For example, Les Moonves, who is CEO of CBS, has made it clear that in his opinion, what drives retransmission consent prices is network programming not the local news. *See Les Moonves Insists That Retrans Cash Is Network Driven*, Radio & Television Business Report, June 3, 2011, *available at* http://www.rbr.com/tv-cable/les-moonves-insists-that-retrans-cash-is-network-driven.html (emphasis supplied). Mr. Moonves has said that because of the leverage that broadcasters have in retransmission consent negotiations the "sky's the limit" when it comes to the amount that consumers can be forced to pay for local television stations. CableFAX Daily, June 3, 2011, at 2.

[13] Communications Daily, May 5, 2011, at 5.

[14] While data indicating the precise number of instances in which one station has control over the exercise of retransmission consent for multiple stations in a market is hard to come by, a review conducted in 2011 by BIA/Kelsey on behalf of Time Warner Cable indicated that there are more than 40 examples of "virtual duopolies" in which one station uses its multicast capacity to operate as the market affiliate of two Big Four networks and nearly 150 instances in which one station's multicast capacity allows it to serve as an affiliate of both a Big Four network and one of the "Little Two" networks (CW or MyNetwork). *See* Testimony of Melinda Witmer, Executive Vice President & Chief Video and Content Officer, Time Warner Cable, before the Committee on Commerce, Science and Transportation, United States Senate (July 24, 2012), *available at* http://www.commerce.senate.gov/public/?a=Files.Serve&File_id=bd33c7c9-bd4d-43c0-93d5-091e1fd3328b.

20 percent higher when a single station negotiates on behalf of more than one affiliate in a market.[15] Moreover, a common consequence of local station consolidation is a merging of station news gathering and reporting operations, resulting in staff layoffs and a reduction in local programming. In these situations, consumers are actually ending up paying more for less.

Consolidation of stations and collusive retransmission consent negotiations are practices that are widespread and increasing.[16] A survey of small cable operators has identified 48 pairs of separately-owned, same market television stations in 43 television markets that are using a single representative to negotiate retransmission consent.[17] The FCC is currently considering proposals to prohibit this anticompetitive practice in two separate rulemakings.

Pressure to satisfy the demands of the national networks also has driven local stations to make more frequent use of threatened blackouts, and actual blackouts, to force a distributor to capitulate to the stations' retransmission consent demands. The number of retransmission consent-related shutdowns increased

[15] Letter from Ross J. Lieberman, Vice President of Government Affairs, American Cable Association, to Marlene H. Dortch, Secretary, Federal Communications Commission, MB Docket No. 10-71 (filed June 3, 2013).

[16] *Id.*

[17] Letter from 25 Smaller Cable Operators to Marlene H. Dortch, Secretary, Federal Communications Commission, MB Docket No. 10-71 (filed Feb. 4, 2013). This number does not reflect the even greater number of instances in which cognizable duopolies or multicast "virtual duopolies" result in a single entity controlling retransmission consent decisions for more than one station in a market. *See* note 14 *supra*. *See also* Letter from Barbara Esbin, Counsel to American Cable Association, to Marlene H. Dortch, Secretary, Federal Communications Commission, MB Docket No. 10-71 (filed Feb. 16, 2011) (indicating that there were at least 93 sharing arrangements in 78 markets).

from 12 in 2010 to 51 in 2011 to 91 in 2012.[18] These blackouts are directly at odds with what was supposed to be the goal of retransmission consent: preserving the universal availability of free over-the-air broadcast programming.

At BendBroadband, we have had one retransmission consent-related blackout in recent years. It was disruptive and frustrating to our customers and is not something I would be eager to repeat. But I am concerned that if the current structure is not modified, we and other companies will continue to face similar circumstances in the future as the only backstop to protect our customers from the doubling and tripling of retransmission consent fees.

3. The Unnecessary Costs Imposed on Cable Consumers for Separated Security in Set-top Boxes.

All aspects of the video marketplace have changed dramatically and the market for navigation devices is no exception.

Seventeen years ago when Section 629 was enacted, Congress believed that consumers had only one option to obtain multichannel video programming at home—by leasing a set-top box from their incumbent cable provider. In response, it directed the FCC to take steps to give consumers a retail alternative to the leased set-top box.

[18] *See, e.g.*, SNL Kagan, Rewarding Blackout Behavior, August 22, 2012; J. Eggerton, ATVA Cites Rise in Retrans Blackouts, Multichannel News, Jan. 2, 2012, *available at* http://www.multichannel.com/distribution/atva-cites-rise-retrans-blackouts/140973.

Today, consumers want to view video programming when and where they want it. The marketplace has responded with a revolution of new alternatives to traditional TV – including Internet connected TVs, streaming to tablets, mobile telephones and other "smart" video devices, as well as numerous new services from traditional cable operators and from new "over the top" and other service providers. For example:

- Consumers can purchase a wide variety of tablets, PCs, and gaming devices, and Smart TVs that can access video services from MVPDs such as Comcast, Time Warner Cable, Verizon and DirecTV – without a set-top box.
- More than 120 million Internet-connected TVs are expected to be sold by 2014, offering video services from MVPDs and over-the-top video providers, including Netflix, Google, Hulu, Roku, Boxee, and game console providers such as Microsoft (Xbox), Nintendo (wii), and Sony (PlayStation).[19]
- Consumers can access multichannel video on their personal computer and other Internet-connected devices using implementations of "TV Everywhere" and set-top boxes are beginning to combine TV with other applications and content.
- Video providers and device manufacturers like TiVo, and designers of gaming stations like Microsoft Xbox are working together on unique programming distribution agreements, combining the retail device and MVPD service experience.

Yet, in a spite of these marketplace developments, the cable industry has been forced to spend approximately one billion dollars to comply with outdated rules that do not apply to its major competitors.[20] At BendBroadband, we were able to avoid some of these costs by obtaining the first FCC waiver of the ban on integrated set-top boxes. That waiver acknowledged the fact that compliance with

[19] Internet-connected-TV sales to skyrocket, Los Angeles Times, April 26, 2011, *available at* http://latimesblogs.latimes.com/technology/2011/04/internet-tv.html.

[20] *AllVid NOI*, *supra*, *citing* Letter from Neal M. Goldberg, Vice President and General Counsel, National Cable & Telecommunications Association, to Marlene H. Dortch, Secretary, Federal Communications Commission, CS Docket No. 97-80, at 14 (statement of Commissioner Baker) (emphasis supplied).

the ban would impede BendBroadband from fulfilling its goal of creating an all-digital video service that would provide the public with otherwise unattainable benefits.

In recent years, a number of other operators have been granted waivers for similar reasons as well as on the basis of other arguments, including simple financial hardship. However, not all cable operators can meet the FCC's stringent waiver standards. This is particularly true for small cable operators. In any event, no cable operator should have to go to the expense and uncertainty of seeking a waiver of the FCC's outmoded and one-sided set-top box rules, and no consumer, whether the customer of a large successful system or a small struggling system, should have to bear the costs associated with Section 629, particularly when customers of cable's competitors do not face the same costs. The time has come for Congress to eliminate these rules.[21]

It is Time for Congress to Act.

The three examples I have discussed today illustrate how a regulated marketplace can end up being distorted if the government does not routinely review and update its role, particularly in the dynamic video world. I believe that the time has come for a comprehensive review of all of the rules governing cable television operators. However, I understand that such a review may not be feasible

[21] Many scholars who have analyzed Section 629 from a legal and economic perspective have concluded that it is time for Section 629 "to be put to bed." T. Randolph Beard, PhD, et al., Wobbling Back to the Fire: Economic Efficiency and the Creation of a Retail Market for Set-Top Boxes, 21 CommLaw Prospectus 1, 58 (2012).

over the next 18 months. Therefore, I would urge Congress to consider some targeted updates to the Communications Act as part of the STELA reauthorization process.

In conclusion, I want to commend your continued interest in these important issues and for holding this hearing today. I also want to acknowledge Representative Scalise and other Members who have advanced the debate on video reform. I believe it is time for Congress to take targeted action to modernize the rules governing the video market to reflect 21st Century realities. Simply hoping that the problems occurring in today's marketplace will go away on their own will not solve the breakdowns that are harming consumers. I am encouraged that the Subcommittee is engaging in this dialog.

Thank you. I would be happy to answer any questions you might have.