The Committee on Energy and Commerce

Memorandum

September 9, 2013

To: Members, Subcommittee on Communications and Technology

From: Majority Committee Staff

Subject: Hearing on "Innovation Versus Regulation in the Video Marketplace"

I. Overview

The Subcommittee on Communications and Technology will hold a hearing Wednesday, September 11, 2013, at 2:00 p.m. in 2123 Rayburn House Office Building on "Innovation Versus Regulation in the Video Marketplace." One panel of witnesses will testify:

1. R. Stanton Dodge, Executive Vice President and General Counsel, DISH Network, LLC
2. Edward L. Munson, Jr., Vice President and General Manager, KPHO-TV
3. David Rozzelle, Executive Vice President, Suddenlink Communications
4. James Campbell, Vice President of Regulatory and Legislative Affairs, Midwest Region, CenturyLink, Inc.
5. Sandra Aistars, Executive Director, Copyright Alliance
6. John Bergmayer, Senior Staff Attorney, Public Knowledge

American consumers have unprecedented access to high-quality video content. From traditional over-the-air broadcasting to the vast offerings of the Internet, from feature-length films to short YouTube uploads, the media landscape has changed significantly in the last 40 years. However, despite the similarities between video distribution services, they are not regulated equally – or in some cases, at all. As part of the Subcommittee's review of the Satellite Television Extension and Localism Act (STELA) this hearing will examine the disparities in the laws governing video content, specifically those laws and regulations that impact their abilities to acquire and distribute content to consumers. The laws governing broadcasters, cable operators, and direct broadcast satellite (DBS) providers were enacted during the respective infancies of each industry. In an era when these technologies are increasingly substitutes for one another, is government intervention in the video marketplace still necessary to protect content creators, the companies that deliver content to our homes and mobile devices, and consumers?

II. Background

The legal regime that governs the delivery of video has become increasingly fractured as technology has changed the video marketplace. Over the past 40 years, alternatives to traditional broadcast delivery of video content have revolutionized Americans relationship with video content. Far from the era of three channels on the VHF dial, today's consumers have significantly more content available to them than ever before. Unfortunately, many of the laws that regulate these services are outdated and may no longer serve a purpose. At 17 years old, the Telecommunications Act of 1996 (Telecom Act) is the youngest of the major statutes that govern this market, followed closely by the Cable Television and Consumer Protection and Competition Act of 1992 (Cable Act) and the Satellite Home Viewer Act of 1988 (SHVA). None of these compare, however, to the fact that regulation of the broadcast industry predates the creation of the Federal Communications Commission in 1934.

These statutes have seen changes over the years, but none of those changes have addressed the fundamental changes in the marketplace that innovation and competition have brought to U.S. consumers.

A. Broadcasting

Modern broadcasters trace their regulatory history back to 1927 and the FCC's predecessor agency, the Federal Radio Commission. Broadcast stations are licensed by the Federal Communications Commission under Title III of the Communications Act of 1934, as amended, as public trustees that serve the "public interest, convenience, and necessity" as stewards of spectrum. Because of this distinction, a broadcast license carries a host of regulatory obligations. Among the increasingly complex sets of rules are requirements to air content serving local communities (localism), political advertising, sponsorship identification, indecency regulation, and children's programming.

Additionally, the Communications Act also places limits on aggregate broadcast station ownership. While this standard has evolved over time away from a hard cap on the number of stations, current law places a limit on the percentage of American households a single TV broadcaster may reach. Currently, that limit is 39 percent – last addressed by Congress in 2004. In addition to the national cap, the law limits the number of broadcast properties a single entity may own in the same market. The last significant update to this limit occurred in 1975, when the FCC adopted the ban on newspaper and broadcast station cross-ownership. During the past decade, the Commission has put forth numerous attempts to reform the media ownership rules, which consistently have been remanded to the Commission by the Federal courts.

B. Cable

Cable is primarily regulated by a combination of Federal law and local franchising requirements, largely on rate regulations, signal carriage, build-out requirements, public interest obligations, and programming regulation. Statutes covering cable providers were last significantly updated in the 1990s through the Cable Act and provisions of Telecom Act. Both of these laws took a regulatory approach to the industry, seeking to increase competition and lower rates in an industry where few competitors existed at the time.

The two statutes laid significant obligations on the cable industry, including the adoption of Federal rate regulation; codification of the retransmission consent and "must-carry" regimes, which prescribe the ways that local broadcast signals are carried on cable systems; a requirement that broadcast signals must be placed on a cable operator's lowest-priced tier, which a subscriber must purchase before he can purchase any other premium programming; regulation of the market for the consumer equipment required to access the cable network; and requirements that cable operators carry leased access channels and public interest, educational, and government (PEG) channels.

As the cable industry matured, operators began to invest in content development and production. The current regulatory regime prohibits cable operators from favoring content from affiliated networks and studios and also from withholding certain cable-generated content from competitors. Under the "program access" regulatory regime, other video providers may bring complaints against programming networks affiliated with cable operators, if those networks unreasonably withhold programming. Under the "program carriage" regime, independent networks may bring complaints that cable operators affiliated with networks have discriminated against the independent networks in favor of their own.

C. Local Exchange Carrier Video

The incumbent telephone companies began entering the video market in the early part of the 2000s; video service was intended to be a third revenue stream that would help pay for the deployment of fiber networks. In order to encourage telephone providers to enter and provide competition in this market, many States took over franchising authority from local municipalities and counties. Verizon's FiOS and CenturyLink's Prism services provide video service in parts of the country. They are regulated much like cable operators at the FCC and under State franchise agreements at the State level. AT&T has acquired State franchises to provide service, but has consistently asserted that its video offering, U-Verse, is not a cable service and not subject to certain cable requirements.

D. Direct Broadcast Satellite

DBS providers are governed by SHVA and its progeny, the Satellite Home Viewer Act of 1994, the Satellite Home Viewer Improvement Act of 1999 (SHVIA), the Satellite Home Viewer Extension and Reauthorization Act of 2004 (SHVERA), and the Satellite Television Extension and Localism Act of 2010 (STELA). In the earlier stages of development, satellite operators were unable to target specifically local services to communities, but DBS offered the valuable service of delivering video to communities that could not receive television signals due to terrain or distance. SHVA ensured the necessary copyright authorizations to allow satellite operators to redistribute the distant signals of out-of-market broadcast network affiliates to "unserved" households.

In order to provide "distant signal service," satellite providers received a compulsory license under the Copyright Act and an exemption from the retransmission consent and must-carry rules. However, as the technology of DBS progressed, SHVIA established "local-into-local" service and "carry-one-carry-all" requirements for DBS. Under these rules, if a DBS operator carries any local station on its satellite, it must carry all of the broadcast stations in the market. Moreover, it must abide by the retransmission consent regime and negotiate carriage of the signal. If a DBS operator carries a local network affiliate under these rules, the law now prohibits the operator from bringing a distant signal into the market unless the station falls under a specific set of criteria that define the channel as "significantly viewed" within the local market.

E. Over-the-Top Video

The biggest innovation in the distribution of video has been the delivery of video over the Internet (over-the-top or "OTT" delivery) for consumption on demand. Industry analysts estimate that over 35 percent of American households have connected their televisions directly to the Internet, while millions more view OTT video programming via laptops, tablets, smartphones, and other connected devices.

Netflix and Amazon.com are established players in this emerging market, but other established technology companies like Apple, Intel, Google, and Sony increasingly have been venturing into the market for the delivery of video programming. Additionally, traditional multichannel video programming distributors (MVPDs) like cable and DBS providers as well as content creators, are now including online distribution in their business strategies, offering content directly through their own websites, YouTube channels, via TV Everywhere, and a variety of mobile apps. These new forms of video content delivery are largely unregulated, with the exception of the 21st Century Communications and Video Accessibility Act of 2010, which requires closed captioning and video description for certain types of streamed OTT video.

III. Discussion

Despite the fact that these services are increasingly substitutes for one another, the rules governing the video distribution market continue to perpetuate an antiquated view of the market and ignore the realities of current technologies. Many of the rules that have been adopted both by Congress and by the FCC over the last 40 years have been reactions to a perceived lack of competition. Cable operators had 98 percent of the pay-TV distribution market when Congress passed the 1992 Cable Act amendments and 53 percent of national program networks were at least partially owned by a cable operator. At the time of the 1996 Telecommunications Act amendments, cable still had an 89 percent share and 44 percent of national networks remained vertically integrated with a cable company. By contrast, as of the end of 2011, cable's market share had dropped to 57 percent and roughly 15 percent of national networks were vertically integrated with a cable operator. The two nationwide direct broadcast satellite providers have 34 percent of the pay-TV market and were the second and third largest providers, which they remain today. Over the same intervals, the percentage of TV homes relying exclusively on over-the-air broadcasting dropped from 36 to 27 to 9.6. Meanwhile, the number of national program networks has grown from 106 to approximately 800 between 1994 and 2012.

A. Content Carriage

Despite these changes in the market for content and distribution, our laws assume that there is a disparity of bargaining power between broadcasters and MVPDs and discriminate against MVPDs based on the technology used for delivery.

Carriage Guarantees: Must-Carry and Carry-One-Carry-All. While broadcasters with high-value content negotiate with cable and DBS providers for carriage, broadcasters that lack sufficient interest in the consumer market to demand retransmission consent can avail themselves of rules that ignore consumer demand and guaranteed carriage on MVPD systems. Moreover, must-carry applies to all cable providers, but the carry-one-all rule only applies in markets where DBS providers are carrying local content.

Negotiation Guarantees: Basic Service Tier, Buy-Through and Channel Placement. Under current law, broadcast signals must be placed on a cable operator's lowest-priced tier, which a subscriber must purchase before he can purchase any other premium programming and broadcast stations are guaranteed preferential channel placement based on their historical channel number. Only broadcasters and local government PEG channels are guaranteed to reach every member of a cable operator's subscriber base. Other programmers negotiate for placement on cable programming tiers. DBS operators, telcos, and OTT providers are not subject to a basic tier buy-through provision. However, cable operators may seek exception from this rule by a finding of effective competition by the FCC.

B. Content Access

Mandatory Wholesaling: Program Access Regulation. The FCC's program access rules require cable operators to license content created by cable-affiliated networks to their competitors. Although cable operators in the past have had exclusive rights to some sports programming, it is unclear whether the program access rules continue to be necessary in an era in which DBS operators are able to negotiate for exclusive rights to high-value sports programming and in which the Internet permits distribution of high-value content in other ways.

Blurred Lines: Bundling of Retransmission Consent and Other Programming Rights. The FCC estimates that approximately 95 percent of all television viewing hours have been produced by just seven content owners. MVPDs have complained that because modern content creators are often engaged in both broadcasting and cable programming, retransmission consent negotiations are unfairly conflated with negotiations for premium cable channel networks and digital content rights. In fact, one cable provider – Cablevision – has filed suit charging that the practice of bundling content constitutes a "tying" arrangement under antitrust laws as it forces MVPDs to purchase additional unwanted content in order to obtain desirable content.

C. Exclusivity Rules

Other provisions, such as the network non-duplication and syndicated exclusivity rules, also limit the ability of cable and satellite operators to freely negotiate, but should not be revisited unless done at the same time as compulsory copyright provisions. The network non-duplication and syndicated exclusivity rules prevent cable and satellite operators from importing network or syndicated programming from out-of-market broadcast stations if the local stations have negotiated geographic exclusivity agreements with the rights holders of the programming. These provisions operate in tandem with the compulsory copyrights, which restrict the rights holders of broadcast content from prohibiting the content's use and set the royalties, if any, the rights holders may collect. The network non-duplication and syndicated exclusivity rules' restrictions on cable and satellite operators' ability to freely negotiate broadcast program carriage ameliorate the compulsory copyrights' restrictions on the rights holders' ability to freely negotiate use of and compensation for the content. That is why any re-examination should occur together.

D. Media Ownership Rules

The FCC's rules governing media ownership have been a source of uncertainty. Originally devised to ensure viewpoint diversity in a world where broadcasting was the only way to deliver video to American homes, attempts to revisit the media ownership rules to address the rise of competitive content delivery technologies have resulted in one court remand after another to the detriment of investment in local broadcasting.

Local Broadcast Ownership Limits. Governed by restrictive local ownership rules, broadcasters have made use of joint service agreements (JSAs) and local marketing agreements (LMAs) to increase audience reach, garner scale for advertising, and pool limited resources. JSAs and LMAs allow a broadcaster to program and sell advertising for another station in a market without actually attributing those stations toward its ownership, which allows them to avoid running afoul of the FCC's ownership limits. MVPDs have argued that these shared service arrangements increase broadcaster leverage in carriage negotiations, particularly when shared service agreements occur between affiliates of the national broadcast networks in a single market.

National Ownership Limits. Broadcasters face an additional limit on the percentage of U.S. households they are permitted to reach. Currently set at 39 percent, this limit was originally meant to ensure that one broadcaster could not control the message reaching a disproportionate percentage of the country. However, in the modern video marketplace, there are no such restrictions on other voices in the market. For example, unlike broadcast content, cable news networks are permitted to reach nearly every cable and DBS subscriber in the country. Moreover, the FCC is currently reconsidering the formula under which it calculates station coverage – the so-called "UHF discount." Elimination of the UHF discount without more comprehensive reform of the media ownership rules could render broadcasters existing holdings of those companies with pending applications at the FCC out of compliance and force divestiture or other significant corporate changes.

If you need more information, please call David Redl or Grace Koh at (202) 225-2927.