

Statement of Matt Polka, President and CEO

American Cable Association

Before the Senate Commerce Committee

Hearing on Video Content

Tuesday, January 31, 2006

Thank you, Mr. Chairman and members of the Committee. My name is Matt Polka, and I am the President and CEO of the American Cable Association. ACA represents 1,100 smaller and medium-sized cable companies providing advanced video, high-speed Internet access and telephone service in smaller markets and rural areas in every state.

I appreciate the opportunity to speak to you today and will focus most of my remarks on retransmission consent. As I will explain, especially when dealing with smaller cable companies, broadcasters' escalating retransmission consent demands are resulting in higher cable costs, less choice, and, in some cases, required carriage of objectionable content. I will also address the related problem of forced bundling and tie-ins – how the major media conglomerates

require us to distribute, and our customers pay for, channels that our customers do not want. We believe the current system of regulations have unintentionally fostered much of the trouble. We also believe practical solutions exist and look forward to sharing our ideas with you today.

Unique Perspective

ACA brings a unique perspective to this hearing. Our members are smaller cable providers that do not own programming or content, and that are not affiliated with large media companies. This independence enables us to see what's good and what's bad in the current video market without being blinded by competing and conflicting interests that many of the vertically integrated companies face. Our sole mission is simple: we want to deliver high-quality advanced services and desirable programming that our local communities want.

Obsolete Laws and Regulations

We believe that current laws and regulations inhibit our ability to best serve our customers, who also happen to be your voters. After 20 years in the cable business, I have seen increasingly how retransmission consent abuse and wholesale programming practices impede our ability to best serve our local communities. To help remedy this, I urge you to continue your inquiry into video programming, pricing, and packaging. In doing so, I know Congress can benefit consumers by spurring innovation, competition, and flexibility.

Mr. Chairman, the crux of our concerns comes from the unfortunate and unintended consequences of the retransmission consent regime, a law governing the carriage of local broadcast television stations that was put into place in the 1992 Cable Act. In the 14 years since its enactment, the world of media has fundamentally changed. Through unprecedented consolidation, broadcasters and media companies have become much more powerful. When dealing with smaller cable companies, broadcasters no longer need the protection given them in 1992. Now, broadcasters are using retransmission consent in ways that restrict choice, raise costs, and force consumers to take channels they don't want. Retransmission consent today as used by the media giants, hurts "localism" rather than enhances it. Retransmission consent continues to be the root cause of the primary concern of so many: increasing consumer rates for cable and satellite television.

Just yesterday, an independent study issued by Arlen Communications confirmed that broadcasters are exploiting the current retransmission consent regime when dealing with smaller providers. The Arlen study describes how broadcasters use of exclusivity and escalating demands are hurting consumers in smaller markets and, in some areas, impeding the rollout of broadband. I encourage you and your staffs to give careful consideration to the Arlen report.

Retransmission Consent "Payment"

Under the current retransmission consent regime, powerful networks and affiliate groups demand payment from cable providers for their broadcast

network. That “payment” may be in the form of cash-for-carriage, which for ACA members is often an astronomical price unfettered by any correlation with actual, identifiable market value, or cable operators may “choose”, and pay for, affiliated non-local programming on their cable system. If cable operators opt to carry affiliated programming on their system, programmers dictate channel placement and set minimum penetration requirements that leave our members with no option but to include the affiliated programming on the expanded basic lineup. In other words, their “must have” broadcast network that has been granted extensive protections by Congress in order to preserve “localism” now gives them leverage to force the carriage of their affiliated programming onto our channel lineup and into our consumers’ homes.

Here is the part of the problem that is not well understood: While broadcasters are demanding escalating retransmission consent prices, at the same time they are using regulations and contracts to exclude access to lower cost substitutes. Put another way, retransmission consent “prices” are not disciplined by a competitive market. The result is predictable, prices go up and consumers are harmed. In short, broadcasters have gamed a system that has its roots in legal and regulatory fiat, not market-based mechanisms. We urge you to change that situation.

Family Tiers/Programming Contracts

With regards to children's programming, I want to commend those cable operators like Time Warner and Comcast who are working to offer a family-friendly tier to answer this Committee's call to clean up the airwaves. My members are ready and willing to offer the same service option, offering packages of customized content based on the markets we serve. However, our lack of clout with the programmers whose contracts mandate carriage of their channels does not allow our members to offer tiers and we are still trying to find a way to provide new tiers of service that does not put us in legal jeopardy with our programming partners. The programming conglomerates will have to loosen their vice-grip on tying and bundling, and lower their penetration requirements before more tiering choices can ever become the norm in the cable and satellite pay-television marketplace.

I believe nothing exemplifies the severity of this problem more than the fact that ACA shares the same views on this matter as EchoStar, one of our biggest competitors. EchoStar has the same unfortunate experience in retransmission consent negotiations as ACA members because they, too, do not own programming, and therefore do not have market leverage when negotiating with the media conglomerates.

In fact, contractual obligations have already had a negative impact on the family-friendly tiers being rolled out by Time Warner and Comcast. Members of this Committee noted at the indecency hearing held just two weeks ago that

while the tiers were a step in the right direction, they were limited in the channels they offered. There was concern among some Senators who observed the lack of marketability in the tiers that offered G-rated programming only and eliminated sports altogether from the package. What the cable companies who are offering the tiers didn't tell you, most likely due to the non-disclosure agreements in their contracts, is that these are the only channels the conglomerates would allow them to offer on such a tier! Furthermore, those companies offering family-friendly tiers are already saying they will have to cap the number of subscribers that can sign up for the family friendly tier. That is because if too many consumers want this offering, they will not meet their contractual penetration obligations dictated by the programming owners. I'm sure the programmers are not about to waive their penetration requirements for us should family friendly tiering become popular. However, if you can ask them if they would release us from those obligations so that we can meet your call for more family oriented programming tiers, we would be able to offer a much more robust and appealing suite of programs to your constituents.

There was also question at the indecency hearing as to why the market cannot determine what is offered on tiers. We at ACA have the exact same question. We, who live and work in the communities we serve, believe we should have the ability to answer our consumers' desires and the market's demand by offering the channels our subscribers want to watch. Instead, it is the tying and bundling of programming in the take-it-or-leave-it contracts

extended to us by the conglomerates in Hollywood and New York that determine what is offered on the lineup of the cable television in the 8 million, predominantly rural homes we serve across America.

I know the issue of indecency on television has been one of recent concern to this Committee, and in particular to you, Chairman Stevens. Let me point out that the most objectionable and adult-oriented channels on our lineup are carried because they are tied to one of the must-have broadcast networks that is broadcast on public airwaves, or even more alarming, are tied to the carriage of popular children's programming, as in the case of Logo, the gay and lesbian network, being tied to one of the Nickelodeon services.

Additionally, in many markets today a cable or satellite provider that wants to carry family programming, such as Nickelodeon, must also carry much more suggestive and sexually explicit programming on MTV and Spike TV, AND must put that programming on the same tier as the children's programs! Essentially, to get *Spongebob Squarepants*, a well-known children's program, cable and satellite providers and their customers have to also take *Undressed* or *Stripperella*, two highly sexual, adult programs. Here's what MTV's website says about its program, *Undressed*: "Not getting enough action before you go to bed? *Undressed* will definitely be changing that! This season is sure to titillate your senses – so tune in!" Did Congress intend to perpetuate this type of situation and allow the use of the public airwaves to be used as leverage to carry such programming?

A la Carte

I must say there is great irony in the recent announcement that companies like Time Warner and Comcast will offer a family-friendly tier. The programmers and MSOs have said for years that tiers and a la carte offerings would destroy economic models, and have dismissed the notion that offering such services could ever happen. With pressure from this Committee and the real threat of legislative action, their strident position managed to change within a week's time. Furthermore, these same programmers, who were the strongest opponents of flexible, market-based offerings, are now selling their individual programming on iTunes, where customers can go online and download an individual program and watch it on their handheld iPod device. I believe most casual observers would call this kind of offering "a la carte" as it allows consumers not to select just the network they want to watch, but the specific program they desire. While ACA has called for greater market place innovation and flexibility to distribute programming to consumers, programmers have historically forced us to distribute the one size, take-it-or-leave-it offerings because they claimed any other model would destroy the fragile balance that they rely upon to stay profitable. Hopefully, now Congress and the FCC realize that the market is much more resilient than they had claimed and no longer has to take our word for it, they can see it in the actions of the programmers themselves.

And certainly networks can't really fight to keep retransmission consent in its current form for the sake of preserving localism: not when they are selling their prime programming product they produce for free over-the-air television and bypass their own affiliates. They are selling their highest-rated programming stripped of any local advertising and without giving the affiliate a share of the \$1.99 charged to the consumer for the download. As the market moves toward this model, there is no doubt affiliates' ad revenues will be reduced as viewers no longer need to watch their station to view their prime programs, which will eventually have an impact on the quality of local news and services offered by those affiliates.

How does this approach protect "localism?" It appears to me that nothing may imperil the financial viability of local stations more than this new business model. The conglomerates have undermined their own argument that they are for localism and they should no longer be able to use the tool of retransmission consent to hide their interests. In fact, the localism they worry so much about is safe due to another regulatory tool that should be retained. The ACA believes that "must carry" should remain the governmentally-granted tool to ensure that local stations are not shut out from any market.

Cash or Tying

Today, programmers have two sources of revenue: one is the fees they charge operators to gain access to the programming and the other comes from the advertising fees they charge. For this reason, the programmers demand

channel placements on basic or expanded basic tiers in order to get their offerings in front of the maximum number of eyeballs possible, which helps drive up their advertising profit. The largest programmers who have broadcast and cable channels effectively bypass market forces and bundle their broadcast channels with their affiliated programming, and force distributors to charge consumers for channels they don't even want – and in many questions, channels they find objectionable. If an operator opts out of the retransmission consent agreement and wants to take a stand-alone channel, the cash-for-carriage demand is most often an unreasonable price with no market basis, and is significantly greater than the price of the bundle of channels offered. To make matters worse, those programmers demanding such costs, channel placement, and carriage of additional channels are able to hide behind nondisclosure provisions in their contracts, further complicating the ability to address the abuse of retransmission consent practices.

Price Discrimination

Additionally, the wholesale price differentials between what a smaller cable company pays in rural America compared to larger cable operators in urban America have little to do with differences in cost, and much to do with disparities in market power. These differences are not economically cost-justified and could easily be replicated in the IP world as small entrants are treated to the same treatment our members face

For instance, ACA members have reported wholesale programming price differentials between smaller companies and major cable companies of up to 30%, and in one case, 55%. In this way, smaller cable systems and their customers actually subsidize the programming costs of larger urban distributors and consumers! We even end up with worse pricing than satellite companies DirecTV and EchoStar, who are the main competitors to our rural cable systems. Price discrimination against smaller cable companies and their customers is clearly anti-competitive conduct on the part of the programmers – they offer a lower price to one competitor and force another other competitor to pay a 30-55% higher price FOR THE SAME PROGRAMMING. The effect of these practices by the programmers is that three MVPDs in the same town pay wildly different rates for the same product that each is distributing in that town.

Forced Carriage Eliminates Diverse Programming Channels

The practices of certain programmers have also restricted the ability of some ACA members to launch and continue to carry independent, niche, religious and ethnic programming. The main problem: requirements to carry programmers' affiliated programming on expanded basic eliminate "shelf space" where the cable provider could offer independent programming.

If video providers are to provide outlets for niche programming that appeals in their markets (i.e. Spanish communities), you must ensure that they are not subject to the handcuffs current law allows to be placed upon them. The programmers argue that their affiliated programming would not get carriage

without retransmission consent, which would minimize subscribers' viewing choices. However, there are numerous independent channels that want to be carried but do not have a broadcast network to bundle with their channel. Even if they present programming a cable operator wants to launch in his market area, he often does not have the "shelf space" to do so because of the forced carriage of affiliated programming by the programmers. If the programmers are so certain they have valuable programming, why are they so relentless in their fight to preserve their right to tie their affiliated programming to their broadcast network? Why not let the market determine what is desirable? If the programmers produce must-have content, consumers will demand it and cable operators will carry it. They should not be allowed to use their leverage of public airwaves to get carriage of affiliated programming.

Remedies

To fix this situation, Congress must update and reform: (1) the retransmission consent and (2) program access laws.

Retransmission consent reform.

- **Smaller cable operators should have the "right to shop" for the most economical programming package to offer their subscribers.** Broadcasters use a combination of regulations and contracts to block cable operators from retransmitting stations from outside a broadcasters' market. Exclusivity is now being exploited by broadcasters to raise the cost of retransmission consent for smaller

cable operators and their consumers. In other words, the conglomerate-owned station makes itself the only game in town, and can charge the cable operator a monopoly "price" for its must-have network programming. The cable operator needs this programming to compete. So your constituents end up paying monopoly prices.

ACA believes there is a ready solution to this dilemma. When a broadcaster seeks a "price" for retransmission consent, give small cable companies the ability to shop for lower cost network programming for their customers.

Accordingly, in its March 2, 2005 Petition for Rulemaking to the FCC, ACA proposed the following adjustments to the FCC's retransmission consent and broadcast exclusivity regulations:

- One: Maintain broadcast exclusivity for stations that elect must-carry or that do not seek additional consideration for retransmission consent.
- Two: Eliminate exclusivity when a broadcaster elects retransmission consent and seeks additional consideration for carriage by a small cable company.
- Three: Prohibit any party, including a network, from preventing a broadcast station from granting retransmission consent to a small cable company.

On March 17, 2005, the FCC released ACA's petition for comments. By opening ACA's petition for public comment, the FCC has acknowledged that the current retransmission consent and broadcast exclusivity scheme requires further scrutiny. Before codifying a new regulatory regime for video services utilizing IP, Congress should ask similar questions and make the important decision to update current law to rebalance the role of programmers and providers.

- **Tying through retransmission consent must end.** The law should prevent the media giants from holding local broadcast signals hostage for monopolistic cash-for-carriage demands or more carriage of affiliated media-giant programming, which was never the intention of Congress when granting this power.
- **Codify the News-Hughes conditions made by the FCC when approving the NewsCorp acquisition of DirecTV.**

The FCC acknowledged the disproportionate market power NewsCorp would have as a programmer and a distributor when they sought to acquire DirecTV. The FCC imposed conditions on News Corp. to apply during their retransmission consent negotiations. The three key components of those conditions include: (i) a streamlined arbitration process; (ii) the ability to carry a signal pending dispute resolution; and (iii) special conditions for smaller cable companies. ACA believes

conditions like these applied to smaller and medium-sized cable operators would improve the current retransmission consent process.

Program access reform.

- **Price discrimination must end.** The programming pricing gap between the biggest and smallest providers must be closed to ensure that customers and local providers in smaller markets are not subsidizing large companies and subscribers in urban America. The programming media giants must disclose, at least to Congress and the FCC, what they are charging local providers, ending the strict confidentiality and non-disclosure dictated by the media giants. Confidentiality and non-disclosure mean lack of accountability of the media giants.
- **Transparency must be created** if consumer rates are of concern to you. Most programming contracts are subject to strict confidentiality and nondisclosure obligations, and ACA members are very concerned about retaliation by certain programmers should they discuss the specifics of any deal. For instance, if you ask me today what a specific ACA member pays a certain programmer, I could not tell you without fearing legal action by the media giant. Programmers could agree to waive nondisclosure for purposes of this hearing or even in our contracts, but they never do. Ask them today, and I'd be shocked if they would disclose specific terms and conditions. Ask them why this confidentiality and non-disclosure exists.

Who does it benefit? Consumers, Congress, the FCC? I don't think so. Why is this information so secret when much of the infrastructure the media giants benefit from derives from licenses and frequencies granted by the government?

Congress should obtain specific programming contracts and rate information directly from the programmers, either by agreement or under the Committee's subpoena power. That information should then be compiled, at a minimum, to develop a **Programming Pricing Index (PPI)**. The PPI would be a simple yet effective way to gauge how programming rates rise or fall while still protecting the rates, terms, and conditions of the individual contract. By authorizing the FCC to collect this information in a manner that protects the unique details of individual agreements, I cannot see who could object.

Armed with this information, Congress and the FCC would finally be able to gauge whether rising cable rates are due to rising programming prices as we have claimed or whether cable operators have simply used that argument as a ruse. A PPI would finally help everyone get to the bottom of the problems behind higher cable and satellite rates.

Conclusion

In conclusion, let me reiterate that ACA members are eager to offer their customers more choices and lower costs. Today, broadcasters and programmers prevent that. The roll-out of family-friendly tiers two weeks ago proved that more consumer choice is achievable, and with help from this Committee, I believe we as operators can do more to create marketable tiers of programming. The retransmission consent and broadcast exclusivity regulations have been used by the networks and stations to raise rates and to force unwanted programming onto consumers. This must stop. If a station wants to be carried, it can elect must-carry. If a station wants to charge for retransmission consent, let a true competitive marketplace establish the price.

Mr. Chairman, ACA members would prefer mutually beneficial carriage arrangements with programmers. For this to occur, certain media conglomerates would need to temper economic self-interest with a heightened concern for the public interest in localism, consumer choice, and reasonable cable rates. However, it has become increasingly clear that without congressional or regulatory involvement, these companies will continue to abuse retransmission consent using scarce public spectrum granted them for free to extract ever-increasing profits from rural consumers.