TESTIMONY OF
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BEFORE THE
UNITED STATES SENATE
COMMITTEE ON COMMERCE, SCIENCE & TRANSPORTATION

Video Content

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Chairman Stevens, Co-Chairman Inouye, and Members of the Committee, I appreciate the opportunity to appear before you today to discuss issues relating to video content.

Two years ago, the Federal Communications Commission ("FCC") concluded that: *"[T]he vast majority of Americans enjoy more choice, more programming and more services than any time in history."*[1] Two years later, that statement can be made with even more conviction. It is undeniable that American consumers now enjoy access to an unprecedented array of video programming delivered in a growing number of ways by an ever-increasing number of competing providers. Comcast is one of those providers. And in every community that we serve, we are competing with DirecTV, with Dish Network (EchoStar), often with companies like RCN, Knology and WideOpenWest ("WOW"), and any day now with companies like AT&T and Verizon.

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[1] *In re Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, 10th Annual Report, 19 FCC Rcd. 1606 ¶ 4 (2004).

This competition has driven our company, and the entire cable industry, to improve. But more importantly, it has given the American consumer the richest cornucopia of video programming in the world, with huge diversity of voices and content, meeting almost every conceivable need and interest.

Competition in Distribution

When Congress and the FCC assess competition in video distribution, they have tended to confine their analysis to what they call the "multichannel video programming distributors," or "MVPDs." These include traditional cable television operators, "broadband service providers" like RCN, WOW and Knology, direct broadcast satellite ("DBS") providers like DirecTV and Dish Network, local exchange carriers like Verizon and AT&T, providers of Multichannel Multipoint Distribution Service, electric utilities, and satellite master antenna TV systems. Taken as a whole, the growth of these competitors has been extraordinary since Congress passed the Cable Television Consumer Protection and Competition Act of 1992 ("1992 Cable Act"). At that time, nearly 14 years ago, Congress foresaw the possibility of significant *potential* competition from these providers of multichannel video services, and it took measures to promote that competition. Today, that competition is real, robust, and thriving, as the most recent data from the FCC and other sources affirm.

The headline story is the extraordinary growth of DBS. DirecTV and EchoStar each offer their services to almost every household in the United States, and they have captured over 27 million customers. Each year for the past five years, the DBS companies have added two to three million new customers, while the cable industry's basic subscribership has remained flat.

Each of those two companies is now larger than every cable company in America except for Comcast.

The Bell Operating Companies are also making a large-scale entry into the multichannel video marketplace, and we believe they, too, will be formidable competitors.

Not every consumer chooses to take service from a MVPD, however. Anywhere from 15-20 million households prefer to rely on over-the-air television. And in several markets, local broadcast stations are banding together to create a multichannel over-the-air alternative offering dozens of cable networks to compete with cable and satellite. U.S. Digital Television is now operational in four cities (Albuquerque, Dallas, Salt Lake City, and Las Vegas), and for $19.95 per month provides its customers with 25-40 channels, including all the local broadcast stations (and their HD signals) and many of the most popular cable networks.

We think that the rapidly changing video marketplace compels Congress and the FCC to view "video competition" even more broadly. Today, tens of millions of Americans also supplement their viewing with DVD and videotape rentals and purchases, and Netflix has become a national phenomenon. In addition, an increasing number of Internet streaming and download options are emerging – witness the incredible explosion of services and devices at the Consumer Electronics Show earlier this month. From iPods to mobile phones to digital video recorders, everything is becoming a "video download" device.

The problem with television in America is not lack of choice – the problem is how a consumer can manage all of that choice!

In this unbelievably dynamic marketplace, neither Comcast nor anyone else can rest for even a moment. Each and every day, we compete to attract new customers and to keep our existing customers happy. This is why we have spent over $40 billion since 1996 to add the capacity to let us deliver 200 or more video channels to almost every home we pass... and added dozens of international and foreign-language channels... and added a dozen or more high-definition television ("HDTV") channels in every market... and have become the industry leader in providing video-on-demand ("VOD"), offering our digital homes over 3000 different programming choices any time, day or night, in every conceivable niche, including more local programming. We have to work hard to remain the first choice of our customers – and the way that we do that is by constantly investing in more capacity so that we can add new programming, new channels, and new features.

In short, the video distribution marketplace is more competitive and diverse than ever. As Congress looks to the future, it's wrong to view television as we viewed it in 1992 – it's a fundamentally different medium, and it has become fundamentally and irrevocably competitive.

Competition in Content

The explosion of distribution outlets has launched a corresponding explosion in content. When the 1992 Cable Act was passed, there were approximately 68 national programming networks (and only a dozen or so regional networks) in operation in the U.S.[2] The majority of them were owned by cable companies (largely because independent programmers, the broadcast networks, and the Hollywood studios were not very interested in investing in cable programming at the time) – in fact, 57 percent of cable networks had "some ownership affiliation with the

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2 H.R. Rep. No. 102-628, at 41 (1992) (noting that there were "68 nationally delivered cable video networks").

operating side of the cable industry."[3] The average household did not have cable at all, and those that did normally had access to about 36 analog channels of programming.

Fast forward to 2006 – incredibly, there are over 388 full-time national programming networks in operation today, and nearly 100 regional networks as well. The number of "vertically integrated" channels has dropped to 23 percent, and Comcast has a financial interest in approximately seven percent of the networks that we carry. Eighty-five percent of all American TV households take service from a MVPD, and a typical MVPD household enjoys access to over 200 video channels. In addition, many producers – both majors and independents – are creating programming for video-on-demand, and some may use VOD exposure as a springboard for the creation of new full-time channels.

There are three important reasons for this proliferation of programming choices:

* First, the cable industry's dedication to invest over $100 billion to expand our distribution networks and tens of billions more to improve the quality and diversity of our programming offerings;

* Second, the emergence of DBS and other distribution media to provide additional outlets for programming;

* And third, the freedom that the law has given us to package and promote this programming in "tiers," and to create tiers and packages that respond to consumer demand, makes economic sense for our industry, and allows us to respond to competition from DBS and other providers.

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3 *Id.* (noting that "39 [of the 68], or 57 percent, have some ownership affiliation with the operating side of the cable industry").

To elaborate on the third point, it is important to note that having the freedom to create programming tiers and bundles lowers key costs and improves the economics of programming in ways that help to support those hundreds of channels. Program tiers *lower transaction costs* because it is easier, less confusing to customers, and less costly to cable operators to sell a bundle of services in a tier with a single transaction than to try to sell hundreds of different services on an a la carte basis. Tiers *reduce marketing costs* because program services sold in a tier do not have to spend as much to market the service (or to retain subscribers) as they would if customers were required to make (and could constantly change) individual purchase decisions for each service. Tiers *lower distribution costs* because the distribution cost per subscriber is the same regardless of the number of channels delivered, so the more channels subscribed to, the lower the average cost of distributing a channel. Tiers *increase the value of advertising* because they expand viewership by capturing occasional and spontaneous viewers. And tiers *reduce equipment costs* because the only way in which to deliver services sold a la carte is to require customers to purchase or lease addressable set-top boxes for every TV in their homes.

The benefits of tiering in this fashion are widely understood and appreciated by both network programmers and would-be programmers. That is why so many of them have so vigorously opposed calls to require distributors to sell programming a la carte. The fact that a la carte would result in consumers paying more for less has been recognized in virtually every informed analysis done to date, including studies by the FCC's Media Bureau, the Government Accountability Office, Bear Stearns, Booz Allen, and Paul Kagan, among others.

Tiering and bundling of programming are entirely consistent with promoting both consumer choice and the economic viability of programming. Take Comcast's Arlington, Virginia system as an example. Our customers today can choose from over 1,000 program and price combinations to create a mix of services to meet any program interest or financial requirement:[4]

- *Limited Basic:* 32 channels, including all local broadcast stations, C-SPAN and C-SPAN2, News Channel 8, TV Guide, ABC Family, WGN Superstation, three Arlington Public School channels, a local government channel, and a leased access channel.
- *Expanded Basic:* 45 services, including CNN, ESPN, Discovery, Nickelodeon, Bravo, Food Network, Weather Channel, History Channel, and BET.
- *Premium Services:* services offered on a stand-alone basis, including HBO, Showtime, Cinemax, The Movie Channel, STARZ, ART (Arab Radio & Television), TV Asia, and Zee TV (an Indian-language channel).
- *Digital Classic:* an interactive programming guide, VOD access, 45 music channels, and 20 digital services, including Discovery Kids, Noggin, Fine Living, and Toon Disney.
- *Digital Plus:* Digital Classic services plus 23 additional digital services including National Geographic, three Discovery channels, Sundance, and 12 Encore channels.
- *Digital Silver:* Digital Classic services, Digital Plus services, and one premium service including the service's multiplexed channels and subscription VOD service.
- *Digital Gold:* Digital Classic services, Digital Plus services, and three premium networks including the services' multiplexed channels and subscription VOD services.
- *Digital Platinum:* Digital Classic services, Digital Plus services, and five premium services (HBO, Cinemax, Showtime, The Movie Channel, and STARZ) including the services' multiplexed channels and SVOD services.
- *Hispanic Tier -- CableLatino:* An add-on package for any subscriber that has the Digital Classic or Digital Plus services. This package is comprised of 18 Hispanic language services, including Discovery en Español, CNN en Español, and Toon Disney Español.

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[4] A customer must purchase Limited Basic in order to purchase any of the other packages listed here. This is because Congress prohibits cable operators from providing any tier of cable service to any customer who does not buy a tier that includes all local broadcast channels, as well as public, educational, and governmental channels. 47 U.S.C. § 543(b)(7).

- *Sports Tier:* An add-on package for any subscriber that has the Digital Classic or Digital Plus services. The Sports Tier is comprised of three out-of-market regional sports networks and Gol TV, NBA TV, and Fox Sports World.
- *HDTV Channels:* A package of 14 networks transmitted in HDTV, including ABC, NBC, CBS, Fox, WB Network, two PBS signals, iNHD, ESPN-HD, Comcast SportsNet-HD, HBO HD, Showtime HD, Cinemax HD, and STARZ HD.[5]

Additional flexibility is provided by the ability to add premium channels and services in various combinations, our pay-per-view and VOD programming options, as well as the new Family Tier that we announced in December and will roll out company-wide over the next few months.

The Role of Regulation in the Licensing of Program Content

Policymakers have always understood that market forces are superior to government regulation in enhancing consumer welfare, and that is no less true in the area of video content.

Back in 1992, when DBS had yet to launch its first satellite and sign up its first customer, the cable industry faced little direct multichannel competition. In response to consumer complaints, and in the absence of meaningful alternative sources of programming, Congress passed strict regulations governing the cable industry. But even then, Congress expressed a strong preference for competition over regulation, and put significant emphasis on encouraging competitive entry.[6] In the years since, multichannel video competition has taken deep root, and today is irreversible. As a result, many of the regulations that currently govern the cable industry were intended to address less competitive market conditions that have long since changed.

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5 Comcast does not charge separately for this programming but only for the HD-capable set-top box needed to receive it. With respect to premium services, customers receive only the HD versions of services they purchase.

6 *See* 47 U.S.C. § 521(6).

Two of those regulations that are relevant to this hearing are the so-called "program access" provisions of the 1992 Act,[7] and the "program carriage" provisions of that Act.[8] The relevant provisions of the *program access* statute were intended to ensure that national satellite-delivered cable programming services in which cable operators had an attributable financial interest would be made available to the industry's competitors on rates, terms, and conditions comparable to those available to cable companies. The *program carriage* provisions were intended to ensure that, at a time when cable companies were perceived to be the sole providers of multichannel services, those companies could not play a "gatekeeper" role through actions that unfairly barred or conditioned distribution of independent programmers.

Program Access

The program access provisions, implemented into rules by the FCC,[9] ensured that fledgling DBS providers and other competitors would have access to programming perceived as critical to their success. These provisions represented a major departure from normal competition policy, which would encourage investment and innovation in exclusive programming. Exclusive programming permits competitors to distinguish themselves from one another. For example, DirecTV has for several years had exclusive rights to the complete

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7 Cable Television Consumer Protection & Competition Act of 1992, § 12, Pub. L. No. 102-385, 106 Stat. 1460 (codified at 47 U.S.C. § 548).

8 *Id.* § 19 (codified at 47 U.S.C. § 536).

9 *See In re Implementation of Sections 12 and 19 of the Cable Television Consumer Protection and Competition Act of 1992: Development of Competition and Diversity in Video Programming Distribution and Carriage*, First Report & Order, 8 FCC Rcd. 3359 (1993).

package of National Football League games, which has helped it to distinguish itself from both its cable and satellite competitors and contributed to the company's success.

In adopting program access requirements, Congress clearly did not intend to commoditize all video programming. The relevant provisions of the statute do not apply to any programming in which a cable operator does not have an attributable financial interest, nor does it apply to terrestrially distributed cable networks (of which there were more than a dozen in operation when the 1992 Act was passed). Nor does the statute require that all programming be sold to everyone or sold at the same price to all distributors. Thus, in adopting this striking exception to freedom of commerce, Congress specifically limited its marketplace intrusion, with full knowledge of what it was doing.

It can be said that the program access provisions have been a great success – though it would probably be more accurate to say that the marketplace is working. In the 14 years since Congress enacted these provisions, there have been far fewer program access complaints with the FCC than either the FCC or Congress envisioned (we estimate fewer than 50 in total), and almost none of these complaints has resulted in a ruling adverse to the programmer – in fact, most have been settled. Importantly, as competition has grown, the number of program access complaints has dwindled, not increased. What is clear in today's marketplace is that national programming networks, whether or not affiliated with a cable operator, desire broad distribution of their services and have every incentive to ensure that as many consumers as possible can see their programming, including the 27 million DBS subscribers and the customers of other MVPD competitors.

Perhaps the most frequently reiterated complaint under the program access rules concerns Comcast SportsNet (Philadelphia). The FCC (twice) and the courts (once) have thoroughly considered and rejected complaints by DirecTV and EchoStar that Comcast's creation and distribution of this high-quality regional sports network violated the program access rules. All have concluded that Comcast was within its rights to make the economically sound decision to terrestrially distribute this network using a pre-existing terrestrial distribution system.[10] And while the DBS companies and others have cried wolf for nearly a decade, claiming that the FCC's decision would encourage companies to move their most valuable programming off of satellite (and therefore beyond the reach of the program access rules), the fact of the matter is that that has not happened. In fact, each of the four regional sports networks launched by Comcast since it created the Philadelphia network has been satellite-delivered, again for sound economic reasons.

DirecTV and EchoStar both claim that Philadelphia professional sports programming is "must-have" programming and that they cannot compete in that region without it. The facts, however, do not support that claim.

Since the mid-Nineties, nearly a hundred local Philadelphia professional sports events have been available on local broadcast stations, but the DBS companies did not carry these signals (which are available to them free of charge) until they were required to by federal law. It is difficult to understand why, if this is "must-have" programming, they would not bother to carry it for free.

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[10] For reasons known only to RCN, that company has claimed for several years that it has not received access to Comcast SportsNet (Philadelphia) on reasonable terms and conditions. However, RCN has had the contractual right to carry Comcast SportsNet (Philadelphia) from the day it signed on the air, and RCN still has those rights today, on the same terms and conditions that Comcast and other cable companies carry the network. And in fact RCN has carried the network on those terms since day one -- even though Comcast is under no obligation to make it available.

Moreover, based on the latest data from Media Business Corp. (as of 9/30/2005), it is clear that *DBS penetration in Philadelphia is higher than or comparable to that in many other urban markets*. Philadelphia has a DBS penetration of 12.04% -- higher than Hartford (8.6%), Providence (9.39%), Springfield-Holyoke (8.65%), and Laredo, TX (7.92%); comparable to Boston (10.73%), Las Vegas (10.96%), El Paso (11.01%), and Palm Springs (11.80%); and not significantly lower than New York (15.24%), Tampa (14.03%), Baltimore (14.15%), Milwaukee (15.08%), Norfolk (14.22%), or Harrisburg (13.29%), among others. And in fact, in the last five years, the DBS companies have *tripled* their market share in Philadelphia.

As I noted earlier, most programmers – including cable companies that own programming – want maximum distribution for most of their products. But that should not mean that cable companies, DBS companies, and others should not have the freedom to create and invest in some original and exclusive programming as well, in order to distinguish themselves from one another in the marketplace. In fact, Congress and the FCC should consider that the program access rules (and the corresponding restrictions that now apply to DirecTV as a consequence of its merger with News Corp.) may now be having the perverse effect of *reducing investment* by the beneficiaries of these rules (including two of the three largest MVPDs in America, DirecTV and EchoStar) in original programming – why invest and create when you can have access to someone else's work on the cheap?

Program Carriage

The program carriage rules were intended to be a guarantee against the ability of a cable operator, who 14 years ago might be presumed to have "monopoly gatekeeper" status, to bar or handicap independent programming networks from gaining distribution. These rules have almost never been invoked, again largely because the marketplace works. Anyone who has an attractive programming idea, a sensible business plan, and a willingness to negotiate carriage terms that make sense for both the programmer and the distributor, has had the opportunity to build a business.

In the past year, one company (Mid-Atlantic Sports Network, or "MASN") has filed a program carriage complaint, invoking these little-used provisions of law – the first such complaint *ever* filed against Comcast. A second company (The America Channel, or "TAC") has steadfastly refused to file a program carriage complaint, but it has attempted to leverage every other opportunity to get the government to force Comcast to carry it.

Let me address the MASN situation first. The Baltimore Orioles, as part of a deal with their affiliate, TCR, and Major League Baseball, created a new sports network (MASN) with the intention of carrying Baltimore Orioles games in 2007. And in an unprecedented move, Major League Baseball also granted to the Orioles organization control over the television rights of the new Washington Nationals baseball club. Comcast SportsNet (Washington/Baltimore) ("CSN") has the television rights to Orioles games through the 2006 season, and it paid millions of dollars for the right to negotiate exclusively for renewal of those television rights and for the right to match any third-party offer received after that period of negotiation expired. For the Orioles' organization to agree to transfer to MASN the rights to Orioles games for annual license fees, and to declare that the Orioles games would be available only on MASN starting in 2007 without providing CSN the opportunity to match this deal, was a blatant breach of CSN's contractual rights. CSN is pursuing its rights in court. Meanwhile, TCR filed a complaint at the FCC alleging that Comcast's decision not to carry MASN violates the program carriage rules. Without detailing here the lack of merit of TCR's filings (we would gladly provide to the

Committee upon request copies of relevant public documents filed at the FCC), it should be noted that some of TCR's allegations at the FCC were so frivolous and so outrageous that a consultant for Major League Baseball -- which is the business partner of the Orioles -- intervened on his own motion to denounce and refute those allegations.

Comcast wants to carry Orioles and Nationals games. But Comcast also wants to protect the contractual rights negotiated and paid for by CSN. We hope for a timely resolution that is in the best interest of our company, our customers, and the teams' fans.

Now let me briefly address the complaints by TAC. This is a would-be network that asserts that its inability to negotiate a carriage agreement with Comcast is an absolute bar to its viability. The fact is that TAC has done none of the things necessary to establish a viable network. It lacks a secure source of financing; it has not assembled any programming expertise; it has no coherent business plan; and -- most importantly -- it has created no programming. Not surprisingly, with a single exception, no established cable or DBS operator has entered into a carriage agreement with TAC.

TAC asserts that independent program networks cannot succeed without a carriage agreement from Comcast and Time Warner, and it claims that those companies will not work with independent program networks.

In response to the first point, I am attaching to my testimony a column by C. Michael Cooley of The Sportsman Channel, which appeared in the October 3, 2005 edition of Multichannel News, whose headline sums it up: "How I Started a Network Without Comcast." Moreover, there are many networks that have become viable with *no* cable carriage, reinforcing the point that there are a sufficient number of U.S. MVPD households served by competitors to support such programming.

In response to the second point, marketplace facts refute TAC's assertion. Comcast carries scores of independent networks. In fact, it has no choice but to carry a significant number of independent programmers because customers demand it.

The fact of the matter is Comcast owns an attributable financial interest (which, for purposes of the FCC's rules, can be as little as five percent) in only about seven percent of the channels it carries. In other words, 13 out of every 14 channels carried by Comcast are owned by companies that are completely independent of Comcast. This should not come as a surprise -- it is our goal, and a competitive necessity, to provide the best programming and the best value for our customers, regardless of who owns or produces the programming.

TAC lacks any basis for invoking the program carriage rules, which is the likeliest explanation for TAC's failure to file a complaint with the FCC. In the meantime, we have had continuing discussions with TAC over the past year, and we remain open to a meaningful dialogue. But it is important to remember that TAC is entirely in control of its own fate – and its failure to secure any meaningful carriage commitment from any of our established competitors suggests that the problem lies not with Comcast, but with TAC's business plan.

I anticipate that some parties at today's hearing may raise other complaints or allegations regarding the operation of the program access or program carriage rules, and I stand ready to provide information to the Committee that would respond to any such complaints.

Conclusion

Over the past 14 years, competition in the video marketplace has exploded. When the 1992 Cable Act passed, the majority of consumers had little choice from whom they purchased multichannel video service and comparatively limited programming choice. Today, almost every consumer in America can choose from among at least three MVPDs, each offering hundreds of programming services. And the number of viable programming alternatives aimed at the consumer market continues to increase with telephone company entry, innovations by terrestrial broadcasters, the emergence of the Internet as a viable video medium, and other distribution options.

The video marketplace is robust, dynamic, and hotly competitive. In light of the changes in both distribution and content creation over the past 14 years, this is the time for Congress to consider reducing, not expanding, regulation of video content. I urge this Committee to demand the facts from those on this panel who would argue otherwise, because the facts do not support their calls for regulation.

I thank the Committee for this opportunity to appear today.

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OPINION

PLAYBACK

How I Started a Network —Without Comcast

BY C. MICHAEL COOLEY

It has been said of late that if a network doesn't secure Comcast Corp., the nation's largest MSO, then it will have a tough time even getting a foot in the door to start talks with the remaining cable providers.

Perhaps these folks haven't considered The Sportsman Channel (TSC) and how we had already secured the remaining cable operators: Time Warner Cable, Charter Communications Inc., Adelphia Communications Corp., Cox Communications Inc. and 14 other of the top 25 MSOs, all without the security or assistance of having Comcast. We are living proof that channels can survive without Comcast, contrary to the belief of many. TSC has been around for over two years and our channel, which is dedicated exclusively to hunting and fishing programming, is not just surviving, but flourishing.

Other start-up networks tend to have the approach of "If you have Comcast, they will come." Securing carriage is the key, but there is a formula: Provide a superior quality channel with lower subscriber fees that draws subscribers. Our team focuses on quality customer service and first-class marketing tactics to our affiliates, for an "If you can prove yourself, they will come" approach.

Another successful method for an independent channel employed at TSC was setting the launch date *and* keeping it.

The date never moved, even though we didn't have any agreements signed when the champagne popped on April 7. Our team approached the launch with 100% confidence in our product.

It certainly didn't take long after we drank the champagne for us to secure our first contracts with the National Cable Television Cooperative. This gained the attention of MSOs in the top 10 — and eventually deals were struck in 2004.

We just recently completed our agreement with Comcast, which makes them the last of the top five MSOs to come on board, not the first. This proves that we didn't need a deal with them to validate our channel or secure distribution with other MSOs.

Some pessimists believe Comcast only launches channels if it is financially involved. TSC is an independent, and Comcast is, after all, still a business. It will launch channels that it believes will keep it competitive and increase subscriber counts.

No one knows better than me that starting a new channel in this market is a daunting and difficult task. But it can be done, and I am not sure if holding Comcast responsible is entirely the reason for the high level of complexity we experience as channel presidents.

That's especially true since there are 70 million other cable subscribers, plus another 25 million DBS subscribers out there.

Just because you are unable to be first to reel in a big fish doesn't mean the ocean won't provide you with a worthy catch. ■

C. Michael Cooley is president and CEO of The Sportsman Channel.