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Video Program Distribution and Cable Television: Current Policy Issues and Recommendations

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VIDEO PROGRAM DISTRIBUTION AND CABLE TELEVISION

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Executive Summary

Important changes in the video market, particularly with respect to cable television over the last ten years, have raised several policy issues. The expanded technological capabilities of optical fibers and computers create new ways to transport and access video programming in cable systems and telephone networks. Meanwhile, growing market concentration and structural changes in the cable television industry have placed the potential for expanding consumer video choices at risk. In addition, some courts are effectively limiting the ability of municipalities and other government entities to carry out the intent of the Cable Act to be the primary source of regulation over cable television.

Today, over 80 percent of all U.S. homes have access to cable television and about 50 percent subscribe to basic cable service. Important segments of the population, however, do not yet have access to cable television. Generally, cable television has been a great success, with rapid growth in the number of systems, number of subscribers, asset values, and gross revenues. Cable has shifted from its early role as a broadcast antenna service focused on facilities, to an original programming service, due largely to the advent of satellite technology. The number of cable networks has steadily grown, attracting more subscribers, which in turn has lead to greater support from advertisers and the creation of additional cable networks.

Success has been accompanied by an accelerating amount of criticism of the cable industry. There is evidence that rates of basic cable service have greatly increased in some communities. These increases may simply be adjustments to rates kept artificially low prior to deregulation; it is too soon to reach an informed judgment.

The common occurrence of exclusive cable franchises does not serve the public interest. The franchising process has seriously impeded entry by competitors and imposes substantial costs on franchisees, cable subscribers, and the public. Municipalities could, instead, encourage competitive cable operators to service a franchise area which would result in greater choice, better service, and lower prices to consumers. In fact, many of the "market power" problems and issues we face today are direct outgrowths of a franchising process that has, and continues to, erect large entry barriers.

Telephone companies should be encouraged to provide video transport facilities on a common carrier basis, leasing channels to all video programmers (for example, current cable operators, broadcasters, sports organizations, producers, and others.) At least two steps might encourage the provision of facilities by telephone companies: removing the requirement that common carriers lease channels only to franchised cable operators or franchising authorities, and permitting telephone companies to

provide some services ancillary to the provision of video transport facilities (or channel capacity), such as billing, order taking, and maintenance.

Instead of permitting telephone companies to provide both video transport and programming services in their service areas, such "video common carriage" will, we believe, insure the greatest possible diversity of viewer choice and will increase the competitiveness of the video market. Such video common carriage would also reduce concerns arising from ownership trends in the cable industry, such as the ability of cable firms to limit the availability of programming to competitive media.

Television broadcast networks and local broadcast licensees are prohibited from operating cable systems. The national television market has changed substantially since the network exclusion was created so its repeal is appropriate. The more difficult question of local broadcast cross ownership is best addressed by the Federal Communications Commission on a waiver basis.

Two important trends in the nationwide growth of cable television, increased ownership concentration of system operators and vertical integration of those operators into programming supply, pose potential diversity problems. In terms of vertical integration, there are not substantial differences in the number or type of programming carried by cable operators whether affiliated with a programming network or not. At this time, limits on vertical integration are undesirable. Government policies should not impair the ability of cable to develop new programming and advertising alternatives in the form of cable networks. However, the trend towards increased concentration of ownership among cable operators may increase the ability of those firms to reduce diversity of programming. There is increasing evidence that one or only a few firms have the ability to create a program distribution "bottleneck." Therefore, we recommend the FCC initiate an inquiry to evaluate the effects of cable ownership concentration on diversity.

Program exclusivity can benefit buyers, sellers, and the public because it is an important component of the copyright system which ensures creators have adequate incentives to produce more programming. The Copyright Act generally strikes an appropriate balance between the rights of owners and the needs of users. The compulsory license for cable television, however, should be phased out over time because it unnecessarily distorts the market for video programming. Until that license is repealed, however, broadcasters should be able to enforce programming contracts in which they have negotiated exclusive rights, and it would be reasonable to condition exercise of the cable compulsory license on carriage of all local broadcast signals.

Throughout this study, we have sought policy options which will result in consumers having a choice of multi-channel video program services. That choice can be accomplished by more direct competition from multiple cable systems serving more communities. Alternative multi-channel program services such as DBS and MMDS could provide non-wire based competition. In addition, telephone companies and other firms providing video transport facilities over wire-based networks will create more opportunities for competitive program service providers. The problems which are foreshadowed by the trends towards vertical integration and ownership concentration could be largely diminished by greater competition in the local market.

Introduction

In a generation, the video programming marketplace has been transformed. Where once there was only network television broadcasting, there are now such options as multiple independent television stations, videocassette recorders (VCRs), home satellite dishes (HSD), and cable television. In the future, video programs may also be widely distributed via high-powered, direct broadcast satellites, multi-channel multipoint distribution services (MMDS), and fiber optic cables. Policy issues affecting cable television and other video distribution systems will profoundly affect the video programming choices available to consumers, the firms offering those choices, and the prices of those choices.

Over the last thirty years, the American cable television industry has gone from a relatively minor commercial adjunct to the over-the-air television broadcasting business to the dominant video distribution medium in the country, with over 80 percent of all U.S. television households passed by cable and projected 1988 revenues of about $12 billion derived from serving about 52 percent of 90 million homes.

Entrepreneurial initiative has accomplished much of this industry growth. But it is also attributable to Government policies aimed at fostering the emergence of an alternative to the broadcast distribution system long dominated by the national networks and the telephone distribution system long controlled by AT&T.

Perhaps the hand of Government has been most evident in the local franchising process which has insulated the vast majority of cable systems from direct competition. At the Federal level, special tax treatment of limited partnerships -- heavily employed in the early years by cable television companies -- as well as legislative measures accorded cable firms guaranteed access to telephone and electric utility poles at regulated prices. For many years, cable television systems were not subject to ordinary copyright laws, and when they were brought under that regime, cable was granted extraordinarily preferential terms. The cable television business was also a primary beneficiary of the rapid growth of the domestic communications satellite business, itself in large part the result of Federal policies which made technology as well as launch services available at concessionary prices.

Demand for cable television services remains strong; at the height of recessionary conditions prevailing earlier this