

**Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554**

In the Matter of)	
)	
)	
Annual Assessment of the Status of Competition)	MB Docket No. 17-214
in the Market for the Delivery Of)	
Video Programming)	
)	

**COMMENTS OF
THE FREE STATE FOUNDATION***

I. Introduction and Summary

These comments are submitted in response to the Commission’s request for comments regarding Section 628(g)’s requirement that the Commission report annually on “the status of competition in the market for the delivery of video programming.” There is clear and convincing evidence that today’s nationwide video market is fully and effectively competitive. The Commission should declare this to be the case in its upcoming *Nineteenth Video Competition Report*. In light of today’s effectively competitive conditions, the Commission should pull the plug on open proceedings that proposed to expand the agency’s legacy video rules to new services, devices, and apps. Also, through its Modernization of Media Regulation Initiative, the Commission should eliminate its legacy video rules where possible or reform them by making them less intrusive and costly. And at long last, as contemplated by the Communications Act, the Commission should sunset its video navigation device regulations.

At the end of 2015, 99% of all households were served by three competing multi-channel

* These comments express the views of Randolph J. May, President of the Free State Foundation, and Seth L. Cooper, Senior Fellow. The views expressed do not necessarily represent the views of others associated with the Free State Foundation. The Free State Foundation is an independent, nonpartisan free market-oriented think tank.

video subscription distributors (MVPDs), and 18% of the households were served by four MVPDs. Cable MVPDs' share of the national market was 53% of the households, while direct broadcast satellite (DBS) providers served 33%, and former telephone company MVPDs served 13.4% percent.

While total MVPD subscriptions dropped for the third straight year in 2015, consumer adoption of online video distributor (OVD) services continues to rise. By early 2017, Amazon Prime subscriptions climbed to 80 million and Netflix surpassed 50 million. Also, Hulu subscriptions reached 12 million by mid-2016. According to a 2017 survey, 64% of TV households subscribed to Amazon Prime, Hulu, or Netflix. Niche OVD services, such as HBO Now, also have emerged. Now MVPDs offer online video services, such as Verizon's go90. And broadcast networks offer streaming video services and apps, such as CBS All Access.

MVPDs offer consumers different multi-functional video devices, including ones that are exclusive to their services, such as Comcast' X1 DVR and Charter's WorldBox. MVPDs support CableCARD-enabled devices manufactured by third parties. Internet-connected streaming devices for viewing content provide additional choices: smart TVs, Apple TV, Amazon Fire TV, Chromecast, Roku, gaming consoles, tablets, and smartphones. MVPD services are increasingly accessible by streaming devices. All of this points to a fully competitive video device market functioning in conjunction with a fully competitive video distribution market.

The Commission is to be commended for acknowledging "intergroup competition" among MVPDs, OVDs, and broadcast stations in preparing its new report. Indicators that OVD services increasingly are perceived by consumers as close substitutes include but are not limited to: continuing declines in MVPD subscriptions as OVD subscriptions rise, availability of new OVD services and original OVD content, and preferences for OVDs among younger consumers.

There remains a glaring disconnect between the competitive state of today's convergent, IP-based digital video market and the legacy regulatory framework that was premised on early 1990s cable bottlenecks and analog technology. Old regulations offer little to no benefit but impose compliance costs and risks dis-incentivizing innovation and investment.

As part of its Modernization of Media Regulation proceeding, the Commission should remove its legacy video rules or reorient them in a deregulatory direction. The Commission should close regulatory proceedings in which it proposed to expand legacy regulations, such as its MVPD re-definition proceeding for expanding program access rules to OVDs and its AllVid proceeding for imposing legally dubious and extremely costly new rules on video devices. Further, the Commission should sunset network non-duplication and syndicated exclusivity regulations, since carriage and payment arrangements can be handled by negotiated contracts.

For legacy video restrictions that are contained in statute and cannot be repealed, the agency should establish a rebuttable presumption of market competition in applying such restrictions and thereby reduce the burdens they pose. The Commission can employ rebuttable evidentiary presumptions of market competition for case-by-case inquiries into provider conduct under its legacy video regulations, such as its program access and carriage rules. Under this approach, clear and convincing evidence of consumer harm tied to market power abuse would be required to justify regulatory intervention. The Commission or a party claiming a violation would bear the burden of overcoming that presumption of market competition with evidence.

Finally, given competition among MVPDs and the emergence of choices among services and devices for viewing Internet-accessible video programming, the Commission's old video device rules are no longer justifiable. Data regarding OVD subscribership and substitutability for MVPD service bolsters this conclusion. The Commission should examine the need for such rules

and, in the absence of findings of market power or consumer harm, declare the market for video devices to be “fully competitive” and sunset those rules pursuant to the direction contained in Section 629 of the Communications Act.

II. The Nationwide Video Services Market Is Effectively Competitive

Market data cited in the *Eighteenth Video Competition Report* (2017),¹ in addition to more recent data, provides clear and convincing evidence that the national MVPD market is effectively and fully competitive. The upcoming report should expressly recognize this.

The *Eighteenth Report* indicates that, at the end of 2015, 99% of all households were served by three competing MVPDs, and 18% of households were served by four MVPDs.² Cable MVPDs’ share of the national market was 53%, while direct broadcast satellite (DBS) providers served 33%, and former telephone company MVPDs served 13.4% percent.³ Meanwhile, total MVPD subscriptions dropped one million, down to a 99.4 million total.⁴

Additionally, the *Eighteenth Report* identified the rising popularity of OVD services.⁵ In the time since the report was released, consumer adoption of OVD services has increased further. By the first quarter of 2017, Amazon Prime subscriptions in the U.S. climbed to 80 million and Netflix subscriptions in the U.S. surpassed 50 million.⁶ Also, Hulu subscriptions in the U.S. reached 12 million by the second quarter of 2016.⁷ According to an early 2017 survey, about

¹ Annual Assessment of the Status of Competition, *Eighteenth Report* (“*Eighteenth Video Competition Report*”), MB Docket No. 15-158 (rel. Jan. 17, 2017) (Media Bureau), available at: http://transition.fcc.gov/Daily_Releases/Daily_Business/2017/db0117/DA-17-71A1.pdf.

² *Eighteenth Report*, at ¶ 21 (Table III.A.2).

³ *Eighteenth Report*, at ¶ 19.

⁴ *Eighteenth Report*, at ¶ 68.

⁵ *Eighteenth Report*, at ¶¶ 128-187.

⁶ Stephanie Pandolph and Jonathan Camhi, “Amazon Prime subscribers hit 80 million,” *Business Insider* (April 27, 2017), available at: <http://www.businessinsider.com/amazon-prime-subscribers-hit-80-million-2017-4>; Tom Huddleston, Jr. “Netflix Has More U.S. Subscribers Than Cable TV,” *Fortune* (June 15, 2017), available at: <http://fortune.com/2017/06/15/netflix-more-subscribers-than-cable/>.

⁷ Hulu, Press Release: “Hulu Goes Bigger and Bolder at 2016 Upfront Presentation, Unveils +30% Growth in Subscribers, New Programming Deals and Ad Partnerships (May 4, 2016), available at: <https://www.hulu.com/press/hulu-goes-bigger-and-bolder-at-2016-upfront-presentation-unveils-30-growth-in->

64% of TV households subscribed to Amazon Prime, Hulu, or Netflix.⁸ As the *Eighteenth Report* recognized, niche OVD services have also been launched – such as HBO Now, Showtime, and STARZ. MVPDs offer online video services, such as DISH Network’s Sling TV, Verizon’s go90, and AT&T’s DIRECTV NOW. Additional OVD services are offered by wireline providers.⁹ Broadcast networks have also launched streaming video services and apps, such as CBS All Access and Watch ABC.¹⁰ Moreover, OVDs are negotiating “exclusive streaming rights, which they use to attract consumers seeking specific video content,” and are also “investing in original programming to attract and retain customers.”¹¹

The *Eighteenth Report* grudgingly acknowledged “MVPDs are introducing innovative services on the devices that they lease,” yet claimed the device market lacks competition. This is an unsupportable claim. MVPDs offer consumers multi-functional HD video devices that are unique to their respective services, including the Comcast X1 DVR, Charter WorldBox, and DIRECTV HR 44 Genie Server. Further, all MVPDs support CableCARD-enabled devices manufactured by third parties. Importantly, Internet-connected streaming devices provide additional choices for consumers: smart TVs, Apple TV, Amazon Fire TV, Chromecast, Roku, video game consoles, Internet-connected Blu-Ray players, tablets, and smartphones. Increasingly, streaming devices can access MVPD content.

Consumer usage of apps to view video content on Internet-connected devices also continues to rise. As described earlier, most popular pay-TV networks have stand-alone apps for

[subscribers-new-programming-deals-and-ad-partnerships/](#). See also *Eighteenth Video Competition Report*, at 75, ¶ 180.

⁸ Leichtman Research Group, “82% of U.S. TV Households Have a DVR, Netflix, or Use VOD,” *supra*.

⁹ Public Notice: Media Bureau Seeks Comment on the Status of Competition in the Market for the Delivery of Video Programming, MB Docket No. 17-214 (Aug. 24, 2017), at 5-6.

¹⁰ See, e.g., Richard Lawler, “Now Fox is live streaming its prime-time TV across the US,” *Engadget* (July 12, 2016), available at: <https://www.engadget.com/2016/07/12/now-fox-is-live-streaming-its-prime-time-tv-across-the-us/>.

¹¹ *Eighteenth Report*, at ¶ 160-161.

smart TVs and streaming devices. OVD services are widely viewable on the same devices.¹² And MVPDs have introduced or planned apps that consumers can use to watch MVPD video programming without set-top boxes. Over 460 million IP-enabled consumer-owned devices support video apps.¹³

Broadcast TV is a resurgent alternative for video consumers. Households relying on over-the-air (OTA) broadcast service exclusive of any MVPD service increased to 12.4 million in 2015. 26.7 million households relied exclusively on OTA service on at least one TV. Some consumers “seek to use a combination of OVDs and broadcast services” in place of an MVPD.¹⁴ According to an analysis cited in the report, in 2015 retransmission consent fees paid by MVPDs to TV broadcast stations increased to about 23% of total TV revenue, or \$6.4 billion.¹⁵

In view of the prevalence of consumer choice and competition in the video marketplace, the forthcoming *Nineteenth Video Competition Report* should finally acknowledge that the nationwide market for MVPD services and the market for video devices are effectively and fully competitive.

III. OVD Services Are Substitutes for MVPD Services

The Commission is to be commended for taking a closer look at “intergroup competition” between MVPDs, OVDs, and broadcast stations in preparing its upcoming report.¹⁶ Data regarding consumers who have dropped MVPD services in favor of OVD services provides strong indicators that OVD services are increasingly perceived by consumers as close substitutes. Additional indicators of OVD substitutability include: the rising number of OVD services and increasing content – including exclusive content – available via such services, the growing

¹² *Eighteenth Report*, at ¶ 59.

¹³ *Eighteenth Report*, at ¶ 194.

¹⁴ *Eighteenth Report*, at ¶ 66.

¹⁵ *Eighteenth Report*, at ¶ 125.

¹⁶ Public Notice, MB Docket No. 17-214, at 3.

number of OVD subscriptions, preferences for OVD services among younger consumers, and growing financial investment in original OVD programming.

The *Eighteenth Report* – like its two predecessor reports – shows a continuing overall decrease in MVPD subscriptions,¹⁷ while OVD subscriptions climbed over the same period. As indicated earlier, MVPD subscriptions declined by about one million between the end of 2014 and the end of 2015 to just over 99 million, whereas the combined total of subscribers to Amazon Prime, Netflix, and Hulu OVD services now surpasses 140 million. News accounts and analyst forecasts repeatedly show the seriousness with which investors take recent and probable future MVPD subscriber losses.¹⁸ The *Eighteenth Report* also observed that MVPDs offer “skinny bundles” of video channels and reduced rates “[i]n response to competition from OVDs, slow growth in household incomes, and higher programming costs.”¹⁹

The Commission should reject dismissals of OVD substitution that are based on unduly narrow product definitions or constrained conceptions about competition. Price competition between MVPDs and OVDs constitutes only one plane of competition. Quality and quantity enhancements and innovative offerings also benefit consumers. MVPDs continue to offer service upgrades, including mobility viewing, time-shifting capabilities, and more channels. Ultra-HD video is beginning to be offered, with additional rollouts slated. Any substitution analysis must factor in such values offered by MVPDs. Further, the Commission should consider the MVPD market’s susceptibility to the “innovator’s dilemma,” whereby value-conscious consumers of established services are enticed away by simpler, less expensive OVD options.²⁰

¹⁷ *Eighteenth Report*, at ¶ 68.

¹⁸ See, e.g., Gerry Smith and Michaela Ross, “Cable Channel Subscriber Losses Have Investors Bracing for Worst,” *Bloomberg* (Feb. 10, 2016), available at: <http://www.bloomberg.com/news/articles/2016-02-10/media-investors-on-edge-as-cable-networks-cite-subscriber-losses>.

¹⁹ *Eighteenth Report*, at ¶ 53.

²⁰ See, e.g., Claire Groden, “Why Uber isn’t Disruptive but Netflix Is,” *Fortune* (Nov. 17, 2015), available at: <http://fortune.com/2015/11/17/uber-disruption-christensen/>; Adam Richardson, “Netflix’s Bold Disruptive

IV. The Commission Should Remove or Reorient Legacy Video Rules in a Deregulatory Direction as Part of Its Modernization Media Regulation Initiative

There remains a glaring disconnect between the effectively competitive state of today's convergent, IP-based digital video market and the legacy video regulations premised on early 1990s cable bottlenecks and analog technologies. Legacy video regulation offers little to no discernible benefit in today's competitive video market. Rather, such regulatory restrictions impose compliance costs and create dis-incentives to innovation and investment, resulting in conditions ultimately unfavorable to consumer welfare.

As part of its Modernization of Media Regulation proceeding,²¹ the Commission should remove its legacy video rules or reorient its legacy video framework in a deregulatory direction. In a *Perspectives from FSF Scholars* paper, "A Proposal for Reforming the FCC's Video Competition Policy,"²² FSF Senior Fellow Seth Cooper recommended the Commission undertake just such a comprehensive review of the Commission's video policies. Consistent with that reform proposal, and as part of its Modernization of Media Regulation Initiative, the Commission should close regulatory proceedings in which it has previously proposed to expand legacy regulations. The Commission should, for example:

- Close the MVPD re-definition proceeding. Extending the scope of program access, program carriage, or other legacy requirements to certain online video services makes no sense. Those disruptive services emerged in a free market environment that should be preserved to foster future growth.
- Close the fatally flawed AllVid proceeding. New regulations on devices and apps are unnecessary. And the Commission's proposal was not based on any serious

Innovation," *Harvard Business Review* (Sept. 20, 2011), available at: <https://hbr.org/2011/09/netflix-bold-disruptive-innovation>.

²¹ https://apps.fcc.gov/edocs_public/attachmatch/FCC-17-58A1.pdf.

²² Seth L. Cooper, "A Proposal for Reforming the FCC's Video Competition Policy," *Perspectives from FSF Scholars*, Vol. 12, No. 5 (Feb. 8, 2017), available at: http://www.freestatefoundation.org/images/A_Proposal_for_Reforming_the_FCC_s_Video_Competition_Policy_020717.pdf.

analysis.²³ AllVid would have imposed heavy costs, initially to be paid by MVPDs and video programming owners, but ultimately to be paid by consumers. The Copyright Office has described how the AllVid proposal is contrary to copyright law and video programming owners' "exclusive right to *authorize parties of their choosing* to publicly perform, display, reproduce and distribute their works."²⁴ To the extent the Commission proposed ways to reduce existing burdens, it should promptly adopt such relief and close the proceeding.

- Close the program carriage procedures proceeding. Therein, the Commission adopted a "stand-still" rule requiring MVPDs to carry programming for an indeterminate period after their contracts with independent video programmers expired. That is contrary to free market principles and violates MVPDs' First Amendment rights in choosing TV channel lineups. The rule was struck down by the Second Circuit for violating notice requirements. Closing the proceeding will ensure that it is not revived.

In connection with its Modernization of Media Regulation proceeding, the Commission should eliminate rules that are no longer justifiable because breakthroughs in digital technology and competition has replaced analog-era cable TV bottlenecks with competition among convergent IP-based platforms. For example, the Commission should sunset network non-duplication and syndicated exclusivity regulations. Those regulations, which allow local TV broadcast stations to block MVPDs who carry a network's local broadcast affiliate on their channel lineups from importing programming from out-of-market sources, are not necessary. National broadcast TV networks, local TV stations, and MVPDs are capable of negotiating contracts to make royalty and other payment arrangements in exchange for carriage.

For legacy video restrictions that are contained in statute and cannot be repealed by the Commission, the agency should establish a rebuttable presumption of market competition in applying such restrictions and thereby reduce the burdens they pose. The Commission should likewise adopt – or at least propose – such deregulatory presumptions through its Modernization

²³ See Government Accountability Office, Video Programming: FCC Should Conduct Additional Analysis to Evaluate Need for Set-Top Box Regulation" ("GAO Report"), GAO-17-785 (September 2017), available at: <https://www.gao.gov/assets/690/687512.pdf>.

²⁴ Maria A. Pallante, Register of Copyrights, U.S. Copyright Office, Letter to Blackburn, Butterfield, Collins, and Deutch (Aug. 3, 2016), available at: http://blackburn.house.gov/uploadedfiles/co_set-top_letter.pdf.

of Media Regulation Initiative. As we explained in our *Perspectives* paper, “A Proposal for Reforming the FCC’s Video Competition Policy”:

Rebuttable evidentiary presumptions of market competition can also be employed when the Commission conducts case-by-case inquiries into provider conduct under its legacy video regulations. Under this approach, clear and convincing evidence demonstrating consumer harm tied to market power abuse would be required to justify regulatory intervention. The Commission or a party supporting regulatory intervention or claiming occurrence of a violation would bear the burden of overcoming that presumption of market competition with proffered evidence.

For instance, the Commission’s *Program Access Orders* (2010 and 2012) replaced its ban on exclusive contracts by vertically-integrated cable programmers with a rebuttable presumption of market competitiveness, subject to qualifications. Pursuant to a comprehensive review of its video regulations, the Commission should seek ways to expand this type of approach taken in the *Program Access Orders*. In the video market context, the net effect of applying such a rebuttable evidentiary presumption of marketplace competition would be to make the Commission’s regulations less intrusive and more protective of First Amendment free speech rights of MVPDs. This is another important reason for doing so.²⁵

Consistent with this reform proposal, the Commission should, for example, adopt and apply a rebuttable presumption of market competition in connection with its program carriage rules. The *Program Carriage Order* (2011) requires only a *prima facie* case of unreasonable discrimination by MVPDs against unaffiliated programmers based on a set of indeterminate factors that stress competitor welfare. Applying a presumption of market competition and requiring parties filing program carriage complaints to provide clear and convincing evidence of harm tied to market power abuse would better respect MVPDs’ First Amendment rights.

The Commission’s adoption of rebuttable presumptions of effective competition in local cable markets was deemed a proper exercise of agency discretion and upheld by the D.C. Circuit

²⁵ Randolph J. May and Seth L. Cooper, *Perspectives from FSF Scholars*, Vol. 12, No. 5 (February 8, 2017), “A Proposal for Reforming the FCC’s Video Competition Policy,” at: http://www.freestatefoundation.org/images/A_Proposal_for_Reforming_the_FCC_s_Video_Competition_Policy_020717.pdf.

in *NATOA v. FCC* (2017).²⁶ That precedent would apply to the Commission’s adoption of a rebuttable presumption of market competition as proposed here.²⁷

V. The Commission Should Sunset Its Legacy Video Device Rules Absent Findings of Market Power and Consumer Harm

When the Commission first implemented Section 629 in 1998, local MVPD markets were still highly concentrated and permitted exercise of market power by incumbent cable systems. But Section 629 includes a unique sunset provision whereby its rules “shall cease to apply when the Commission determines that: (1) the market for the multichannel video programming distributors is fully competitive; (2) the market for converter boxes, and interactive communications equipment, used in conjunction with that service is fully competitive; and (3) elimination of the regulations would promote competition and the public interest.”²⁸ A recent GAO report has raised the sensible question of whether its existing rules are still necessary.²⁹

Given competition among MVPDs and the emergence of choices among services and devices for viewing Internet-accessible video programming, the Commission should no longer be so intrusively regulating the video device market. Data regarding OVD subscribership and substitutability for MVPD service bolster this conclusion. Combined, these data points supply an evidentiary basis for the Commission to declare the video device market “fully competitive” and to sunset its Section 629 rules immediately or on a set-timetable. A “fully competitive” market should be found when there is no evidence of market power or consumer harm.

²⁶ *National Association of Telecommunications Officers Association v. FCC*, No. 15-1295 (D.C. Cir. July 17, 2017); Amendment to the Commission’s Rules Concerning Effective Competition; Implementation of Section 111 of the STELA Reauthorization Act, MB Docket No. 15-135, Report and Order (“*Effective Competition Order*”) (released June 3, 2015), available at: http://transition.fcc.gov/Daily_Releases/Daily_Business/2015/db0610/FCC-15-62A1.pdf.

²⁷ Randolph J. May and Seth L. Cooper, “D.C. Circuit Ruling Supports FCC’s Use of Deregulatory Presumptions,” *Perspectives from FSF Scholars*, Vol. 12, No. 24 (July 27, 2017), available at: http://www.freestatefoundation.org/images/D.C._Circuit_Ruling_Supports_FCC_s_Use_of_Deregulatory_Presumptions_072717.pdf.

²⁸ 47 U.S.C. § 549(e).

²⁹ See GAO Report, *supra*.

VI. Conclusion

For the foregoing reasons, the Commission should declare that the MVPD nationwide market and the video device market are effectively and fully competitive and eliminate or reform its video regulatory policies in accordance with the views expressed herein.

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