The Free State Foundation

A Free Market Think Tank For Maryland…Because Ideas Matter

Perspectives from FSF Scholars
December 2006
Vol. 1, No. 9

Below is a letter to the editor by Free State Foundation President Randolph J. May published in the Wall Street Journal on December 2, 2006, and the November 25th WSJ editorial, "Tied Up in Cable," to which the letter responds:

Your editorial highlights the impending regulatory debacle unless the FCC waives its so-called integration ban that on July 1, 2007, will prevent cable operators from offering their customers set-top boxes that contain integrated security and navigation functions. Failure to waive the regulation is expected to add $2-$3 to the monthly lease charge for digital set-top boxes at the same time the government, in conjunction with the transition to Digital TV, is preparing to provide subsidies to all those who do not already have the capability of receiving digital transmissions. Discouraging consumers from acquiring new digital boxes by making them more expensive during the DTV transition would be a glaring example of the government working at cross-purposes to the detriment of both consumers and taxpayers.

You are right that the "supposedly de-regulatory" 1996 Telecommunications Act delegated the authority to the FCC to devise the regulations that are now the root cause of the problem. But at least in this instance, as opposed to many others in the 1996 Act, Congress was foresighted enough to recognize that technology and marketplace developments might outrun any regulations devised by the FCC. Indeed, in addition to the waiver authority cited in your editorial, Congress included in the statute explicit authority allowing the FCC to sunset the set-top regulations upon a determination that the multichannel video and navigation device markets are competitive and that elimination of the rules would promote the public interest. With competition among what heretofore we have called "cable," "satellite," "telephone," and "wireless" companies becoming ever more fierce to provide an array of broadband services, including multichannel video, it is time for the FCC not only to waive the rules but to "sunset" them. In the competitive multichannel video marketplace that now exists, "integration bans" don't make sense. The service providers have every incentive not only to allow, but to encourage, the use of whatever equipment will maximize the value of their service platform in the eyes of consumers.

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Tied Up in Cable
WSJ, November 25, 2006; Page A8

With mergers to rule on, multibillion-dollar bets on fiber-optic cable being laid and obscenity on broadcast television to babysit, you'd think the Federal Communications Commission would have better things to do than micromanage the market for cable boxes -- a market that mostly doesn't exist anyway. No such luck.

Like much of the trouble in telecom these days, this problem goes back to the supposedly de-regulatory 1996 Telecommunications Act. Tucked in there alongside its better-known goofs was Section 304: "Competitive Availability of Navigation Devices." This section required the FCC to open up the market for third-party "navigation devices" -- which basically meant cable boxes.

This idea encapsulates in a nutshell what was wrong with the 1996 Act. Rather than lifting regulations and letting market forces prevail, the Act is riddled with attempts to generate competition by government fiat. So it is with Section 304. Without really asking whether it made sense to require competition in cable boxes, our Solons simply decreed that the FCC should make it happen.

It hasn't happened, in part because Section 304 has never been enforced and in part because it's unclear just how big a market there is for consumer-purchased set-top boxes when the boxes can be leased from the cable company at regulated rates for a couple of dollars a month. The regulatory machine nonetheless marches on. And unless the FCC takes action on a number of waivers requested by the cable companies, the industry faces a $600 million annual bill to comply with a regulation with no real purpose. That's right: $600 million, which will of course be passed along in higher rates for consumers.

In order to facilitate competition, the FCC required the cable companies to come up with a way to provide their security codes to third-party devices, whether they are set-top boxes or cable-ready televisions. The method settled upon was a device called a cablecard. Users who didn't want the set-top box could instead get a cablecard from the cable provider and plug that into their TV, for example. This has been done, and there are some people out there using these cablecards, although most people don't bother.

The trouble with the FCC has come because the cable companies themselves don't use the cablecards in their own boxes -- the theory is that if everyone had to use the cards, the cable companies might somehow make the cards more

attractive to consumers. So the FCC wants the cable companies to use cable boxes that need a cablecard, too -- never mind that the cost is high and the benefits to anyone are dubious.

The FCC could make this go away by granting a waiver from the rule, as the 1996 Act allows when the FCC determines it is in the public interest to do so. But so far there's been little sign that the FCC is inclined to do the industry any favors. The National Cable and Telecommunication Association -- a cable industry lobbying group -- put in a waiver request back in July. The FCC is supposed to rule on waivers within 90 days, but it didn't even put the application out for public comment until a week after we first called the FCC about the issue late last month.

The cable industry has had run-ins with FCC Chairman Kevin Martin over "a la carte" pricing and the expansion of obscenity rules to cable channels. This lends the cablecard shakedown a flavor of political payback -- especially coming from what is supposed to be a deregulatory, free-market-oriented FCC. Mr. Martin, who long bemoaned the absence of a Republican majority on the Commission, now has one, but there's still too little evidence of the Commission acting like it.

Concern about Mr. Martin's commitment to free markets had led Senators to hold up his renomination as Chairman for six months, turning what should have been a no-brainer into a last-minute confirmation earlier this month. The Commission, and Mr. Martin, could do the economy a favor by worrying less about political gamesmanship and more about getting on with the deregulation the telecom industry needs.

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