513. In general, ordinary market contracting is an efficient governance structure for transactions supported by general purpose assets not dedicated to the specific output demand of a given customer. As asset specificity deepens, market contracting as a governance structure gives way to either hybrid structures or hierarchy (vertical integration) as the least costly to organize transactions.[1088] The pervasiveness of asset specificity in the program production industry suggests that complex contracts between broadcast television networks and program suppliers may not be the least costly governance structure for effectuating transactions.

514. Broadcast television networks have a single, strategic focus, namely, the maximization of the number of television viewers that are attracted to mass audience and niche audience programming.[1089] This strategic focus is crucial to broadcast television networks, since the sale of audiences to national advertisers provides their only stream of revenue from broadcast operations in contrast to cable networks which may receive both advertiser and subscriber revenue.[1090] By contrast, local broadcast television stations pursue a more complex business strategy as licensed broadcast facilities. First, the local station seeks to maximize the size of its audience it attracts within its local television market. If the local station is a network affiliate, then the local station will promote the network's program schedule together with syndicated programming the station may acquire to help fill out its daily program schedule. Second, the local station will also promote its own locally-produced programming, such as news and public affairs programming, that it believes is responsive to issues or viewer preferences in the communities served by the station Station management may vary the allocation of time devoted to any particular type of programming, including network programming, to respond to emerging preferences or news events in the communities located in its local television market.

515. As the networks have lost viewer market share over the last decade in response to the growth in cable and DBS, the traditional contractual relationship between a television network and a local station affiliate may be a less efficient governance structure. From a transaction cost perspective, television networks view their massive sunk investments in network programming as increasingly risky assets as non-broadcast program options proliferate.

516. With respect to contractual safeguards, the networks have attempted to negotiate substantial penalties for failure to clear a full schedule of network programming. With respect to changes in governance structure, the broadcast television networks have argued for elimination of the

[1088] The condition of asset specificity, if pervasive, poses substantial contracting hazards such that ordinary market exchange as encountered in competitive markets may be impaired or even effectively blocked In other words, the transaction cost of operating a market mechanism as a governance structure in the presence of deep asset specificity may be so high that a market will simply fail. Thus, market failure may be attributable not only to various externalities but to excessive transaction costs as well This insight is attributed to Kenneth Arrow, according to Williamson *See* Oliver E. Williamson, THE ECONOMIC INSTITUTIONS OF CAPITALISM 19 n.8 (1985).

[1089] Roughly speaking, broadcast television revenues tend to be proportional to audience size. Assuming that marginal operating cost is small relative to the fixed cost of operating a broadcast television network and generally invariant with respect to changes in audience size, then maximizing audience size is roughly equivalent to maximizing profit.

[1090] In most cases, broadcast television networks today are organizational units of larger media enterprises, *e g*, ABC is one of numerous business units operated by the Disney corporation, that have numerous revenue streams. Corporate management ordinarily expects, however, that each business unit will recover its unit-specific fixed and variable costs, contribute to the cost of shared corporate services and functions, and earn unit-specific profit.

national ownership cap, which would permit the networks to substitute hierarchy (vertical integration) for the current contractual relationship with independently-owned station affiliates. Presumably, the networks believe, consistent with transaction cost logic, that conflicts in strategic focus between stations and the network respecting programming decisions can be resolved more efficiently, *i.e.*, at minimal transaction cost, if hierarchy, *i e.*, forward vertical integration, replaces market contracting as the governance structure.

517. Thus, our transaction cost analysis suggests that our national ownership cap probably restricts the full transition to the least costly way for organizing transactions between television networks and local television stations, *i e.*, forward vertical integration, *assuming* that realization of a network's singular strategic focus on mass or niche audience size is the preferred policy objective. If, however, locally produced programming and ultimate program selection authority are a higher policy priority, then our transaction cost economic framework identifies the relevant policy trade-off, namely, the incremental social benefit of local programming viewed as a component of our localism policy goal versus the increased social and private costs of inefficient contracting.

518. *Program Production and Acquisition Market.* Competition in the program production and acquisition market is important because networks and owners of individual television stations compete with each other, as well as with cable television networks, to acquire programming that will continue to attract viewers to their channels. Although television station owners as a group are relatively significant purchasers of programming, we have no evidence that they exercise market power in the program production market [1091]

519 In considering the effect of the national television cap on competition in the program acquisition market, we first must identify the market participants. The broadcast networks contend that the following categories of firms compete in the program acquisition market: broadcast television networks, individual television stations (and group owners thereof), non-broadcast program networks (*i.e.* cable networks), syndicators, pay-per-view systems, VHS and DVD rental stores.[1092] NASA counters that major broadcast networks are a discrete sub-market, or "strategic group," within the program purchasing market.[1093] We generally agree with the networks' definition of the relevant market participants, although we exclude video sales and rental stores. We disagree with the networks' contention that such outlets are clearly a substitute for the delivered video programming of broadcast channels and cable channels. Those channels are the most conventional form of television viewing that can be substituted among by viewers almost instantly. It is possible to analyze the impact on the program acquisition market of relaxing the national television ownership cap by examining company expenditure shares. The following describes estimates of expenditure shares and calculation of a hypothetical HHI. The analysis assumes that the buyers in this market are broadcast networks, broadcast stations, and cable networks.[1094] OPP Working Paper 37 (Table 32) provides estimates for the year 2000 of programming

[1091] *See* Miscellaneous Requests, Independent Producers *infra* Section VIII(D)

[1092] Fox Comments, Economic Study E

[1093] NAB/NASA Reply Comments at 57

[1094] Our market definition includes pay cable networks as well as pay-per-view networks, but in the absence of data, they are excluded from this analysis

expenditures by the Big Four commercial networks and by television stations.[1095]

520. The table below provides program expenditure data for the year 2000 for the Big Four broadcast networks in column 2 and for eight firms that own cable networks in column 4. The eight firms include the top four broadcast networks, the two biggest cable network owners that do not own television stations, and the two companies with the biggest cable network shares that also own television stations. There is also a residual category that includes all other cable network expenditures as "Other."

521 Column 3 includes some hypothetical broadcast station owner shares. We do not know exactly how station expenditures are divided up among companies that own television stations. The numbers in this column represent a "worst case scenario" of what could happen if the national television cap were eliminated. In 2000 there were 1248 commercial television stations on the air. We know that the major commercial networks each reach virtually 100% of US television households and that each network has roughly 200 affiliated stations.[1096] If stations were distributed evenly across markets, then there would be room for six television station companies each reaching all US television households.

522 However, stations are not evenly distributed across markets. There are 50 Nielsen DMAs with fewer than four commercial stations, but they account for only 4.6% of US television households, so, from the point of view of station programming expenditures, it is reasonable to assume that each of the top four broadcast networks could achieve 100% coverage of US television households. However, there are 120 markets with fewer than six commercial television stations, and those markets account for 19 7% of US television households. So it is reasonable to assume that two additional station groups could grow to 80% coverage. This analysis assumes that television station program expenditures are divided among six firms: the four networks with 100% coverage, and Cox and Hearst, each with 80% coverage. We assume that expenditures are proportionate to coverage. The resulting expenditure estimates are in column 3. These estimates reflect a level of concentration that is higher than the true level There are 63 markets with more than six commercial stations in them. Adding up the excess over six stations in each market yields a total of 259 stations. We know that a single company can own multiple stations in the same market, but it is likely that even with more companies owning two stations in a market that there will still be more than six station owners in some markets.

523. Column 5 contains hypothetical total programming expenditures for the eight firms, aggregating across broadcast network, broadcast station, and cable network categories, and using the hypothetical consolidated television station ownership pattern described above. Column 6 shows market shares and column 7 implements the HHI calculation by squaring and summing the market shares. The resulting "worst case" HHI of 1535 is in the moderately concentrated range. Even with the highly unrealistic assumption of a 100% national reach by four companies, and an 80% reach by two companies,

[1095] The network figure is based on gross advertising revenue data from the Television Bureau of Advertising, FCC data on net advertising as a percentage of gross, and a trade press estimate of network programming expenditures as a percentage of net advertising revenues This yields a total figure for the top four networks rather than estimates for each network This analysis assumes that the networks each spend the same amount, which we believe is a reasonable approximation although Fox probably spends less than the other three. The television station estimate is based on data in the NAB Television Financial Report. The cable programming network figures come from Kagan World Media publications, ECONOMICS OF BASIC CABLE NETWORKS (2002) at 432-433 and CABLE PROGRAM INVESTOR (Jan. 17, 2003) at 6 Data are available for 65 basic cable networks and for the HBO, Showtime, and Starz premium channels

[1096] There are 210 Nielsen DMA markets, and in a few cases a network has more than one affiliate per market.

these levels of market share provide us with no basis to conclude that the current 35% cap on national television ownership is needed to protect competition in the program acquisition market.

Hypothetical HHI for Program Acquisition (data are year 2000 in millions of $)						
	Broadcast Network	Broadcast Station	Cable Network	Total	Market Share	Market Share Squared
Cox	0	969.5	139.4	1108.9	4.37	19.13502
Hearst	0	969.5	530	1499.5	5.92	34.98944
ABC	2581.75	1212	1276.7	5070.45	20.00	400.071
Fox	2581.75	1212	521.8	4315.55	17.02	289.812
GE	2581.75	1212	300	4093.75	16.15	260.7875
Viacom	2581 75	1212	1466.4	5260.15	20.75	430.5666
Time Warner	0	0	2162.9	2162.9	8.53	72.79758
Liberty Media	0	0	786.3	786.3	3.10	9.621009
Other	0	0	1052.5	1052.5	4 15	17.23806
Total	10327	6787	8236	25350	100.00	1535.018

524. *National Advertising Market* The Commission's focus is not on advertisers, but on the ability of broadcasters to compete for advertising revenues. Broadcast networks compete for advertising dollars by creating national audiences for their programming. If the networks cannot generate national audiences, their ability to compete for advertising revenues will decline, thereby diminishing their ability to invest in innovative programming As a result, viewers will experience a decrease in programming choices and quality.

525. In its 1984 decision, the Commission determined that elimination of the national cap would not harm competition in the national advertising market.[1097] The Commission found that the number of firms in the market would ensure continued vigorous competition in that market. In the *Notice*, we sought information on whether our conclusion in 1984 continues to be valid. To analyze competition in this market, we sought comment on the firms that compete in the national television advertising market, including the extent to which national spot advertisements and/or syndicated programming are fungible with network television advertising from the perspective of advertisers.[1098] The national television advertising market brings together those advertisers wishing to reach a national audience with television networks that provide national exposure. Broadcast television networks are the leading suppliers of national television advertising.

526. NAB/NASA claims the record demonstrates that national spot advertising is competitive

[1097] *1984 Multiple Ownership Report and Order*, 100 F C C.2d at 52 ¶102.

[1098] National spot advertising time is sold by stations to national advertisers, which aggregate national or regional coverage by purchasing advertising spots from stations in multiple markets. Syndication refers to advertisements sold in syndicated programs. *See* OPP Working Paper 37 at 11

with national advertising.[1099] National advertisers can purchase advertising on a collection of local television stations that can approximate a national advertisement on a single network. Local television stations sell national spot advertising through advertising agencies, which aggregate the available advertising on local stations for national spot buyers. NAB/NASA contends that when demand for national advertising on a particular network show exceeds the available supply of national network advertising time, advertisers turn to the national spot advertising market to reach viewers.[1100] Television stations rely in part on the national spot advertising market for a portion of their advertising revenue. NAB/NASA argues that if the ownership cap is raised, the broadcast networks will increase their ownership of television stations and decrease the national spot availabilities to such an extent that the viability of the national spot market will be impaired.[1101] Specifically, NAB/NASA contends that a network-owned station will not compete against its network for national (spot) advertising revenue. The result, according to NAB/NASA, is that competition in the national advertising market will be diminished by the decreased viability of national spot advertising as a substitute for network advertising. NAB/NASA asserts that the resulting loss of revenue to local stations will harm their ability to compete with other delivered video providers.[1102]

527. *Discussion.* We agree that a strong national spot advertisement market is an important component of the financial stability and competitiveness of television station owners. We find, however, that the increase in the cap from 25% to 35% has not harmed national spot advertising revenues. Our analysis of advertising revenue data indicates that despite increases in ownership of stations by CBS, NBC and Fox since 1996, there has been no diminution in the national spot advertising market that can be reliably associated with an increase in network station ownership. With the exception of 2001, national spot advertising has experienced a relatively consistent growth.[1103]

528. Although we agree with NAB/NASA that network-owned stations have less incentive to compete directly with an affiliated broadcast network in the national advertising markets, we cannot agree that such competition in fact would not occur. If national advertisers are willing to pay a higher per-spot price to network-owned stations than are local advertisers, network-owned stations might well accept the higher priced advertising Thus, the profit-maximizing behavior of the network-owned stations might well serve as a substitute for national advertisers seeking to purchase national spot advertising. Such a response by network-owned stations would maintain the viability of national spot

[1099] *See* B D. McCullough & Tracy Waldon, *The Substitutability of Network and National Spot Television Advertising*, 37 Q. J. BUS. & ECON 3 (Spring 1998) (*"Network Substitutability"*) (concluding that the estimated elasticities suggest that the network and national spot advertisements have been, and continue to be, good substitutes in the aggregate) *But see* Silk, Klein, and Berndt, *supra* note 519 at 323-48 (eight national media classes are not viewed as substitutes by national advertisers)

[1100] NAB/NASA Comments at 59

[1101] *Id* at 61-62.

[1102] *Id*

[1103] Since 1996, the broadcast networks have increased the number of owned and operated stations, yet the national spot advertising volume has risen from $9.1 billion in 1995 to $12.2 billion in 2000. From 1990-1994, the compound annual growth rate (CAGR) in the national spot advertising market was approximately 4.9% as compared to the CAGR for 1995-2000 of approximately 6.1% *See* OPP Working Paper 37 at 13. *See also* Richard Billotti, *The Case for Moderate Growth in TV Advertising*, EQUITY RESEARCH (Jan. 3, 2003).

advertising as an option for national advertising regardless of the level of the national television cap. Moreover, even if the top four networks were to acquire additional local stations and declined to use the national spot advertising availabilities to compete with their own network's advertising availabilities, there is every reason to think the network-owned stations would seek to take national advertising dollars away from *other* broadcast networks. That is, even if an NBC-owned station sought not to compete with the NBC network for advertising dollars, the NBC-owned stations have incentives to compete in the national spot market for advertising dollars that might otherwise go to the CBS, ABC, and Fox networks. Consequently, we cannot say that the national cap is necessary to protect competition in the national advertising market.

529. *Innovation.* In the *Notice*, we asked whether the national ownership cap promotes or hinders innovation in the media marketplace.[1104] Affiliates argue that non-network owners encourage innovation because affiliates provide a competitive outlet for innovative programming. NAB/NASA provides nine examples of innovation by non-network group owners, such as satellite newsgathering encouraged by affiliates to improve upon network-delivered news; the development of the local newsmagazine format; all-news cable channels developed for cable carriage; digital TV experiments such as the multicasting by several affiliates of the NCAA tournament; the delivery of local news in HDTV format; and the creation of iBlast, a joint venture between affiliates and an outside firm to develop new uses for digital spectrum.[1105]

530. Taking an opposing view, Fox contends that the cap limits networks' investment in innovative programming by "inhibiting economic efficiencies" that come with a larger number of owned and operated stations As evidence, Fox refers to a study by Michael Katz which concluded that, by inhibiting the potential economic efficiencies available to group owners, the rule artificially raises the cost of operating television stations and limits the return that group owners can realize on their programming investments.[1106] Katz argues that the rule drives group owners to direct more of their resources away from free television and toward alternative means of distributing programming content, such as subscription-based cable channels.[1107]

531. *Discussion.* The current national ownership cap appears to encourage innovation in broadcast television by preserving a number of separately-owned station groups, including non-network owned station groups. The current number of station group owners has led to innovation in ways that benefit the public. Those developments include the creation of local all-news channels in partnership with local cable companies, the implementation of program formats such as local newsmagazines, and, importantly, experimentation with the spectrum allocated to local broadcasters for digital television.[1108]

532. The transition to digital television represents a critical evolutionary step in broadcast television. We are committed to ensuring the rapid completion of that transition in a way that delivers the greatest possible benefits to the viewing public. We believe that the broadcast industry is more likely

[1104] *Notice*, 17 FCC Rcd at 18549-50 ¶ 146.

[1105] *See* NAB/NASA Reply Comments at 23-27

[1106] Fox Comments at 43; Katz, *supra* note 65

[1107] Katz, *supra* note 65 at 48-51

[1108] NAB/NASA Reply Comments at 57-58.

to rapidly address the technical and marketplace issues associated with digital television if there are a variety of group owners exploring ways to use the spectrum. The record shows that non-network owners of television stations are actively exploring different ways of using digital spectrum. It is also important to have group owners with potentially different economic incentives in this area examining transition mechanisms to digital television. Because of networks' ongoing investment in programming, it is possible that networks may have incentives to use digital spectrum differently from affiliates. The Fox television network, for instance, has indicated its interest in using the spectrum of its owned stations as well as its affiliates for future services.[1109] Therefore, we conclude that a national television cap is necessary to preserve a number of separately-owned television station groups, including non-network groups, that will increase the types of digital transition experiments and ultimately facilitate a rapid and efficient transition to digital broadcast television.

b. Diversity

533 The *1984 Multiple Ownership Report and Order* concluded that the local community is the relevant market for evaluating viewpoint diversity and that, therefore, the national TV ownership rule is not needed to promote viewpoint diversity.[1110] The *1984 Multiple Ownership Report and Order* also stated that the national market is not relevant for evaluating viewpoint diversity, but even if it were, the proliferation of media outlets renders the national ownership restrictions unnecessary.[1111] In the *1998 Biennial Review Report*, the Commission did not analyze the rule's effects on viewpoint diversity and merely stated, without evidentiary support, that the rule promotes diversity of programming.[1112] In remanding the national TV ownership rule, the court in *Fox Television* found that the Commission had failed to support its 1998 conclusion that the rule is necessary to strengthen affiliates' bargaining power and had neglected to address its 1984 determination that the national market is not the relevant geographic area to consider when evaluating diversity.[1113] We address the issue of affiliates' bargaining power in the following section and address diversity here.

534 In the *Notice*, we observed that the national TV ownership rule does not appear to be relevant to the goal of promoting viewpoint diversity because people gather news and information from sources available in their local market and that the relevant geographic market for viewpoint sources is local, not national.[1114] We also noted that the viewpoints aired by television stations in one city do not seem to have a meaningful impact on the viewpoints available in other cities.[1115] Commenters do not provide evidence that persuades us to alter those views, and we affirm our 1984 conclusion that the national TV ownership rule is not necessary to promote diversity.

[1109] NAB/NASA Comments at 42.

[1110] *1984 Multiple Ownership Report and Order*, 100 F C C.2d at 27 ¶¶ 31-32.

[1111] *Id* at 27-31 ¶¶ 33-43.

[1112] *1998 Biennial Review Report*, 15 FCC Rcd at 11075 ¶ 30

[1113] *Fox Television*, 280 F.3d at 1042-43.

[1114] *Notice*, 17 FCC Rcd at 18546 ¶136.

[1115] *Id*

535. *Discussion* We conclude that the national television cap is not necessary to promote viewpoint diversity. Americans use media outlets available in their local communities as sources of information. The national television cap, by contrast, ensures a larger total number of station owners *nationwide,* but it has no meaningful impact on viewpoint diversity within local markets.[1116] Therefore, we affirm our 1984 decision that the national television ownership limit is not necessary to promote viewpoint diversity.[1117] We also affirm our decision that the market for viewpoint diversity is local, not national. And we reiterate our 1984 statement that even if the national market were the relevant area to consider, the proliferation of media outlets nationwide renders the current rule unnecessary.[1118]

536. Although proponents of the current rule assert that the increased uniformity imposed by the networks' national distribution agenda limits the number of viewpoints available to the public,[1119] we do not find convincing evidence in the record indicating that raising the current national TV ownership limit would harm viewpoint diversity. Professors Schwartz and Vincent assert that maintaining a diversity of ownership across local markets is beneficial because viewers may become aware of investigative news stories presented by stations in other markets, particularly those of strong stations.[1120] NAB/NASA argues that "this type of cross-fertilization is less likely to occur in the absence of the national TV ownership rule."[1121] For this cross-fertilization to be a plausible scenario, the following minimum conditions must occur· (1) the national cap prevents a station from being acquired by a broadcast network; (2) the non-acquired station produces content that by some measure is meaningfully different (and significant from a viewpoint perspective) from what the network-owned station would have aired; and (3) the airing of that different content becomes known to consumers in other localities. The national cap cannot be justified by reference to such a hypothetical scenario as this.

[1116] It is possible, of course, that the replacement of one station owner by another could in fact reduce the number of independently-owned television stations in that market. If the acquiring firm already owned one station in that market and the seller was selling its only station in that market, there would be one less independently-owned station in that market The impact of such a transaction on viewpoint diversity would be accounted for under the diversity component of our local rules.

[1117] *See* Fox Comments at 34-35. We are not persuaded by claims to the contrary *See* UCC Comments at 49-50, 53-54; Cox Comments at 65; IPI Comments at 63, AFTRA Comments at ¶ 123; CCC Comments at 22.

[1118] *1984 Multiple Ownership Report and Order*, 100 F.C C 2d at 25, 27 ¶¶ 24, 33 *See also* Modern Media Marketplace, *supra* Section IV; Fox Comments at 10-26, Paxson Comments at 9-11, Letter from John C. Quale, Counsel for Fox, to Marlene Dortch, Secretary, FCC (May 2, 2003) ("Fox May 2, 2003 Ex Parte"), Attachment A at 18. *But see* Cox Reply Comments at 18-22 (growth of other media outlets does not negate the need for the 35% cap)

[1119] NAB/NASA Comments at 12; NAB/NASA Reply Comments at 6; Cox Comments at 26-31.

[1120] NAB/NASA Comments, Attachment 1, Marius Schwartz & Daniel R Vincent, *The Television National Ownership Cap and Localism* ("NAB/NASA Comments, Schwartz/Vincent Paper") at 12-13. *See also* NAB/NASA Comments at 12, 69-70, Cox Reply Comments at 12-13

[1121] NAB/NASA Comments at 69

537. Commenters discussing types of diversity other than viewpoint diversity do not provide an evidentiary basis for retaining the current cap.[1122] The *1998 Biennial Review Report* stated that "[i]ndependent ownership of stations also increases the diversity of programming by providing an outlet for non-network programming."[1123] In this *Report and Order*, however, we have concluded that we can and should rely on the marketplace, rather than regulation, to foster program diversity.[1124] Further, the record in this proceeding does not contain evidence that affiliates air programming that is more diverse than programming aired by network-owned stations. Therefore, we cannot affirm our earlier determination regarding program diversity, and we do not find that the cap is necessary to foster program diversity.

c. Localism

538. *Introduction* The Commission's decision in the *1984 Multiple Ownership Report and Order* did not address whether the national TV ownership rule advances its goal of localism.[1125] In the *1998 Biennial Review Report*, however, the Commission did address its localism goal, declining to modify the national TV ownership restriction in part because affiliates "play a valuable counterbalancing role" to network programming decisions by exercising their independent programming discretion regarding what programs best serve the needs and interests of their local communities.[1126] In *Fox Television,* the court stated that, although the Commission had failed to present evidence that the cap in fact promoted localism, localism was a legitimate basis for imposing a national ownership cap.[1127]

539. Based on our analysis of the extensive record in this proceeding, we conclude that a national television ownership limit is necessary to promote localism on broadcast television. The evidence suggests, however, that the current 35% cap is not needed the protect localism, and may in fact be hindering public benefits that are expected to follow from an increase in the cap. We conclude that a national cap of 45% fairly balances the competing public interest values affected by this rule. We recognize that our decision to retain a national ownership cap is contrary to our conclusion in 1984. We reach this different conclusion principally because we find that a cap is necessary to protect localism by preserving a balance of power between networks and affiliates, a policy objective that was not considered in the 1984 decision. In this section, we detail the localism analysis. Thereafter, we discuss our modified rule.

[1122] Cox briefly discusses program, source and outlet diversity, but it does not provide evidentiary support for its arguments Cox Comments at 65-66. CPD fails to explain how repealing the 35% cap would diminish program and source diversity in prime time programming. *See* CPD Comments at 3-6

[1123] *1998 Biennial Review Report*, 15 FCC Rcd at 11075 ¶ 30

[1124] *See* Policy Goals, *supra* Section III

[1125] *See 1984 Multiple Ownership Report and Order*

[1126] *1998 Biennial Review Report*, 15 FCC Rcd at 11074-75 ¶ 30.

[1127] "[T]he public interest has historically embraced diversity (as well as localism) . . . and nothing in § 202(h) signals a departure from that historic scope." *Fox Television,* 280 F 3d at 1042.

(i) Whether a National Cap Promotes Localism

540. In this section we examine the effect of a national television cap on the economic incentives for locally responsive programming by television stations. We also consider evidence that a national cap results in behavior by network-affiliated stations that is responsive to the needs and tastes of a station's local community.[1128]

(a) Economic Incentives for Localism

541. NAB/NASA contends that the current national cap is needed to preserve affiliates' bargaining power with their networks.[1129] NAB/NASA explains that limiting the national audience that networks can reach through their owned stations promotes a balance of power between networks and their affiliates. NAB/NASA also claims that the cap is necessary to counteract the networks' strong financial incentive to promote the widest distribution across the nation of network programming irrespective of the tastes of one or more particular local cities. The widest possible distribution of programming, according to NAB/NASA, increases viewership of network programming, which maximizes network advertising revenues. According to NAB/NASA, maximum national exposure of programming also improves the likelihood that the program owner will realize additional revenues in the program syndication market. NAB/NASA contends that as broadcast networks have ownership stakes in a larger percentage of their prime time programming, their incentive to create programs with syndication value -- and their incentive to stifle local preemption -- increases.[1130]

542. NAB/NASA argues that the incentive of independently-owned affiliates, in contrast to network-owned stations, is to make programming decisions that are more closely aligned with the needs and tastes of their communities of license.[1131] A network derives its income from the programming that the network produces (and the syndication revenue the programs might generate) as well as from its local stations A local station maximizes its income by providing programming desired by its local community irrespective of national programming preferences. Therefore, the programming interests are not always the same.

(b) Evidence of Localism by Affiliates

543. NAB/NASA contends that the national cap is needed to preserve a body of network affiliates not owned by the network that can influence network programming so that it is more suited to

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[1128] Cox argues that allowing networks to significantly expand their station ownership will increase the networks' ability to pressure cable operators, and erode the cable operators' bargaining position, during retransmission consent negotiations Cox Comments at 41-47, Letter from Alexander V Netchvolodoff, Senior Vice President of Public Policy, Cox Enterprises, Inc., to Marlene H Dortch, Secretary, FCC (Feb. 3, 2003) at 1-2. *See also* American Cable Association Petition for Inquiry into Retransmission Consent Practices (filed Oct. 1, 2002); Children Now Comments at 13-15 Fox responds that the negotiations are not affected by the number of stations owned by a network, but by each party's market-by-market evaluation of whether the agreement is beneficial. Letter from John C. Quale, Counsel for Fox, to Marlene H. Dortch, Secretary, FCC (April 21, 2003) ("Fox April 21, 2003 Ex Parte") at 2. Cox's arguments are outside the scope of our biennial review.

[1129] NAB/NASA Comments at 9

[1130] *Id.* at 33

[1131] *Id* at 10.

the tastes and needs of the affiliates' communities.[1132] In support of this argument, NAB/NASA submitted several examples of the influence independent affiliates can have on network programming:

- When NBC aired a special edition of *Fear Factor*, featuring Playboy bunnies, during halftime of the Superbowl (airing on Fox), affiliates objected to the network promos, which ran during all hours of the day, and included tag lines such as "who needs football when we've got bunnies?"

- NAB/NASA states that when NBC began a trial program to accept liquor advertisements, so many affiliates opted out of airing the ads due to local concerns that NBC dropped the program.

- CBS had scheduled the *Victoria's Secret Fashion Show* for 8 p.m. The affiliates objected to the early showing and urged that the program be moved to the 10 p.m. time slot. In response, CBS moved the show to 9 P.M., although some affiliates nonetheless preempted the show as having inappropriate content for their service areas.

- Promotional ads for NBC's *Dog Eat Dog* included shots of nude contestants promoting the program's challenges such as "strip football" and "strip golf." When affiliates objected to the explicitness of the promos and their airing at all times of day, NBC agreed to eliminate strip stunts from future episodes.

- *NYPD Blue* was originally designed to include more nudity and graphic language than is currently aired, but after ABC affiliates objected, the amount of nudity and graphic language in the show was reduced. Even so, a number of affiliates initially refused to carry the show.

- Affiliates expressed concerns about the violent and mature content of the series *Kingpin,* which concerns the life of a drug lord. In response, NBC agreed to allow affiliates to review episodes in advance to ensure the content is appropriate for their local communities.

- In 2002, CBS worked with affiliates to reformat its morning news program, *The Early Show.* One key issue of affiliate concern was whether they would be permitted to provide local news content during the two-hour time block used by the program, as they had with CBS' prior show, *CBS This Morning.* Although some local affiliates are permitted to use the blended format with *The Early Show,* CBS has refused to permit other affiliates to move to the blended local-network news program format.[1133]

- NBC affiliates objected to NBC's intention to broadcast the 2002 Olympic Games live, which would have preempted the evening news on the west coast. After initially resisting the requests of the west coast affiliates to air a delayed broadcast during prime time, the network conducted a viewer survey. Results of the survey, however, substantiated the affiliates' assertion that west coast viewers preferred to watch the games during prime time, and the networks complied.[1134]

[1132] *Id.* at 27

[1133] *Id* at 25-26, 29-30

[1134] *Id* at 30-31.

- NBC affiliates initially objected to NBC's decision to require live broadcasting of the XFL games. On the west coast, games substantially preempted both the affiliates' early evening local news and the national network news. In other parts of the country, overruns of the game preempted the late night local news. When affiliates raised similar concerns about Arena Football, claiming that overruns would preempt the 6 p.m. local newscasts on the east coast, the network agreed to work with the sports league to ensure the games do not run over.[1135]

- KYTV in Springfield, Missouri, preempted a January 6, 2003 episode of NBC's *Fear Factor,* which airs at 7 p.m. Central Time, that involved contestants eating horse rectums because it found the material inappropriate for its community.[1136]

544. Separate from this "collective negotiation" type of localism, parties also submitted evidence regarding the frequency of station-by-station preemptions for affiliates versus network-owned stations [1137] Preemptions are instances in which local stations, whether they are owned and operated by networks or independently owned but affiliated with these networks, choose to air a program other than the program the network distributes to the station. The networks submitted data comparing prime time preemption rates of network-owned stations versus affiliates for 2001. That data showed that affiliates preempted an average of 9.5 hours of prime time programming per year compared with 6.8 hours per year for network-owned stations.[1138] The networks claim that this difference is inconsequential and does not

[1135] *Id.* at 30

[1136] NAB/NASA Reply Comments at 16-17

[1137] Affiliates described numerous examples of individual station preemptions of network programming. Some of these examples follow. WRAZ-TV in Raleigh, North Carolina, chose to stop airing *Temptation Island* after Fox revealed that one of the participating couples had a child because "WRAZ will not support a program that could potentially break up the parents of a young child." *Id* at 17 WFAA-TV in Dallas did not carry the entire first season of *NYPD Blue* because it found the material and language inappropriate for programming scheduled to air at 9 p m in that community. *Id* KNDX in Bismarck, N.D., refused to clear the Fox network's broadcast of the movie *Scream,* which is targeted to young viewers, because of its graphic and disturbing portrayal of teenage murders. *Id.* WFAA-TV, an ABC affiliate in Dallas, was denied permission to preempt *Monday Night Football's* half-time show on November 12, 2001 to cover an American Airlines plane crash. American Airlines is based in Dallas. According to NAB/NASA, ABC permitted two O&Os to preempt the same half-time show to air news covering the same crash. *Id* at 37-38. CBS did not permit WTSP-TV in Tampa Bay to air a debate between Jeb Bush and Bill McBride during the Florida gubernatorial debate because the affiliate would have preempted the season premiere of *48 Hours.* WTSP-TV was a cosponsor of the debate. *Id* at 38. A Raleigh North Carolina Fox affiliate refused to air *Who Wants to Marry a Multimillionaire?* because it "felt it was demeaning to women and made a mockery of the institution of marriage." *Id* at 38-39 WANE-TV, the Fort Wayne, Indiana CBS affiliate, sought to preempt network programming to air a half-hour, early morning local news program geared toward the agricultural community. Although this was initially denied, CBS ultimately relented and granted permission *Id* at 39. In this *Report and Order*, we use the terms "network-owned" stations and "O&O" (*i e* owned and operated) stations interchangeably.

[1138] Fox Comments, Economic Study G provides data showing. (1) both O&Os and affiliates preempt less than one percent of prime-time programming (in 2001); (2) the four networks' 57 O&O stations preempted an average of 6 8 hours per year per station compared to an average of 9.5 hours per year per station for 651 non-owned affiliates; and (3) on average, O&O stations preempt roughly the same amount of programming – 0.8 hours per station per year – as affiliates for news, political and public affairs programming. Fox Comments, Economic Study G.

justify retention of a national ownership cap.[1139] Affiliates assert that even this hand-picked data by networks confirms that affiliates preempt more than network-owned stations and that a national cap is needed to protect localism.[1140]

545. Affiliates seek to explain low preemption rates by arguing that networks have increasingly restricted preemption through their network-affiliate contracts. Cox argues that the networks have been exacting greater concessions from their affiliates, including demands to decrease the number of preemptions.[1141] Affiliates complain that they are subject to preemption caps involving financial penalties or loss of affiliation if they exceed the number of network-authorized preemptions,[1142] while affiliates' local programs are often "preempted" by network overruns (*e.g.*, network sports overrunning local news).[1143] For example, Cox submits information gathered from its television stations in which the stations document their conflicts with the networks over network programming and local tastes and station preemptions.[1144] According to NAB/NASA, Fox allows only two preemptions per year, and NBC allows only five hours of prime-time preemptions per year. Affiliates that exceed their allowable preemption "basket" may be subject to financial penalties or even loss of affiliation.[1145] Thus, while a majority of affiliates did not exceed their permitted preemptions,[1146] affiliates argue that there are good reasons for that result. In addition, affiliates note that they often maintain a "cushion" of unused preemption time in case it is needed, requiring them to exercise discretion in "spending" their preemption time during the year to avoid contractual financial penalties associated with excessive preemption.[1147]

546. *Discussion.* We find that a national television ownership cap is necessary to promote localism. The evidence before us demonstrates both that network affiliates have economic incentives more oriented towards localism than do network-owned stations, and that affiliates act on those incentives in ways that result in networks delivering programming more responsive to their local communities (in the judgment of the affiliate) than they otherwise would. In order for affiliates to continue to serve local community tastes and needs in this way, a national cap is needed to preserve a

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[1139] *Id*

[1140] NAB/NASA Reply Comments at 32-35.

[1141] Cox Comments at 34-38.

[1142] NAB/NASA Comments at 39-43.

[1143] Cox Comments at 34-41; NAB/NASA Comments at 43-45.

[1144] Cox Comments at Appendix C-1

[1145] NAB/NASA Comments at 39-41. NASA filed a Petition for Inquiry into Network Practices on March 8, 2001, and a Motion for Declaratory Ruling on June 22, 2001. NASA claims, among other things, that contractual language contained in network affiliation agreements violates the "letter and spirit" of Section 310(d) of the Communications Act of 1934, the right to reject rule and the time option rule (47 C.F R. § 73.658(d) & (e)). We are addressing the merits of this petition separately from this proceeding.

[1146] Disney Comments at 4-7. Disney Exhibit G presents the number of available and used preemptions for ABC affiliates based on negotiated baskets of preemptions. According to Disney, during all of 2001, affiliates used only 56% of the permissible preemptions available to them and out of 189 affiliates, 150 did not exceed their baskets.

[1147] NAB/NASA Reply Comments at 36-37.

body of independently-owned affiliates. The two ways in which affiliates can promote localism are by collective negotiation to influence the programming that the networks provide and by preemption by an individual station owner to provide programming better suited to its community.

547. The record shows that network-owned stations and affiliates have different economic incentives regarding the programming aired by local stations. We agree with NAB/NASA's study by Schwartz and Vincent that affiliates have an economic incentive to target their local audience by offering programs suited to local tastes.[1148] In so doing, affiliates have an incentive to tailor their programming schedule to meet local preferences.[1149] Localism is fostered by the affiliates' efforts to promote their own economic interest of maximizing the value of their stations by offering programming that local viewers will prefer to watch, even if the programming replaces the network's nationally scheduled programming.

548. The 2001 preemption data comparing network and affiliate preemption rates also supports retention of a national cap. The record shows that in 2001, affiliates preempted 9.5 hours per year of prime time programming versus 6.8 hours per year for network-owned stations. This data bolsters our conclusion that affiliates act on their economic incentives to preempt network programming with measurably greater frequency than do network-owned stations. Although we agree with the networks that the total number of hours preempted by both types of station owners in this comparison is relatively small, these data are for the prime time viewing period, when the vast majority of television viewing occurs. In our view, the practical effect of prime time preemption is far greater than that of preemption during other dayparts.

549. We cannot agree with Fox that network-owned stations provide the same localism value that independently-owned affiliates do. Fox argues that networks listen to the management of network-owned stations as well as to the management of affiliates. It claims that managers of O&Os participate during the networks' program development process and provide more credible input than the management of affiliate stations.[1150] Fox also asserts that affiliates have an "inherent economic conflict" with the network regarding the distribution of profits, have no influence in the development of new programs, and learn of the new programs at the same time as do advertisers.[1151]

550 We agree with Fox that affiliates have an inherent economic conflict with networks. However, we believe that affiliates' economic incentives actually help explain why affiliates regularly raise programming concerns with networks and why affiliates preempt more network programming, on average, than do network-owned stations. In our view, affiliates' economic incentives to maximize local viewership works to promote localism

551 In addition, Fox's claim of minimal affiliate influence over programming is overcome by the significant evidence submitted by NAB/NASA that affiliates regularly raise programming concerns with networks and frequently succeed in altering network programming in ways that protect local interests. These numerous instances of the collective influence brought to bear by affiliates on network programming decisions represents a powerful force for the protection of local viewing interests. They

[1148] NAB/NASA Comments, Schwartz/Vincent Paper.

[1149] Cox Comments at 47-52, 60-62.

[1150] Fox April 21, 2003 Ex Parte at 2.

[1151] *Id*

represent empirical evidence that affiliates collectively serve as an important counterweight to network programming decisions by influencing networks to deliver programming responsive to local tastes.

552. In sum, we believe that this affiliate/network dynamic is beneficial to viewers and should be preserved. We conclude that eliminating the cap altogether would shift the balance of power with respect to programming decisions toward the national broadcast networks in a way that would disserve our localism policy [1152]

(ii) Appropriate Level of the Cap

553. In the preceding section, we found that a national television ownership cap continues to be necessary to promote localism because the record demonstrates that affiliates affect network programming in ways that respond to viewer preferences in affiliates' local communities. In this section, we examine the specific effects of the current 35% cap and whether this particular level achieves our localism objectives.

554 *Preemptions.* Affiliates argue that the networks have limited their ability to preempt network programming in order to provide programming more geared to local needs and interests, and that these limits have become more formidable as the networks have extended their ownership of stations.[1153] Affiliates argue that an increase in the national cap reduces affiliates' ability to resist network pressure not to preempt. The affiliates point to a decline in affiliate preemptions following the 1996 increase in the cap from 25% to 35%. The affiliates' submission indicates that, with respect to all dayparts (as opposed to prime time-only), affiliates preempted, on average, 48 hours per year between 1991 to 1995 and 36 hours per year between 1996 to 2001.[1154] It also shows that, in the year 1995, the year before the cap was increased to 35%, there were, on average, 46 hours of programming preempted, but by the year 2001 the average had declined to 33 hours.

555. The networks offer two responses to the affiliates' data. First, the networks submit preemption data that, according to the networks, shows that the 35% cap has no effect on bargaining power between networks and affiliates. The networks contend that if higher levels of network station ownership actually increased networks' leverage over their affiliates, we would expect affiliates of the largest network station owners to preempt less (because of their diminished bargaining power) than affiliates of a network that had significantly less station ownership. The networks data shows that affiliates of the largest network-owners (CBS and Fox, at 39% and 38% national reach respectively) preempt to an equal or greater extent than do affiliates of ABC, with a national reach of 23%.[1155] The

[1152] Our concerns are substantiated by statements from consumer groups asserting that large companies are less responsive to consumer complaints *See* Catherine Yang, *The FCC's Loner is No Longer So Lonely,* BUS. WK, (Mar. 24, 2003) at 78.

[1153] NAB/NASA Comments at 31.

[1154] *Id* at 16.

[1155] Fox April 21, 2003 Ex Parte at 8-9.

networks assert that this data proves that the 35% cap has no effect on bargaining leverage between networks and affiliates [1156]

556. Second, the networks argue that affiliate preemptions often are not for programming that is of greater public interest, but for syndicated programs.[1157] The data Disney submits suggests that more affiliates preempted ABC programming in favor of syndicated programming than for local specials.[1158] In addition, Disney states that very few half hours of affiliate prime-time preemptions were for news, political, or public affairs programming.[1159] Disney's data, however, is countered by a NAB/NASA survey of affiliated stations, in which respondents reported preempting network programming for: local breaking news (83% of respondents); local news (71% of respondents); local emergencies (70% of respondents); local political programming (74% of respondents); local sports (75% of respondents); religious programming (47% of respondents); "other" programming (*e.g.*, parades, telethons, syndicated programming, movies) (34% of respondents).[1160]

557. Apart from contractual restrictions, a majority of affiliates responding to a NAB/NASA survey -- 68% -- report that they have "experienced pressure from [their] network to not preempt programming."[1161] UCC provides several instances of increased network resistance when affiliates attempted to air programs deemed to be of greater local interest than the network programming. For example, it cites to the experience of Belo's ABC affiliate in Dallas, the headquarters of American Airlines, which failed to get the network's permission to preempt the November 12, 2001, Monday Night

[1156] *Id* In a motion filed May 28, 2003, NAB/NASA asked the Commission to disregard certain portions of network submissions concerning preemption and local news quantity because the networks have not provided the data underlying those submissions. Alternatively, NAB/NASA asked the Commission to infer that the underlying data would not favor the networks' positions on preemption and news quantity of O&O versus affiliate stations. The portions of the network filings the Commission is asked to disregard include, *inter alia*, EI Study G and Disney Exhibit G, relating to preemptions, and EI Study H, relating to local news quantity. Fox opposed the motion on May 29, 2003. We will afford the record evidence the appropriate weight in light of all circumstances, including the extent to which we believe the underlying data is necessary to make an informed decision about the showing.

[1157] Disney Comments at Exhibit H shows, among other things, that during the first quarter of 2002, affiliates preempted ABC programming more for syndicated programming than for local specials.

[1158] Disney Comments at 4-7 Disney Exhibit J shows, among other things, that during the first quarter of 2002, affiliates preempted ABC programming more for syndicated programming (201 half-hours) than for local specials (188 half-hours).

[1159] *Id.* The remaining prime-time preemptions were for sports, telethons, syndicated and local entertainment, paid programming, and paid religious specials. Disney Exhibit J shows that, for all of 2001, of 3,694 half-hours of primetime preemptions, 291 were for news, political, or public affairs programming; 574 half-hours were for telethons; 864 half-hours were for entertainment; 105 were for news; 171 were for public affairs; and 1,561 were for sports related shows.

[1160] NAB/NASA Comments at 17-18, Table 2, Attachment 2.

[1161] *Id* at 17. NAB/NASA sent the survey to 422 ABC, CBS, and NBC affiliated stations asking them to report on their experience with networks regarding preemption It reports receiving 201 "usable" responses.

Football halftime show for local news updates on the American Airlines jet crash in New York that morning.[1162]

558. *Discussion.* Although we concluded in the prior section that a national cap is needed to balance power between networks and affiliates, the record suggests that maintaining the cap at 35% is not necessary to preserve the balance of bargaining power between networks and affiliates. In reaching this conclusion, we rely principally on the evidence showing that the largest network station owners possess no greater bargaining power – as measured by prime time preemptions – than the smallest network station owner. We find this evidence persuasive because it directly compares the extent to which different levels of network ownership of stations actually affect the level of preemption by those networks' affiliates. Implicit in this analysis is an assumption that that data, although not a perfect proxy, is a reliable indicator of relative bargaining power between networks and affiliates. Preemption of network programming by an affiliate has negative consequences to the network, and networks by all accounts seek to avoid preemption by affiliates.[1163] So the ability of an affiliate to preempt in the face of networks' incentives to *prevent* preemption appears to be a reasonable measure of relative bargaining power between networks and affiliates.

559. We are not persuaded by the affiliates' argument that the 35% cap is needed to protect localism because the most recent national cap increase resulted in fewer affiliate preemptions. The principal deficiency in this argument is that it does not control for other plausible causes of the decline in affiliate preemptions. Although NAB/NASA suggests that the 1996 increase in the national cap reduced affiliates' bargaining power, NAB/NASA itself identifies other factors occurring in the same timeframe as the national cap increase that it claims have further eroded affiliate bargaining power. NAB/NASA asserts that the Commission's repeal of its financial interest and syndication rules in the early 1990s gave networks an additional financial incentive (in addition to their incentive to avoid preemption to maximize advertising rates) to discourage affiliate preemption. NAB/NASA contends that vertical integration, including program ownership and syndication by broadcast networks and the trend toward "repurposing" of network programming on affiliated non-broadcast channels have helped increase the networks' leverage over affiliates.[1164] To the extent these additional factors actually enhance network bargaining leverage as NAB/NASA contends, they undercut NAB/NASA's argument that it was specifically the 1996 increase in the national cap that caused affiliates to reduce their preemption of network programming

560. A more accurate assessment of the impact of the 1996 national cap increase on network-affiliate bargaining leverage could be made if affiliate preemption rates from 1991 through 2001 could be compared to the preemption rates of network-owned stations during that same period. If preemption rates on network-owned stations were similar to affiliate preemption rates over that same period, we

[1162] UCC Comments at 51-52 (citing Michele Greppi, *The Insider A(BC's) Tale of Too-Different Cities,* ELECTRONIC MEDIA (Nov. 19, 2001) at 8). Among its other examples, CBS pressured a Florida affiliate into running the season premier of "48 Hours" instead of the state's gubernatorial debate UCC Comments at 52 (citing Wes Allison, *Local PBS Affiliate Will Air Debate,* ST. PETERSBURG TIMES (Sept. 25, 2002) at 1B.). Also, NBC resisted attempts by affiliates to preempt a baseball game to air a presidential debate during the 2000 campaign. UCC Comments at 52 (citing Neil Hickey, *Unshackling Big Media,* COL. J. REV (July/Aug 2001) at 30).

[1163] *See, e g*, NAB/NASA Comments at 17 (stating that 68% of affiliates responding to a survey claimed that they have "experienced pressure from [their] network not to preempt programming").

[1164] *Id* at 31-39

might have a more certain -- and completely different -- explanation for the decline. Networks might well have persuaded us that the uniform decline in preemptions by O&Os and affiliates was caused by some plausible reason unrelated to the change in the national cap. On the other hand, if the data had shown preemption rates on network-owned stations remaining steady while affiliate preemptions declined sharply after 1996, then the affiliates' explanation for the decline (*i.e.* increase in the national cap) would carry more weight than we give it here.

561. The foregoing analysis of preemption data excludes consideration of the content of the programming substituted by the local station for the network programming. Other than our interest in promoting market structures that encourage local news production, we seek to avoid resting broadcast ownership policies on subjective judgments about the public policy value of different types of locally-substituted programming. We agree with NAB/NASA that it is enough, for purposes of assessing stations' responsiveness to local communities, that they preempted network programming. The judgment of when to preempt and what to substitute are uniquely within the judgment -- and responsibility -- of the station.

562 Thus, we reaffirm our conclusion, in the *1998 Biennial Review Report*, that independently-owned affiliates play a valuable role by "counterbalancing" the networks' economic incentive to broadcast their own programming "because they have the right . . . to air instead" programming more responsive to local concerns.[1165] But, the evidence suggests that the current limit of 35% is overly restrictive and that the cap may safely be raised and the benefits of wider network station ownership achieved (discussed below) without disturbing either this balance or affiliates' ability to preempt network programming

(iii) Other Effects of the Current 35% Cap

563 In the preceding sections, we examined two measures of localism -- collective affiliate influence on network programming and specific preemption levels by affiliates versus network-owned stations. In this section we consider a third measure -- the effect of the national cap on the quantity and quality of local news and public affairs programming. We examine this area because local news and public affairs programming can play an important role in citizen participation in local and state government affairs. Thus we seek market structures among broadcasters that encourage stations to produce local news and public affairs programming and thereby contribute to an informed citizenry.

564. In its 1984 decision, the Commission compared the quality and diversity of programming by stations owned by group owners – both network and non-network owners – with that of singly owned stations. It concluded that there was no evidence that group owners provided less or lower quality news and public affairs programming than single owners.[1166] The *Fox* court criticized the Commission for failing to explain in the *1998 Biennial Review Report* why it departed from this conclusion. With the decline in the number of individually owned stations, an increase has occurred in the number of stations sharing common ownership. The Commission sought in this biennial review to understand whether the national TV ownership rule, by preserving a class of affiliates, affects localism by comparing the local

[1165] *1998 Biennial Review Report*, 15 FCC Rcd at 11075 ¶ 30. In its remand, the *Fox Television* court did not dispute the Commission's view in the 1998 decision, but said the Commission failed to show whether it had received evidence substantiating its 1998 conclusion or repudiating its 1984 conclusion. *Fox Television*, 280 F.3d at 1043

[1166] *1984 Multiple Ownership Report and Order*, 100 F.C C 2d at 32-34 ¶¶ 44-51.

news and public affairs programming of network owned and operated stations to that of non-network owned affiliates. We discuss the evidence and our conclusions below.

565 *Quantity of local news and public affairs programming.* In the *Notice,* the Commission requested evidence regarding any clear relationship between the ownership of stations and the quantity and quality of local news and public affairs produced by those stations.[1167] A study conducted by Commission staff concluded that network-owned stations produced more local news and public affairs programming than affiliates and received local news excellence awards more frequently than affiliates.[1168] Responding to that study, NAB/NASA submitted a study indicating that many of the results of MOWG Study No. 7 changed when data pertaining to stations belonging to Fox were not used.[1169] The final study, submitted by Dr. Michael Baumann of Economists Inc., demonstrates that no defensible reason exists for deleting the Fox station data.[1170] This final, comprehensive study provides analysis purporting to demonstrate that network-owned stations, on average, produce more local news than do affiliates across all-sized markets, with an even greater difference in the amount of news offered by network-owned stations in smaller markets.[1171]

566. The results of MOWG Study No. 7 show that network-owned stations air 23% more local news and public affairs programming per week than affiliates (22 8 hours versus 18.5 hours).[1172] In response to MOWG Study No. 7, NAB/NASA conducted a study that revealed no statistically significant difference between hours of local news aired by affiliates and O&O stations.[1173] Unlike MOWG Study No. 7, the NAB/NASA study included data on ABC, NBC and CBS, but did not include data on Fox Television.[1174] Disney argues that there is no policy-based rationale for excluding Fox stations.[1175] Using the NAB/NASA data, but accounting for all four of the networks, Dr. Baumann determined that network-

[1167] *Notice,* 17 FCC Rcd at 18550 ¶ 148.

[1168] MOWG Study No. 7 at 3-6.

[1169] NAB/NASA Early Submission (Dec 9, 2002).

[1170] Letter from Susan L Fox, Vice President, Government Relations, Disney, to Marlene Dortch, Secretary, FCC (Feb 13, 2003) ("Disney Feb. 13, 2003 Ex Parte"). In response to a criticism of MOWG Study No. 7, which could also apply to Fox Economic Study H, Economists Inc conducted a slightly modified analysis filed as part of "Economic Comments on Media Ownership Issues"), which was attached as an exhibit to the Fox Reply. *See also* Fox Comments, Economic Study H.

[1171] Disney Feb 13, 2003 Ex Parte at Attachment.

[1172] Only MOWG Study No. 7 examined newspaper-owned affiliates separately from the other affiliates. It showed that, on average, newspaper-owned affiliates provided more hours per week of local news and public affairs (about 22 hours) than did the other affiliates (approximately 15 hours) The study also showed that network O&Os provided the most local news of all (almost 23 hours).

[1173] NAB/NASA Early Submission (Dec. 9, 2002).

[1174] *Id* On May 5, 2003, NAB/NASA submitted another letter reiterating its argument. The submission, however, provided no new data or additional information *See* Letter from Alan Frank, Chair, NASA, to Michael K. Powell, Chairman, FCC (May 5, 2003) ("NASA May 5, 2003 Ex Parte")

[1175] Disney Feb 13, 2003 Ex Parte, Attachment at 7, n 6

owned stations on average provide more local news -- about 4.2 hours per week -- than do affiliates in all markets. In markets outside the top 25 markets, network-owned stations provide almost eight more hours of local news each week than affiliates do. Inside the top 25 markets, Disney agrees with the NAB/NASA study results that the difference between network-owned stations and affiliates was not statistically significant.[1176]

567. In Dr. Baumann's study, a third data set was used in analyzing local news and public affairs programming on network-owned and affiliate stations.[1177] Results, however, were similar to the first two studies: network-owned stations produce about 6.4 more hours per week of local news than affiliates in all markets tested. As with the modified NAB/NASA data, in markets outside the top 25 markets, network-owned stations provide about 9 hours additional local news each week. This study agrees with the NAB/NASA results that the difference between network-owned stations and affiliate stations in news provided was not statistically significant in markets inside the top 25 markets.[1178]

568. *Local News Quality* Although the Commission does not regulate programming quality, it has attempted to strengthen the ability of local stations to serve their communities through news and public affairs programming. In the *Notice*, we sought to understand whether the national TV ownership rule may have the effect of increasing or decreasing the quantity and/or quality of local news and public affairs programming.[1179] Studies discussing programming quality were submitted in the record.

569. MOWG Study No. 7, for example, finds that network O&O stations win more awards for local news programming than non-O&O affiliates. In evaluating the quality of local news programming, the authors used three measures: (1) ratings received for local evening news; (2) awards from the Radio and Television News Directors Association (RTNDA); and (3) the local television recipients of the Silver Baton of the A I. Dupont Awards. The ratings of network-owned stations and affiliates were virtually identical during the period tested. However, with respect to the receipt of RTNDA awards for news excellence, network-owned stations received those awards at a rate of 126% of the national average and affiliates received them at 96% of the national average. The study found, with respect to the DuPont awards, network-owned stations received awards at 337% of the national average, while affiliates received awards at 77% of the national average.

570. The results of a second study, however, indicate that quality differences between network-owned stations and affiliates are virtually nonexistent. In comparing the record of network-owned stations and affiliates' news operations, a study by Economists Inc. on behalf of the networks focused on the RTNDA awards, one of the awards used in MOWG Study No. 7.[1180] It reasoned that, because a larger number of RTNDA awards are given out each year, they are more likely to offer a better measure of news quality than the DuPont awards. The study examined the RTNDA awards from two

[1176] *Id* at 8-9; NAB/NASA Early Submission (Dec. 9, 2002).

[1177] The measure of weekly minutes of local news, public and current affairs programming was provided by TV Guide for a week in May 2002. The set of explanatory variables includes market rank, whether a station was an O&O or not, and other market characteristics Disney Feb. 13, 2003 Ex Parte, Attachment at 10.

[1178] *Id* at 12, NAB/NASA Early Submission (Dec 9, 2002)

[1179] *Notice*, 17 FCC Rcd at 18550 ¶ 148

[1180] Response of Fox to NAB/NASA Early Submission (Dec 19, 2002) at 5 and App 1

perspectives, first analyzing the awards bestowed in the top 10 markets, and then the top 50 markets. The study concludes that, in either setting, "there is no discernible difference between network-owned stations and affiliates with respect to RTNDA awards."[1181] Neither this study nor MOWG Study No. 7 suggests that affiliates provide higher quality local news and public affairs programming than network-owned stations. Thus, the studies provide evidence that a national limit of 35% is not necessary to preserve a class of affiliates in order to maintain high quality local news and public programming.

571. UCC argues that the number of awards received by stations is not a reliable measure of quality because the awards are not equally available to both network stations and affiliates. It argues that stations must apply for awards and pay entry fees to be considered.[1182] Moreover, it argues, networks generally have promotion and publicity departments that handle award entries, while local stations do not.[1183] While we agree with UCC that factors unrelated to quality programming can affect the number of awards received, there is no evidence that these factors had any measurable effect on the conclusion that network-owned stations' news programming is at least equivalent in quality to that of affiliates.

572. A third study finds that smaller station groups tend to produce higher quality newscasts than larger groups.[1184] In the PEJ Study, affiliates generally had higher quality scores than network-owned stations. Sixteen percent of affiliate stations earned "A's" in programming quality versus 11% of network-owned stations.[1185] According to PEJ's survey results, affiliates generally demonstrate somewhat more enterprise, cite more sources, tend to be more local, and are more likely to air stories that affect the community. Network-owned stations, on the other hand, are more likely to air national stories with no local connection, although they tend to air more points of view and score better in finding the larger implications of a story.[1186] The study also shows that only 22% of stations owned by the 25 largest group owners earned "A" grades for quality, compared with 48% of midsize and small groups. It acknowledges, however, that ratings for local news programming are growing more rapidly at larger group-owned stations than at smaller ones.[1187] Results of the PEJ Study suggest that being a network-owned station does not "improve the kind of local news that citizens see."[1188]

[1181] *Id* at App 1 at 10-11 This study used the same data as MOWG Study No. 7

[1182] UCC Comments at 55 (citing Radio-Television News Directors Association and Foundation, *Awards and Scholarships 2003 RTNDA Edward R Murrow Awards*, at www.rtnda.org/asfi/awards/murrow.shtml; The Graduate School of Journalism at Columbia University, *Alfred I DuPont Columbia University Awards*, www.jrn columbia.edu/events/dupont/entryform.pdf)

[1183] *Id* (citing E-Mail from Jonnet S Abeles, Director, Alfred I. DuPont Awards, Columbia School of Journalism, Nov 7, 2002).

[1184] PEJ Study, supra note 769.

[1185] *Id* at 4.

[1186] *Id* at 9

[1187] *Id* at 3.

[1188] *Id* at 8.

573. A critique prepared by Economists Inc. asserts that PEJ's principal findings are statistically insignificant.[1189] In addition, they contend the study relies on subjective measures of newscast quality, and does not account for other factors affecting news quality, such as geographic differences. In the critique, Economists Inc. states that PEJ has advised that it will not make underlying data available for analysis and review within the time frame of this proceeding; thus only limited information is available for use in determining the validity of PEJ's results.[1190] PEJ responds that the point of its survey was to identify patterns and trends in news quality. It asserts that it was not trying to prove a particular theory of cause and effect with its research, and states it has no financial stake in the outcome.[1191] Whether or not the PEJ Study is unbiased, its results appear statistically insignificant, the underlying data have not been made available, and therefore it cannot be considered reliable or convincing evidence.

574 The affiliates argue, however, that localism cannot be limited to local news and public affairs; rather, it is a rich mix of programming, and that the Commission itself has previously identified other elements, such as opportunities for local self-expression, development and use of local talent, weather and market reports, and sports and entertainment programming as necessary and desirable in serving the broadcast needs and interests of local communities.[1192] As we said in the *Notice*, stations may fulfill their obligation to serve the needs and interests of their communities by presenting local news and public affairs programming and by selecting other programming based on the particular needs and interests of the station's community.[1193] Thus, we acknowledge that other kinds of programming are important in serving local needs. However, we must rely on the data in the record, which focuses on two aspects of localism – program selection decisions by affiliates (preemption/collective negotiation) and the quality and quantity of local news and public affairs programming. From the data, we conclude that network-owned stations provide local news and public affairs programming that is at least equal, and may be superior, to that of affiliates.

575. *Discussion.* We conclude that the national cap is not necessary to encourage local stations to air local news and public affairs programming. The record actually suggests that the national cap diminishes localism by restraining the most effective purveyors of local news from using their resources in additional markets. The studies before us show that network-owned stations air, on average, more local news and public affairs programming than affiliates overall.[1194] MOWG Study No. 7 found that network-owned stations aired 4.3 hours more local news per week than did affiliates.[1195] The Baumann study concluded that the differential was 6.4 hours per week.[1196] The principal objection to the findings

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[1189] Economists Inc., "*The Project for Excellence in Journalism's PEJ Study of Ownership and Quality of Newscasts A Critique*" (Mar 13, 2003).

[1190] *Id* at 2

[1191] PEJ Study, *supra* note 766.

[1192] NAB/NASA Reply Comments at 4 (citing FCC Form 303, Attachment A of 1960 Report and Statement of Policy re: Commission En Banc Programming Inquiry (July 29, 1960))

[1193] *Notice*, 17 FCC Rcd at 18526 ¶ 70.

[1194] MOWG Study No. 7

[1195] *Id*.

[1196] Disney Feb. 13, 2003 Ex Parte.

of these two studies was NAB/NASA's criticism that exclusion of the Fox stations from those two studies would nullify the differential between the two groups of stations.[1197] We agree with Disney that no valid reason exists for excluding the Fox stations.

576 The record also shows that local news on network-owned stations appears to be of higher quality than news on affiliate stations. MOWG Study No. 7 found that network-owned stations received local news excellence awards at a significantly higher rate than did affiliates. For the DuPont awards, networks received 337% of the national average compared with 77% for affiliates. For the RTNDA awards, networks received 126% to affiliates' 96%.[1198] We disagree with commenters relying on the PEJ study to show that smaller group owners tend to produce higher quality local news. We agree with the networks that the findings of the PEJ are statistically insignificant. In other words, according to widely-accepted scientific standards, there is an unacceptably large risk that the PEJ's findings are attributable to random noise in the data. The PEJ Study reports the differences in percentages of newscasts that received a particular grade, but fails to provide any statistical testing on these results. The networks conducted these statistical tests and determined that the differences in news quality were not large enough to conclude that the probability of a newscast getting a particular grade was dependent on the ownership group that aired the newscast.

577. In sum, the record shows that the national cap is not necessary to promote high quality, or relatively larger amounts of, local news programming. The record suggests the opposite – that the current cap prevents networks from acquiring more stations and providing enhanced local news operations.

3. Modification of the National Television Ownership Rule

578 We have concluded that an audience reach cap of 35% is not necessary to promote diversity or competition in any relevant market. We are persuaded, however, that a national cap at some level is needed to promote localism by preserving the balance of power between networks and affiliates. We found that affiliates' incentives are more attuned to their local communities than are those of networks, which seek to assure that the largest audiences possible are watching their programming at the same time. We conclude from the record that preserving a balance of power between a network and its affiliates promotes localism, and accordingly, we will continue to restrict the national audience reach of station owners.

579 Given the benefits to innovation discussed above that derive from having a number of separately-owned station groups, we believe the national ownership cap should continue to apply to all station owners, including those that are not networks. The record shows that there have been a number of instances where having a variety of owners has led to innovative programming formats and technical advances, and we believe that applying the national ownership cap to all station owners will continue to spur innovation, which we believe will be particularly valuable in transitioning to digital television. In addition, applying the cap to all station owners adheres to our longstanding policy of refusing to

[1197] NAB/NASA Comments at 46.

[1198] A score of 100% for a station group would indicate that the stations in that group won precisely the number of awards that would be expected given the number of stations in that group relative to the total number of stations in the U.S

differentiate among different categories of station owners for purposes of the national TV ownership rule.[1199]

580. The next task is to determine what the ownership limit should be. As the court in *Sinclair* recognized, the Commission has wide discretion when drawing administrative lines.[1200] Having found that 35% is too low and 100% (or no limit) is too high, after considering the evidence in the record, we apply our discretion and raise the national ownership cap to 45%. This modification, fundamentally, is a line-drawing exercise in which we attempt to balance the benefits of a television ownership cap against the factors favoring an incremental increase. Finding a point between 35% and 100% is a matter of judgment falling within the particular expertise of the Commission.[1201]

581. We have decided to modify the national cap by raising it 10 percentage points for three primary reasons.[1202] First, while affiliates argue that it is necessary to preserve a balance of power between networks and affiliates so that affiliates can maintain adequate preemption rights, it is evident that networks can exceed a nationwide audience reach of 35% without harming affiliates' abilities to preempt network programming. As discussed above, affiliates of networks with a national reach of greater than 35% seem to have no less bargaining power than affiliates of networks with less than 35% national reach. In accordance with Section 202(h), therefore, the cap must be modified upward. The record does not, unfortunately, help us identify with any precision the point at which a network audience reach would be so large that affiliate bargaining power would be substantially undermined. Given that we are interested in finding a point at which the balance of power between networks and affiliates is roughly equal, however, we believe that a national audience reach cap of approximately half of all homes would be appropriate.

582 Second, we are mindful of the predictive nature of this line-drawing exercise and we have some concern about allowing significant new aggregation of network power absent more compelling evidence regarding the possible effects of that aggregation above current limits. Accordingly, and in light of the fact that Congress raised the ownership cap by ten percentage points in 1996, from 25% to 35%, we are inclined to take a similarly incremental approach and increase the cap by an additional 10 percentage points. Although a cap of 45% does not equate to a precisely equal degree of national reach

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[1199] *See 1984 Multiple Ownership Report and Order*, 100 F C.C.2d at 50-54 ¶¶ 97-107; *1985 Multiple Ownership MO&O*, 100 F C.C 2d at 87 ¶ 30 n.36 (since the adoption of a national TV ownership restriction, the limitations "have been applied in a uniform manner to all industry participants")

[1200] *Sinclair*, 284 F 3d at 162

[1201] *AT&T Corp v FCC*, 220 F.3d 607, 627 (D.C. Cir. 2000) (the Commission "has wide discretion to determine where to draw administrative lines"), *Cassell v FCC*, 154 F.3d 478, 485 (D C. Cir 1998) (the Commission's line-drawing is entitled deference so long as it is not "patently unreasonable"); *Health and Medicine Policy Research Group, et al v FCC*, 807 F.2d 1038, 1043 (D.C Cir 1987) ("the scope of review is particularly limited when the FCC engages in 'the process of drawing lines'"); *Hercules Inc v EPA*, 598 F.2d 91, 107-108 (D C Cir. 1978) (agency's numbers must only be within a "zone of reasonableness"). *See also* Letter from Jonathan D. Blake, Counsel for NASA, and Henry L. Baumann, Executive Vice President for Law & Regulatory Policy, NAB, to the FCC Chairman and Commissioners (April 30, 2003) at 1.

[1202] *But see* Letter from Jonathan D. Blake, Counsel for NASA, to Marlene Dortch, Secretary, FCC (May 8, 2003) Attachment at 7 (no evidence to support raising the cap to 40%, 45% or 50%) ("NASA May 8, 2003 Ex Parte").

for networks and their affiliates, a 45% limit ensures that networks will not obtain a greater national audience reach than their affiliates collectively will have.

583 Finally, although we elect not to modify the cap to the point advocated by Paxson (50%), we agree with Paxson that the cap should "accommodate all existing broadcast combinations and give some additional room for growth."[1203] A 45% cap will allow some, but not unconstrained, growth for each of the top four network owners.[1204] Broadcast networks have lost market share in recent years to cable and DBS, and allowing them to achieve better economies of scale and scope may help them remain competitive in the marketplace.[1205] Further, given the rise in programming costs and increasing competition from non-broadcast national media, the economies of scale and scope made possible by network expansion of station ownership will contribute to the preservation of over-the-air television by deterring the migration of expensive programming, such as sports programming, to cable networks.[1206] Accordingly, we herein modify the national audience reach rule to impose a 45% cap.

584. Although we affirm our finding in the *1984 Multiple Ownership Report and Order* that increased network ownership of stations will not harm either competition or diversity,[1207] our decision to retain a national ownership cap is a departure from our conclusion in 1984 that the national TV ownership rule should be repealed.[1208] In 1984, we gave very limited consideration to the potential

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[1203] Paxson Comments at 13-15. We decline to adopt Paxson's suggestion that we establish a presumption to increase the cap biennially by at least 2.5% until it reaches 60%. *Id*

[1204] Under the current rule, ABC owns ten stations reaching 23.6% of the national audience; CBS owns 39 stations reaching 39% of the national audience (these stations include the CBS as well as the UPN owned and operated stations, including 3 satellite stations); Fox owns 37 stations reaching 37.8% of the national audience (includes two satellite stations); and NBC owns 29 stations reaching 33.6% of the national television audience (these stations include the NBC as well as the Telemundo owned and operated stations, as well as a station located in Puerto Rico). *The Top 25 TV Station Groups*, B'CASTING AND CABLE (Apr. 7, 2003) at 32-34. There are currently 1,340 commercial television stations licensed by the Commission The percentage of these television stations owned by each of these networks is as follows· ABC owns less than 1%; CBS owns approximately 3%; Fox owns approximately 3%; and NBC owns approximately 2%.

[1205] Paxson Comments at 10 (due to competition from cable and DBS, network prime time viewership has declined to 57%) (citing *2001 Video Competition Report*, 17 FCC Rcd at 1282). *See also* Letter from Jared S Sher, Counsel for Fox, to Marlene Dortch, Secretary, FCC (April 30, 2003), Attachment at 52-54 We disagree with NAB/NASA that network profitability is not a valid reason for raising the national cap in this proceeding *See* Letter from Jonathan D. Blake, Counsel for NASA, and Henry L Baumann, Executive Vice President for Law & Regulatory Policy, NAB, to the FCC Chairman and Commissioners (April 23, 2003) at 1-2; NASA May 5, 2003 Ex Parte at 2-3; NASA May 8, 2003 Ex Parte, Attachment at 5-6

[1206] Fox Comments at 43 (the rule limits the return that networks can earn on their programming investments and drives them to direct their resources away from free television and toward subscription-based cable channels) Viewers complain that desirable programming already has begun migrating to subscription-based outlets. Thomas Smith Comments at 4, *see also* NABET-CWA Reply Comments at 2; The Grange Reply Comments at 3; Fox May 2, 2003 Ex Parte at 16; Letter from John C. Quale, Counsel for Fox, to Marlene Dortch, Secretary, FCC (May 12, 2003), Attachment 2 at 5-7.

[1207] *1984 Multiple Ownership Report and Order*, 100 F.C.C.2d at 46, 50-54 ¶¶ 86, 97-107.

[1208] *See id* at 18-20 ¶¶ 4-10.

effects of the cap on localism.[1209] That attention was devoted to the quality and quantity of news and public affairs programming on group-owned versus individually-owned stations.[1210] In this *Report and Order*, by contrast, we have expanded our "localism" measures to include the important consideration of program selection by local stations. The 1984 decision did not address the balance of power between networks and affiliates and how that affects program selection.[1211] It is this factor that is the central factor in our decision to retain a national cap.

4. UHF Discount

585. In the *Notice*, the Commission invited comment on the relevance and continued efficacy of the 50% UHF discount.[1212] The *Notice* explained that the discount was enacted because UHF stations were competitively disadvantaged by weaker signals and smaller household reach than VHF stations.[1213] In light of greater carriage of UHF stations on MVPDs since enactment of the UHF discount in 1985, we sought comment on the continued need for the UHF discount.

586. We conclude that the UHF discount continues to be necessary to promote entry and competition among broadcast networks. VHF signals typically reach between 72 and 76 miles, while UHF signals reach approximately 44 miles. This signal disparity results in a significantly smaller household reach of UHF signals compared with VHF signals. Fox, NBC and Viacom submitted data showing that, in markets where they own both a UHF and a VHF station, the UHF station reaches between 56% and 61% of the service area of their VHF stations.[1214] Similarly, Paxson states that in eight cities where it owns UHF stations, its stations reach between 35.7% and 78.2% of the homes reached by VHF stations in those markets [1215]

587. This diminished UHF signal area coverage affects UHF stations' ability to compete with VHF stations in two ways. First, although cable and DBS operators serve 86% of U.S. households, the Commission recently determined that roughly 30% of television sets are not connected to MVPD service

[1209] In our 1984 decision, we acknowledged that "network-owned stations have rendered meritorious service to their local communities" *Id* at 53 ¶ 105 This observation, which continues to hold true, does not, however, negate the importance of the affiliates' role in furthering localism.

[1210] *Id* at 31-36 ¶¶ 44-56.

[1211] *See* Cox Comments at 9; Letter from Jonathan D. Blake, Counsel for NASA, and Henry L Baumann, Executive Vice President for Law & Regulatory Policy, NAB, to Marlene Dortch, Secretary, FCC (May 9, 2003), Attachment at 2; Letter from Jonathan D. Blake, Counsel for NASA, and Henry L Baumann, Executive Vice President for Law & Regulatory Policy, NAB, to the FCC Chairman and Commissioners (May 15, 2003) at 1-2.

[1212] *Notice*, 17 FCC Rcd at 18545 ¶¶ 130-131 The UFH discount is intended to recognize the deficiencies in over-the-air UHF reception in comparison to VHF reception.

[1213] *Id* at 18545 ¶ 130.

[1214] Letter from John C. Quale, Counsel for Fox, to Marlene Dortch, Secretary, FCC (May 20, 2003) ("Fox May 20, 2003 Ex Parte")

[1215] Letter from John R. Feore, Counsel for Paxson, to Marlene Dortch, Secretary, FCC (May 16, 2003) at Attachment 3

and receive exclusively over-the-air broadcast stations.[1216] UHF stations reach far fewer of these broadcast-only viewers as VHF stations Second, weaker UHF signals make it more difficult for a UHF station to qualify for cable and DBS carriage. Commission regulations require a local television station to place a Grade B signal over the cable or DBS headend in order to qualify for carriage.[1217] Alternatively, if a station does not place a Grade B signal over the headend, it may pay for an alternative method of delivering its signal to the headend, such as a fiber optic connection.[1218] Non-carriage on a cable system will, as a practical matter, make the UHF station unavailable to homes in the MVPD's service area.

588. In addition to diminished signal coverage, UHF stations require between 1.5 and 3 times greater electricity costs to operate than VHF stations.[1219] UHF stations also require more expensive transmitters than VHF stations.[1220] These factors, along with the signal coverage disparity, appear to diminish the ability of UHF stations to compete in the delivered video programming market. According to a 1997 study provided by Paxson, VHF affiliates of the top four broadcast networks had approximately 50% higher ratings than UHF affiliates of the top four networks.[1221] Paxson then replicated this study with 2002 ratings information and determined that the ratings disparity between UHF and VHF stations had actually *increased* between 1997 and 2002. Paxson's filing shows that, in November of 2002, network-affiliated VHF stations received approximately 57% higher ratings than network-affiliated UHF stations, compared with 50% in 1997.[1222] Thus, even after controlling for factors such as programming and market size, UHF stations continue to experience a competitive handicap compared with VHF stations. This disparity translates into reduced advertising revenues for UHF stations.[1223] Thus we disagree with UCC that the UHF handicap has largely been eliminated by greater cable and DBS carriage of UHF signals.[1224]

589 In addition to strengthening competition between UHF and VHF stations, the UHF discount promotes entry by new broadcast networks. Paxson asserts that the UHF discount enhanced its ability to launch a new broadcast network because it could own more UHF stations than VHF stations. Paxson states that the additional ownership of stations permitted by the UHF discount provides a

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[1216] *2001 Video Competition Report*, 17 FCC Rcd at 1282 ¶ 79

[1217] 47 C F R § 76.55(c)(3).

[1218] 47 C.F R. § 76.66(g).

[1219] Letter from John R. Feore, Counsel for Paxson, to Marlene Dortch, Secretary, FCC (May 7, 2003) ("Paxson May 7, 2003 Ex Parte"), Attachment C at 11.

[1220] *Id*

[1221] Paxson May 7, 2003 Ex Parte, Attachment C at 9 (stating that VHF-based affiliates received a 9.6 prime time rating compared UHF affiliates' 6 4 rating).

[1222] Letter from John R. Feore, Counsel for Paxson, to Marlene Dortch, Secretary, FCC (May 30, 2003), Attachment at 2.

[1223] Fox May 20, 2003 Ex Parte, Declaration of Michael Ward, General Manager, WNCN(TV) (stating that advertisers routinely discount the prices paid for advertising on UHF stations versus VHF stations).

[1224] UCC Comments at 57-58

significant financial incentive for new networks to enter and compete with established networks.[1225] This is because ownership of stations, as opposed to affiliation with separately-owned stations, enables a network such as Paxson's to earn both national and local advertising revenues.[1226] Univision also states that the UHF discount has enabled it to enter the market with programming tailored to Hispanic audiences. Univision explains that its entry as a broadcast network is particularly beneficial to Hispanic audiences because they rely disproportionately on over-the-air broadcast channels.[1227]

590. Finally, we observe that the established broadcast networks generally have not sought to take advantage of the UHF discount to gain greater national reach through local stations. The four most established broadcast networks collectively own 67 stations, 12 of which are UHF stations.[1228] Instead of replacing their VHF stations with UHF stations and owning up to 70% national coverage, they have retained their VHF stations and sought elimination of the national ownership cap. By contrast, Paxson, a recent entrant into the broadcast network business, owns 61 stations, all of which are UHF.[1229] Absent the UHF discount, Paxson's audience reach would be 61.8% of the nation's television households. This data indicates that the UHF discount plays a meaningful role in encouraging entry of new broadcast networks into the market. For these reasons, we retain the UHF discount.

591. The Commission has previously said it will issue a notice of proposed rulemaking proposing a phased-in elimination of the discount when DTV transition is near completion.[1230] At this point, however, it is clear that the digital transition will largely eliminate the technical basis for the UHF discount because UHF and VHF signals will be substantially equalized. Therefore, we will sunset the application of the UHF discount for the stations owned by the top four broadcast networks (*i e.*, CBS, NBC, ABC and Fox) as the digital transition is completed on a market by market basis. This sunset will apply unless, prior to that time, the Commission makes an affirmative determination that the public interest would be served by continuation of the discount beyond the digital transition. For all other networks and station group owners, we will continue to examine the extent of competitive disparity between UHF and VHF stations as well as the impact on the entry and viability of new broadcast networks. In a subsequent biennial review, we will determine whether to include stations owned by these other networks and station group owners in the sunset provision we have established for stations owned by the top four broadcast networks.

B. Dual Network Rule

592. The dual network rule provides: "A television broadcast station may affiliate with a

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[1225] Paxson May 7, 2003 Ex Parte, Attachment C at 18.

[1226] *Id.*

[1227] Univision Reply Comments at 6 (52.8% of Hispanic television households in the top 30 markets subscribe to cable television. This compares with 67 8% of U.S. households that subscribe to cable overall.). *See* OPP Working Paper 37 at 41.

[1228] *The Top 25 Station Groups*, BROADCASTING & CABLE, Apr. 7, 2003.

[1229] Paxson owns 61 stations, 60 of which belong to the PAX television network. Paxson also owns a station that is affiliated with ABC. *Id See also* Paxson Comments at 2

[1230] *1998 Biennial Review Report*, 15 FCC Rcd at 11079-80 ¶ 38.

person or entity that maintains two or more networks of television broadcast stations unless such dual or multiple networks are composed of two or more persons or entities that, on February 8, 1996, were 'networks' as defined in § 73.3613(a)(1) of the Commission's regulations (that is, ABC, CBS, Fox, and NBC)."[1231] Thus, the rule permits common ownership of multiple broadcast networks, but prohibits a merger between or among the "top-four" networks, *i.e.*, ABC, CBS, Fox, and NBC. In this *Order*, we conclude that the dual network rule is necessary in the public interest to promote competition and localism

1. Background

593. The original dual network rule, which prohibited any entity from maintaining more than a single radio network, was adopted over sixty years ago.[1232] The rule was later extended to television networks.[1233] The Commission believed that an entity that operated more than one network might preclude new networks from developing and affiliating with desirable stations because those stations might already be affiliated with the more powerful network entity.[1234] In addition, the Commission expressed concern that ownership of more than one network could give the owner too much market power.[1235] The rule, therefore, was intended to serve the Commission's competition and diversity goals.[1236]

594 In the 1996 Act, Congress directed the Commission to amend the rule,[1237] which it did, to permit common ownership of two or more broadcast networks, but not a merger among ABC, CBS, Fox, or NBC, or between one of these top-four networks and UPN or WB.[1238] In 2001, the Commission further modified the rule to permit a top-four network to merge with or acquire UPN or WB.[1239] The Commission found that: (1) competition in the national advertising market would not be harmed; (2) greater vertical integration was potentially an efficient, pro-competitive response to increasing

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[1231] 47 C F R § 73.658(g)

[1232] 6 Fed. Reg at 2282 (May 6, 1941).

[1233] *Amendment of Part 3 of the Commission's Rules*, 11 Fed. Reg. 33 (Jan 1, 1946).

[1234] *1998 Biennial Review Report*, 15 FCC Rcd at 11095-96 ¶ 70

[1235] *Id*

[1236] *Id.*

[1237] Section 202(e) of the 1996 Act directed the Commission to modify the dual network rule to prohibit a television station from affiliating with any entity that owns more than one of the four major networks (ABC, CBS, Fox, or NBC) or one of the four major networks and an emerging English-language network which, on the date of the 1996 Act's enactment, "provides 4 or more hours of programming per week on a national basis pursuant to network affiliation arrangements with local television broadcast stations in markets reaching more than 75 percent of television homes " 1996 Act, § 202(e) The legislative history of the "emerging network" provision indicated that it was intended to apply to only the UPN and WB television networks *See* S Rep. No 230, 104th Cong., 2d Sess. at 163.

[1238] *See* note 1062, *supra*

[1239] *Dual Network Order supra* note 95.

competition in the video market; and (3) program diversity would not be harmed because the two combined networks would have economic incentives to diversify their program offerings.[1240]

595. The restrictions in the current rule apply only to combinations of the top-four networks. All existing network organizations, and all new network organizations, may create and maintain multiple broadcast networks. Thus, the current rule permits common ownership of multiple broadcast networks created through internal growth and new entry.

596. Although the dual network rule gives all network organizations the opportunity to pursue any economic efficiencies that may arise from the maintenance of multiple broadcast networks, it restricts the manner in which specific network organizations may operate multiple broadcast networks. Specifically, the rule permits ABC, CBS, Fox, and NBC to develop multiple broadcast networks by: (1) creating new broadcast networks; (2) acquiring new broadcast networks; or (3) acquiring video networks from non-broadcast media (*e.g.*, cable or satellite) and migrating them to broadcast networks. However, the rule prohibits ABC, CBS, Fox, and NBC from developing multiple broadcast networks by merging with one another.

597 In the *Notice*, we sought comment on whether the present dual network rule is necessary in the public interest as the result of competition. We asked whether it promotes the goals of competition, diversity, or localism. We further asked whether, if the rule serves some of our purposes and disserves others, the balance of its effects argue for keeping, modifying, or abolishing the dual network rule.[1241]

598. Despite the voluminous record developed in this proceeding, few commenters addressed the dual network rule.[1242] Several commenters assert that the top-four networks are unique in that they regularly compete against each other for viewers (*i.e.*, their programming is targeted at similar national audiences, as opposed to the niche audiences smaller broadcast networks and cable networks target), that they each consistently generate the largest national audiences for their programming (thereby receiving the most advertising revenue, which, in turn, provides the funding to purchase the most desired programming), and that competition would be harmed by allowing any of them to merge.[1243] Several commenters also assert that concentration of ownership in the top-four networks would result in harms to diversity by providing fewer national and local viewpoints in news reporting and fewer programming choices for viewers.[1244] One commenter also argues that localism would be harmed by a top-four network merger because the merger would increase the economic leverage the networks have over their

[1240] *Id* at 11124-25, 31 ¶¶ 24-25, 37.

[1241] *Notice*, 17 FCC Rcd at 18552-53 ¶ 159.

[1242] Those specifically mentioning the dual network rule in their comments are: AFL-CIO; AFTRA; CCC; Children Now, CWA; Fox; NAB/NASA; Smith; Stapleton; UCC, and Writers Guild. Of these eleven commenters, five devoted one paragraph or less to a discussion of the rule.

[1243] *See* CCC Comments at 17, NAB/NASA Comments at 73-74, 77; Stapleton Comments at 16; Writers Guild, *et al* Comments at 16

[1244] *See* AFL-CIO Comments at 63-64; AFTRA Comments at 36-38; CCC Comments at 18-19; UCC, *et al.* Comments at 59-60, Writers Guild, *et al* Comments at 14.

affiliates.[1245] The sole commenter arguing for elimination of the rule, Fox, asserts that competition will not be harmed because consumers have access to a vast array of other media outlets, that diversity will be maintained because common network ownership provides incentives to produce a diverse schedule of programming, and that localism will not be affected because stations have strong financial incentives to provide local programming regardless of their network affiliation.[1246] We analyze these arguments below in discussing whether the rule is necessary in the public interest as the result of competition.[1247]

2. Discussion

599. Under Section 202(h), we consider whether the dual network rule continues to be "necessary in the public interest as the result of competition." In determining whether the rule meets this standard, we consider whether the rule promotes competition, localism, and diversity. We conclude that the dual network rule continues to be necessary in the public interest to promote competition and localism.

a. Competition

600. We begin by summarizing the complex roles played by broadcast networks. Broadcast networks acquire a collection of programs from program producers. The programs are selected based on their ability to attract audiences that can be sold to advertisers. These programs - with advertisements embedded - are then made available to television audiences through the broadcast network's owned and operated broadcast television stations ("O&Os"), and also through contractual arrangements with affiliated broadcast television stations. Thus, a broadcast network serves many roles. It is an intermediary between local broadcast stations and advertisers and program producers Because the top-four broadcast networks are participants in the program acquisition market and the national advertising market, mergers among them can affect competition in each of these markets.

601. Given the level of vertical integration of each of the top-four networks, as well as their continued operation as a "strategic group"[1248] in the national advertising market, a top-four network merger would give rise to competitive concerns that the merged firm would be able to reduce its program purchases and/or the price it pays for programming. As a result, we conclude that the dual network rule remains necessary in the public interest to foster competition.

(i) Program Acquisition Market

602. The top-four networks are the broadcasting components of vertically-integrated firms, which compete against each other to acquire programming that will attract the largest national

[1245] *See* NAB/NASA Comments at 75-76

[1246] *See* Fox Comments at 44-45, 47-48.

[1247] In its Comments, NAB/NASA states that "NAB takes no position on whether the Commission should retain the current version of the dual network rule." NAB/NASA Comments at 72, NAB/NASA Reply Comments at 57. The arguments opposing changes to the dual network rule are therefore made by NASA.

[1248] A strategic group refers to a cluster of independent firms within an industry that pursue similar business strategies. *See* footnote 1259, *infra*, for a discussion of strategic groups.

audiences.[1249] Competition in the program acquisition market is important because networks compete with each other to acquire new, diverse, and innovative programming. A top-four network merger would give rise to competitive concerns that the merged firm would restrict the consumption of programming by using its market power to limit competitors' access to sources of programming. In addition, the merged network could use its market power to control the price it pays for programming or to raise competitors' costs of acquiring programming. In concentrated markets, viewers have access to fewer programming choices if the number of national, independent purchasers of programming decreases due to limited access to programming and higher programming costs.

603. NASA argues that a merger of two or more of the top-four networks would result in a less competitive program acquisition market, evidenced by lower output, fewer choices, and less technological progress.[1250] CCC argues that the top-four networks represent a distinct and important resource for viewers because only they are able to consistently distribute both news and entertainment programming to a mass audience, using their cable subsidiaries and local broadcast affiliates.[1251] Fox, on the other hand, argues that the rule actually undermines the Commission's competition policy by discouraging broadcast investment to the detriment of consumers of free over-the-air television.[1252] Fox also argues that the program acquisition market is only moderately concentrated, having an HHI of approximately 1120.[1253] In support of this argument, Fox asserts that the program acquisition market is characterized by a large number of purchasers of exhibition rights, including broadcast networks, broadcast stations, cable networks, DBS operators, premium cable networks, pay-per-view providers, and distributors of video cassettes and DVDs.[1254] NASA counters that the major broadcast networks do not compete with the cable networks for mass-audience, prime-time programs, and that the only avenue of distribution for such programs is the television broadcast networks.[1255] NASA therefore asserts that only the major broadcasting networks should be considered in an analysis of concentration in the purchase of national video programming.[1256]

[1249] ABC (a broadcast network) is vertically integrated with Disney (a program supplier); CBS (a broadcast network) is vertically integrated with Viacom (a program supplier); Fox (a broadcast network) is vertically integrated with News Corp and 20th Century Fox (a program supplier); and NBC (a broadcast network) is vertically integrated with NBC Entertainment's subsidiary NBC Studios (a program supplier)

[1250] *See* NAB/NASA Comments at 58-60.

[1251] *See* CCC Comments at 17-18.

[1252] Fox Comments at 48.

[1253] Fox Economic Study E at 1 Fox economists excluded expenditures on news and sports programming because most of the inputs used in creating such programs are not readily substitutable with the inputs used in creating entertainment television programs and theatrical films.

[1254] *Id.*

[1255] NAB/NASA Reply Comments at 57 By NASA's estimate, which is based on an analysis of Fox's Economic Study E, Table E2, the top-four networks account for over 87 percent of programming expenditures by broadcasting networks, and the video entertainment program acquisition market has an HHI of approximately 2100, a result considered "highly concentrated" under the DOJ/FTC Merger Guidelines. *Id*

[1256] *Id.*, citing its Comments at 74-75

604. We agree with Fox and NASA that the context for analyzing the program acquisition market is to consider the shares of expenditures on video entertainment programming. We conclude, however, that a more accurate assay of the market includes the shares of broadcast networks, broadcast stations, basic cable networks, pay cable networks, and pay-per-view networks. We reject NASA's narrow definition because they provide no evidentiary reason to exclude other video programming purchasers and they dismiss the range of programming choices available to viewers over the air, via cable and via satellite. We do not agree with Fox's more expansive definition, specifically the inclusion of home video, as that requires additional action on the part of individual viewers, such as purchasing a DVD player, driving to a video rental store, and renting a DVD. We conclude that using broadcast networks, broadcast stations, basic cable networks, pay cable networks, and pay-per-view networks in our analysis accurately represents the market participants, and their role in delivering programming to large, passive audiences. In order to examine the effect of mergers among broadcast television networks subject to this rule, we can construct hypothetical merger scenarios, building on the scenario developed in the national cap section of this Order. In the absence of actual figures for the network companies' broadcast station expenditures, we can only examine the effects of mergers amongst the networks (i.e., without their complement of O&Os, but including the cable networks they own). For the same reason, we can only calculate the change in the HHI, not the "base level" HHI. So, for example, if Fox merged with GE and Disney merged with Viacom, the HHI would increase by almost 767 points. Then, if these two companies merged with each other, the HHI would increase by 2,246 points. Either of these changes in the HHI would be scrutinized under DOJ Merger Guidelines. Since these networks own television stations, the change in the HHI would actually be higher than in these examples.

605. Accordingly, we conclude that a merger between or among any of the top-four networks would harm competition in the program acquisition market. As noted, we determine in our analysis of the national ownership cap that an increase in the cap would not harm the program acquisition market, principally because networks would be enhancing their owned and operated distribution base. Our analysis of a merger between two or more of the top-four broadcast networks, however, indicates a significant potential for harm to this market In addition to acquiring an entire group of owned and operated stations and all of the affiliation agreements of the stations aligned with the network, a merger would also entail the acquisition of significant program purchasing power by the vertically integrated merging networks. The vertically integrated networks would limit competitors' access to programming by denying remaining networks access to the production output of the merged network.[1257] In addition the merged firm can raise the price paid by those competitors for programming created and produced by the merged network's program production assets. The rule, therefore, remains necessary to promote competition in the program acquisition market.

(ii) National Advertising Market

606. Networks sell national advertising by creating large national audiences for their programming and delivering those audiences to advertisers. Sellers in the national advertising market include national broadcast networks, cable networks, and syndicators. Network O&Os, network-affiliated stations, and independent stations sell national spot advertising time, which is advertising sold on a market-by-market basis to national advertisers. National spot advertising time provides a

[1257] Currently, one network studio may produce programming that is ultimately purchased by another network. For example, Paramount, a subsidiary of Viacom, produces the long running NBC series "Frasier" and the NBC series "Ed." Also, in addition to producing shows for The WB network, Warner Brothers has produced shows for ABC ("The Drew Carey Show" and "George Lopez") and NBC ("ER" and "West Wing").

competitive alternative to national advertising time to a certain extent. These sellers compete against each other not only based on the price they charge for advertising spots, but also based on their ability to deliver the largest number of viewers to their advertisers. If a merger were to reduce competition for advertising dollars, networks would have less incentive to compete against each other for viewers, which would lead them to pay less attention to viewers' needs and to produce less varied, lower quality, and less innovative programming.

607. In our discussion above of the necessity of maintaining the national TV ownership rule,[1258] we conclude that the networks compete with each other and with cable networks for national advertising revenues and that the current ownership cap was not necessary to ensure competition in the national advertising market. However, while we find that the top-four networks do not possess market power today, that would change if two or more of them were to merge with each other. Moreover, as explained in the *Dual Network Order*, the top-four networks comprise a "strategic group" within the national advertising market.[1259] The top-four networks compete largely among themselves for advertisers that seek to reach large, national, mass audiences – a significant portion of the national advertising market that provides the top-four networks with a significant portion of their profits. We therefore conclude that a merger of two or more of the top-four networks would substantially lessen competition in the national advertising market, especially within the strategic group,[1260] with the concomitant harm to viewers described above.

608. The recent growth of cable and DBS does not alter our conclusion. Despite that growth, the top-four networks continue to provide the greatest reach of any medium of mass communications. The top-four networks attract much larger prime-time audiences in relation to advertisement-supported cable networks.[1261] Broadcasting's percentage share of advertising revenue continues to exceed its

[1258] *See* Section VII(A), *supra*.

[1259] *Dual Network Order*, 16 FCC Rcd at 11122-23 ¶ 20. A strategic group refers to a cluster of independent firms within an industry that pursue similar business strategies. For example, the top-four networks supply their affiliated local stations with programming intended to attract mass audiences and advertisers that want to reach such large, nationwide audiences. By contrast, the emerging networks target more specialized, niche audiences similar to cable television networks. The conceptual basis for a strategic group is developed in R. E. Caves and M. E. Porter, *From Entry Barriers to Mobility Barriers Conjectural Decisions and Contrived Deterrence to New Competition*, Q J ECON 91 (May 1977): 241-261. *Also see* Michael E Porter, COMPETITIVE STRATEGY: TECHNIQUES FOR ANALYZING INDUSTRIES AND COMPETITION (New York: The Free Press, 1980), Ch. 7 For additional references on the application of the strategic group concept, see F. M. Scherer and David Ross, INDUSTRIAL MARKET STRUCTURE AND ECONOMIC PERFORMANCE, (3rd ed.) (Boston: Houghton Mifflin, 1990) at 284-85. When properly applied, the concept of a strategic group ordinarily implies that only a relatively few firms will be included within its boundaries so that competitive rivalry will be oligopolistic in nature, although the number of firms actually populating the industry aggregated over all strategic groups may be quite numerous

[1260] Our analysis suggests that economic concentration within the strategic group for 2001, as measured by the HHI, is 2646 This is based on advertising revenue and on shares of the top-four broadcast networks as reported by Richard Bilotti, *supra* note 1103. Any HHI above 1800 indicates a "highly concentrated" market *See DOJ/FTC Merger Guidelines*. A merger between two or more of the top-four networks would produce a change in the HHI of over 100 points, which, according to DOJ guidelines, is an indication that such a merger should be reviewed to ensure that it would not enhance market power or facilitate its exercise *Id.*

[1261] For example, during the month of February, 2003 (1/27/03 – 2/23/03), CBS, NBC, ABC, and Fox delivered prime-time household ratings of 8.9, 8.1, 6.7, and 6 7, respectively, as compared to the top advertiser-supported (continued.. .)

percentage share of viewing.[1262] Moreover, despite a decrease in audience share, the top-four networks continue to command increases in advertising rates, a further testament to the strength of broadcasting television as an advertising medium.[1263]

609. We agree with NASA that despite the emergence of new media on cable, DBS, and the Internet, the top-four broadcast networks still have the largest concentration of viewers and television economic power.[1264] A recent survey shows that each of the top twenty-five prime-time broadcast programs during the week of December 9-15, 2002, all of which were aired by CBS, ABC, NBC, or Fox, achieved considerably higher household ratings than any of the 25 highest ranked cable programs.[1265] The highest-ranked broadcast program had a rating larger than the top five cable programs' ratings combined.[1266] We also agree that as it becomes more difficult to reach a large number of viewers, television broadcasters that can still deliver a mass audience become more valuable.[1267]

610. We further conclude, as we did in the *Dual Network Order*, that obtaining a sufficient number of affiliated stations remains a major obstacle to developing a new broadcast network capable of attracting national advertisers seeking to reach a mass audience.[1268] As long as mobility barriers[1269] deter entry into the major network strategic group, the pricing of network advertising will be sensitive to the

(Continued from previous page)

cable network, TNT, which garnered a 1.8 share rating. (A rating point is equal to 1.067 million households.) *See* Television Bureau of Advertising, Viewer Track, *Monthly Broadcast vs. Cable Primetime Ratings· Feb-2003 vs Feb-2002*, at http.//www.tvb.org/rcentral/viewertrack/monthly/mon-b-c/mon-b-c.asp?ms=Feb-2003_vs_Feb-2002 html (visited March 7, 2003).

[1262] *See e g.*, NAB/NASA Comments at 13, stating that broadcasting's share of advertising revenue in 2001 was 71 5% whereas its audience share stood at 53.7%. In addition, the networks have been able to increase the quantity of advertising availabilities for sale by adding more commercial minutes per hour. *Id.*

[1263] The networks have raised prices for advertising on a cost per thousand ("CPM") viewers basis steadily Prime-time broadcast network CPMs have increased from $9.74 in 1990 to $13.42 in 2000, an average annual growth rate of 3.8%. *See* OPP Working Paper 37 at 28. In addition, an advertising industry compilation indicates that the top-four commercial networks increased hourly commercial minutes by 16.4% from 1991 to 2000, from an average of seven minutes and 47 seconds to an average of nine minutes and three seconds *Id.*

[1264] NAB/NASA Comments at 74

[1265] *Id.*, citing Television Bureau of Advertising, Inc , Viewer Track, *Top 25 Programs on Broadcast and Cable Week Ending Dec 15, 2002, at* http·//www tvb.org/rcentral/index html (visited Jan 1, 2003)

[1266] *Id.*, citing also its earlier notes 34-35 and accompanying text (observing that 99 of the 100 top-rated prime-time programs are broadcast programs, and that the combined average viewership for the four major broadcast networks is almost six times as high as that of the top ten ad-supported cable networks).

[1267] *See* NAB/NASA Comments at 75.

[1268] *Dual Network Order*, 16 FCC Rcd at 11123 ¶ 20. *See also* NAB/NASA Comments at 73

[1269] Mobility barriers are barriers to entry that deter the movement of a firm *within* a given industry from shifting from one strategic group to another. Different strategic groups will be defended by different mobility barriers that vary in their effectiveness in restricting entry into a given strategic group. In general, firms protected by high mobility barriers will have greater profit potential than firms in other strategic groups protected by low mobility barriers.

number of network competitors.[1270] We therefore conclude that the current dual network rule is necessary to maintain competition in national advertising market

b. Localism

611. We conclude that the dual network rule also is necessary to retain the balance of bargaining power between the top-four networks and their affiliates. As noted in the national TV ownership rule section, we conclude that affiliates play an important role in assuring that the needs and tastes of local viewers are served.[1271] Elimination of the dual network rule would harm localism by providing the top-four networks with increased economic leverage over their affiliates, thereby diminishing the ability of the affiliates to serve their communities.[1272]

612. The top-four networks have an economic incentive to promote the widest distribution nationwide of the programming that they produce and to assure that it is carried simultaneously across the country. To reach the most viewers, the top-four networks acquire their own stations ("O&Os"), usually in the largest television markets, and enter into affiliation agreements with station owners throughout the remainder of the country. Through affiliation, the networks benefit from the wide-area delivery of their programming. Network affiliates benefit, in turn, by gaining access to high-quality programming.

613. Affiliates have an economic incentive to tailor their programming to their local audiences. Affiliates can influence network programming decisions by joining forces with other network affiliates in collective negotiations to ensure that the programming provided by the network serves local needs and interests. The strength of an affiliate's influence with its network lies in its power as part of a "critical mass" to join forces with other network affiliates in collective negotiations to try to influence network programming.[1273] On an individual basis, affiliates may also decide to preempt network programming if other programming is available that better suits local needs.

614. As noted by NASA, because of the costs of programming and promotional expenses, network affiliation remains critical for the economic survival of most local television stations.[1274] NASA argues that if the dual network rule were eliminated, a top-four network merger would result in the networks gaining an unfair advantage over their affiliates, noting that a merger would reduce alternative choices of program providers for affiliates as the number of network owners decreases.[1275] As an example, NASA notes that if NBC and CBS were permitted to merge, a terminated CBS affiliate would no longer be able to turn to NBC for affiliation.[1276] The harm would be exacerbated if more than two of

[1270] *See also* NAB/NASA Comments at 75.

[1271] *See* Section VII(A), *supra.*

[1272] *See id.* for a discussion of localism and its importance in the balance of power between networks and their affiliates.

[1273] NAB/NASA Comments at 2-3.

[1274] *Id*

[1275] *Id* at 75-76.

[1276] *Id*

the top-four networks were to combine.

615. We agree with NASA that a top-four network merger would harm localism by providing the networks with undue economic leverage over their affiliates. While a top-four network merger may not result in fewer networks, it would result in fewer network *owners*. We conclude that a top-four network merger would reduce the ability of affiliates to bargain with their network for favorable terms of affiliation, and would result in less influence of affiliates on network programming. As the number of network owners declines, affiliates lose the ability to use the availability of other top independently-owned networks as a bargaining tool with their own networks. In the same way, a combined top-four network's increased leverage could be used to overwhelm affiliate bargaining power with respect to programming issues. A top-four network merger would lead to fewer alternatives for affiliates, which would lead to reduced bargaining power of affiliates, and less influence of affiliates on network programming, including the ability to preempt network programming that affiliates find to not serve their local communities. We therefore conclude that the dual network rule remains necessary to foster localism.

c. Diversity

616 In the *Notice*, we sought comment on the dual network rule's effect on program diversity and viewpoint diversity.[1277] As noted in the national TV ownership rule section, we conclude that the market for diversity is local, not national.[1278] As also noted, we conclude that viewpoint diversity is the most pertinent aspect of diversity for purposes of our ownership rules.[1279] Nevertheless, since several commenters argue that elimination of the dual network rule would result in a diminution of program diversity, we address their arguments.[1280]

617. Several commenters argue that elimination of the dual network rule would result in less diverse programming and that national viewpoints in news reporting would be diminished.[1281] AFL-CIO and AFTRA argue that recent mergers and consolidation in the industry have resulted in instances of reduced viewpoint diversity and program diversity in local markets.[1282] AFTRA also argues that

[1277] *Notice*, 17 FCC Rcd at 18553-54 ¶¶ 160-163.

[1278] *See* Section VII(A) *supra*

[1279] *See id*

[1280] *See* UCC Comments at 59-61; NAB/NASA Comments at 78; AFL-CIO Comments at 61-62; AFTRA Comments at 34; and CCC Comments at 19.

[1281] *See* CCC Comments at 19; UCC Comments at 59; AFL-CIO Comments at 61-62; AFTRA Comments at 34-35; and NAB/NASA Comments at 78.

[1282] AFL-CIO Comments at 61-62, gives the following as examples: Viacom in Philadelphia owns the local CBS and UPN television stations and KYW-AM radio, and has assigned radio anchors to produce news for UPN; Viacom in Detroit dropped its local CBS-TV news and has contracted WXYZ to produce its UPN-TV news; and NBC is combining its news operations with Telemundo. AFL-CIO further states that BET, which is now owned by Viacom, has cancelled several news-related and public affairs shows, and that NBC O&Os have begun to merge station operations with Paxson TV affiliates, only rebroadcasting NBC news on PAX stations. *See also* AFTRA Comments at 34-35.

elimination of the rule will quell new voices and diverse viewpoints, "as emerging networks are quashed in favor of more 'cost-effective' means of delivering content."[1283] CCC argues that because CBS is "repurposing" its original programming on UPN, diversity between the two networks is reduced.[1284] CCC also argues that WB, UPN, and the cable networks do not have the audience reach or the resources to fill the diversity void created if the national networks were reduced by elimination of the rule.[1285] Fox disagrees, arguing that the vast array of other media outlets will provide the public with sufficiently diverse information and views.[1286]

618. One commenter, UCC, argues that despite recent gains in the popularity of other forms of media, national broadcast television continues to be the public's most important source for national and international news.[1287] UCC argues that the average weekday reach of the evening newscasts of ABC, CBS and NBC is about 10 times the combined reach at 6:30 p.m. for Fox, CNN, CNN Headline News, MSNBC, and CNBC.[1288] Because network news on broadcast television is expensive to produce, UCC argues, a top-four network merger would result in the consolidation of news departments in order to achieve economic efficiency.[1289]

619. In the *Dual Network Order*, the Commission found that program diversity at the national level would not likely be harmed by the combination of an emerging network (*i.e.*, UPN or WB) with one of the top-four networks. The Commission found it likely that a common owner would have strong incentives to produce a diverse schedule of programming for each set of local TV outlets in the same market.[1290] In this proceeding, we address possible combinations among only the top-four networks, which are distinct from combinations between a top-four network and an emerging network.[1291] Also, we

[1283] AFTRA Comments at 34

[1284] CCC Comments at 19

[1285] *Id.* at 18

[1286] Fox Comments at 44-45

[1287] UCC Comments at 60.

[1288] *Id.* at 60 (citation omitted).

[1289] *Id* at 60-61

[1290] *Dual Network Order*, 16 FCC Rcd at 11131 ¶ 37 Fox argues in this proceeding that a top-four network merger would result in the same incentives for the merged firm, and that all network outlets, regardless of ownership, will continue to pursue the elusive goal of divining audience tastes. Fox Comments at 45-47.

[1291] We agree with NAB/NASA that the Viacom/UPN (top-four network/emerging network) example cannot be extrapolated to a situation in which a top-four network takes over another one (with which it directly competes), because, as admitted by Viacom, CBS and UPN do not compete for the same viewers *See* NAB/NASA Reply Comments at 59-60. NAB/NASA notes that in the 2001 Dual Network proceeding, Viacom argued that CBS did not really compete with UPN. Rather, it stated that its principal competition came from the broad-based traditional networks operated by ABC, NBC, and increasingly Fox NAB/NASA Comments at 77, citing Viacom's Comments to the *Notice of Proposed Rulemaking* in MM Docket No. 00-108, 15 FCC Rcd 11253 (2000) at 22. *See also* Fox Comments at 46, where Viacom states that "CBS and UPN have set their sights on entirely different demographics "

find in this proceeding that the market for diversity is local, not national.[1292] Further, as noted in the Policy Goals section above, we find that program diversity is best achieved by reliance on competition among delivery systems rather than by government regulation.[1293]

620. We are unable to conclude that the dual network rule can be justified on program diversity or viewpoint diversity grounds. Although we received conjectural statements regarding the repurposing of some programming, and stories of news operations being shared in a few markets, these reports do not evidence a systematic reduction in diversity as a result of media mergers. The record provides no evidence that, because some stations share news operations, viewpoint diversity is diminished. Further, even if a merger among ABC, CBS, or NBC would result in the loss of one weekday evening newscast, a substantial number of outlets that report national/international news would remain to provide diverse viewpoints throughout the day to the public.[1294] Finally, to the extent that we consider programming diversity an issue, the record provides no evidence that the repurposing of programming on different networks results in a diminution of program diversity. In fact, we found in the *Dual Network Order* that the repurposing of programming between two merged networks was likely to produce net benefits to viewers of network television.[1295]

3. Conclusion

621. Given the level of vertical integration of each of the top-four networks, as well as their continued operation as a "strategic group" in the national advertising market, a top-four network merger would give rise to competitive concerns that the merged firm would be able to reduce its program purchases and/or the price it pays for programming. These competitive harms would, in turn, harm viewers through reductions in program output, program choices, program quality, and innovation. We further conclude that a top-four network merger would harm localism by providing the networks with undue economic leverage over their affiliates, reducing the ability of affiliates to bargain with their network for favorable terms of affiliation, giving the networks greater power in program selection, and diminishing alternative choices of programming for affiliates. As a result, we conclude that the dual network rule remains necessary in the public interest to foster competition and localism.

VIII. MISCELLANEOUS REQUESTS

622 Numerous parties submitted comments on issues not specifically raised in the *Notice*. As discussed below, we dismiss most of these requests on procedural grounds because they fall outside the scope of this proceeding. We do not review the merits of these requests. To the extent appropriate, parties are free to re-file these requests as petitions for rulemakings. We deny others for the reasons discussed herein.

[1292] *See* Section VII(A), *supra*.

[1293] *See* Section III(A)(2), ¶ 37, *supra*

[1294] These outlets include cable news networks, daily and weekly newspapers, magazines, and the numerous news-related websites on the Internet. *See* Appendix B, listing all national news sources In any event, we question the assumption that a merger among ABC, CBS, or NBC would result in the elimination of a news department, particularly considering that each network currently attracts a substantial number of viewers to its weekday evening newscast.

[1295] *See Dual Network Order*, 16 FCC Rcd at 11124-25 ¶ 24.

A. Requests That Are Outside the Scope of the Proceeding

1. Proposed Behavioral Rules.

623. Several parties ask that we impose behavioral rules to achieve a number of alleged public interest goals. We invited comment in the *Notice* as to whether behavioral rules might render structural rules unnecessary to achieve our public interest goals of diversity, competition, and localism.[1296] The following proposals, however, relate to policy goals that are unrelated to those served by our structural rules and are therefore outside the scope of the *Notice*.

624. *TV Viewing*. TV Turnoff Network requests that we require all broadcast stations to run announcements reminding the viewing public that: (1) excessive television viewing has negative health, academic, and other consequences for children; and (2) parents and guardians retain and should exercise their First Amendment right and ability to turn off their television sets and limit their children's viewing time.[1297] We dismiss this request because it is outside the scope of this proceeding, which reviews our structural broadcast ownership rules pursuant to Section 202(h). Indeed, the goals sought to be advanced by the proposal bear no relation to diversity, competition, or localism.

625. *PEG*. Alliance requests that we promulgate behavioral regulations that guarantee public, educational, and governmental ("PEG") access on cable and direct broadcast satellite ("DBS") to ensure diversity of voices. Alliance argues that such federal regulations are necessary because PEG access is not mandated by federal legislation, but rather derives from a statute that allows local communities to regulate it.[1298] We dismiss Alliance's request as outside the scope of this proceeding and our authority, generally. The Commission once had access requirements of the type suggested by Alliance, but the Supreme Court struck them down as beyond our statutory authority.[1299] Section 611 of the Act, as amended by the Cable Communications Policy Act of 1984, states that franchising authorities may require operators to designate channel capacity for public, educational and governmental access use as part of their franchise agreement[1300] Congress did not authorize the Commission, however, to implement, enforce, or oversee the broad local access requirements advocated by Alliance.[1301] We note, however, that noncommercial educational television stations may request mandatory carriage on cable systems[1302] and also have satellite carriage rights in markets where DBS provides local-into-local service

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[1296] *Notice*, 17 FCC Rcd at 18520, 18521 ¶ 49.

[1297] TV-Turnoff Comments at 1-8.

[1298] Alliance Comments at 4-6. 47 U S.C § 542(c)(2)

[1299] *See FCC v Midwest Video Corp.*, 440 U.S 689 (1979) (authority to compel cable operators to provide common carriage of public-originated transmissions must come specifically from Congress). *Id* at 708.

[1300] 47 U S C. § 531.

[1301] Although DBS is required to set aside 4% of capacity for public interest ("non-commercial, educational, and informational") programming pursuant to Section 335 of the Act, we do not have authority to adopt the broader rights advocated 47 U.S C. § 335(b) and 47 C.F R. 25.701.

[1302] 47 U S C § 535

pursuant to the "carry-one-carry-all" requirements under Section 338 of the Act.[1303]

626. *Payola.* Future of Music Coalition alleges that a new form of payola exists in which record companies pay independent promoters to ensure that the companies' records are played on the radio. The independent promoters, Future of Music Coalition alleges, then establish exclusive relationships with radio stations and pay these radio stations a large portion of the money received from the record companies in the form of "promotional expenses." Future of Music Coalition asks that we ban this practice, thereby promoting diversity in radio programming.[1304] We dismiss Future of Music Coalition's request because it is outside the scope of the *Notice* and this proceeding.

2. Ownership Issues Outside the Scope of the Proceeding.

627. Some parties request action regarding ownership or attribution issues that were not raised in the *Notice* and that are therefore outside the scope of the proceeding.[1305] We dismiss these requests.

628. *Alien Ownership.* CanWest suggests that our biennial review of media ownership rules and the multilateral trade in services negotiations underway in the World Trade Organization provide a timely occasion to review foreign ownership rules for broadcasting.[1306] We decline to undertake such a review because it would be outside the scope of this proceeding. Moreover, to the extent that our foreign ownership regulations are statutorily based,[1307] we do not have the discretion to modify or repeal them in the biennial review process, pursuant to Section 202(h).

629. *Attribution.* MMTC asks us to expand this proceeding to include review of the attribution rules.[1308] We deny this request because, as we stated in the *Notice*, the attribution limits are not properly reviewed in the biennial review process,[1309] except for review of radio joint sales agreements ("JSAs"),

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[1303] 47 U.S C § 338.

[1304] Future of Music Coalition Comments at 91-92.

[1305] We decline to engage in a far reaching inquiry into possible harms in markets that are outside the Commission's jurisdiction or outside the scope of this proceeding. *See, e g*, Jennifer Poole Comments at 1-2 (arguing that consolidation will lead to a loss of pay and benefits for editorial writers).

[1306] CanWest Comments at 8-10.

[1307] 47 U.S C. § 310.

[1308] MMTC Dec. 9, 2002 Comments at 4.

[1309] The attribution rules do not themselves prohibit or restrict ownership of interests in any entity, but rather determine what interests are cognizable under the ownership rules The focus of the biennial review process is whether the ownership rules are necessary in the public interest as a result of competition. The attribution limits are set at the level the Commission believes conveys influence or control and, as these limits are not related to any changes in competitive forces, they are not reviewed biennially. *Notice* at n.13. *See 1998 Biennial NOI*, 13 FCC Rcd at 11280 ¶ 10.

which we address in the Local Radio Ownership section above.[1310]

630. *LPFM.* REC Networks requests that we refrain from changing our Low Power FM ("LPFM") rules relating to ownership caps and assignment of stations because these rules are consistent with our intentions in establishing LPFM.[1311] LPFM ownership and assignment rules are addressed in Sections 73.855, 73.858, 73.860, and 73.865 of the Commission's rules, adopted in 2000,[1312] and are not addressed in the context of this proceeding. These are non-commercial stations and therefore a consideration of ownership limits for these stations is outside the scope of this proceeding. REC also asks that we impose new ownership restrictions on non-commercial educational stations. We dismiss that request as such limits are outside the scope of this proceeding.

631. *Broadcast Auction Process.* Hodson recommends that we modify the new entrant bidding credit in the broadcast auction process from the current percentages of 25 percent and 35 percent to 30 percent and 45 percent. Hodson also recommends, in its proposed 30 percent tier, that we allow an attributable interest in five mass media facilities nationwide instead of the current three, with the condition that the winning bidder has no attributable interest in a broadcast presence already in the market the proposed broadcast station intends to serve. Finally, for entities eligible for Hodson's proposed 45 percent tier, Hodson recommends that we establish a relaxed payment plan for the winning bid balance that would include an extended payment schedule.[1313] Hodson's proposals go to our broadcast auction rules and process, not our ownership rules. These proposals are not a logical outgrowth of the *Notice* and they are therefore outside the scope of this proceeding.[1314]

3. Translator/Spectrum Issues Outside the Scope.

632. REC also makes other requests involving our rules applying to use of translators. REC claims that the current rules allow distant translators and discourage establishment of new local LPFM stations[1315] Nickolas Leggett asks that we provide alternative opportunities to small broadcasters including: (1) a frequency band for manually operated low-power commercial broadcasters; (2) a citizens

[1310] As addressed more fully in our Local Radio Ownership section above, in 2001, we sought comment on whether JSAs should be attributable. *See Local Radio Ownership NPRM*, 16 FCC Rcd at 19894 ¶¶ 82, 83. That NPRM was incorporated into this proceeding.

[1311] REC Networks Comments at 2-4

[1312] 47 C.F R §§ 73.855, 73.858, 73 860, 73.865. *See Creation of Low Power Radio Service*, 15 FCC Rcd 2205 (2000)

[1313] Hodson Reply Comments at 75-81; Hodson IRFA Comments, MM Dkt. No. 01-317, MM Dkt. No 00-244, Feb. 28, 2002 at VII.

[1314] We addressed the broadcast auction process in a prior rulemaking proceeding In 1998, the Commission determined that it would fulfill its obligations under Section 309(j) of the Communications Act of 1934, 47 U S.C § 309(j)(3)(B), to promote economic opportunity and competition for designated entities, including small businesses, by providing new entrant bidding credits *Implementation of Section 309(j) of the Communications Act -- Competitive Bidding for Commercial Broadcast and Instructional Television Fixed Service Licenses, First Report and Order*, 13 FCC Rcd 15920, 15992-97 (1998), *granted in part and denied in part*, 14 FCC Rcd 8724 (1999), *amended by* 14 FCC Rcd 14521 (1999). Changes to these bidding credits would require a separate rule making.

[1315] REC Networks Comments at 2-4

broadcasting band; and (3) open-microphone neighborhood broadcasting supported by the consolidated broadcasters [1316] We deny these requests that we change our translator rules or afford spectrum to small broadcasters because they are outside the scope of the proceeding.

B. Proposals Addressed in Other Commission Proceedings.

633. *Cable Ownership.* CCC requests that we retain our 30% national cable system ownership limits.[1317] We dismiss CCC's request because it is outside the scope of this proceeding and it relates to an issue that is the subject of a separate rulemaking.[1318]

634. *DTV.* USCCB asks us to promulgate regulations that define digital television ("DTV") broadcasters' public interest obligations.[1319] We dismiss USCCB's request because it is outside the scope of this proceeding. CST requests that we amend or eliminate any of our rules that hinder the digital conversion of broadcasters, cable systems, and telephone systems, and that we establish regulatory policies to encourage the introduction of digital technologies.[1320] We dismiss CST's requests because they are outside the scope of this proceeding.[1321] Further, CST proposes that all broadcast licensees and cable systems that expand their operations as a result of rule relaxations be required to loan a percentage of their expansion revenues to a Digital Conversion Fund.[1322] We decline to adopt CST's proposal because there is no basis for the Commission to directly fund industry's transition to digital television. When Congress established the framework for the digital television transition in the Telecommunications Act of 1996, it gave no indication that the Commission should directly fund industry transition costs for digital television Even if CST's proposal fell within Congress's directives, the establishment of such a fund raises extraordinarily complex and controversial issues such as the measurement by the Commission of 'merger efficiencies' and how the fund would be administered. CST provides us with no meaningful basis to assess the viability or effectiveness of such a program Finally, as explained in Section VI above, the Commission already has considered the relationship between local television consolidation

[1316] Nickolas Leggett Oct. 28, 2002 Comments at 5.

[1317] CCC Comments at 24.

[1318] *See Implementation of Section 11 of the Cable Television Consumer Protection and Competition Act of 1992*, 16 FCC Rcd 17312 (2001).

[1319] USCCB Reply Comments at 1-13.

[1320] CST Reply Comments at 4-5

[1321] The Commission is undertaking a second periodic review of the progress of the transition to DTV. *See Second Periodic Review of the Commission's Rules and Policies Affecting the Conversion to Digital Television*, 18 FCC Rcd 1279 (2003) This *Notice of Proposed Rulemaking* seeks additional comment from the public to refresh the record in three outstanding DTV public interest rulemaking proceedings: *Notice of Inquiry, Public Interest Obligations of TV Broadcast Licensees*, 14 FCC Rcd 21633 (1999); *Notice of Proposed Rule Making, Standardized and Enhanced Disclosure Requirements for Television Broadcast Licensee Public Interest Obligations*, 15 FCC Rcd 19816 (2000), and *Notice of Proposed Rule Making, Children's Television Obligations of Digital Television Broadcasters*, 15 FCC Rcd 22946 (2000). The second DTV periodic review *Notice of Proposed Rule Making* also seeks comment on a large number of issues related to the progress of the DTV transition and steps the Commission could take to facilitate the transition.

[1322] CST Reply Comments at 7

and the transition to digital television. We determined that the efficiencies from relaxing the local television ownership limit would likely promote the transition to digital television.

C. Requests That We Delay the Proceeding or Seek Further Information

635. Some parties ask us to undertake additional studies or delay taking action until after some future events.[1323] We decline to delay action in this proceeding. Our statutory obligation is to review the rules biennially; we have no discretion to willfully deviate from that schedule.

636. *IBOC-DAB.* VCPP requests that there be no relaxation on ownership restrictions until several years after 100% rollout of In Band On Channel Digital Audio Broadcasting ("IBOC-DAB"), arguing that this technology will destroy competition.[1324] We deny VCPP's request. The courts require us to base our ownership decisions on today's marketplace and the facts presently before us. We are not free to adopt a "wait and see" approach.[1325] The impact of IBOC-DAB on diversity, competition, and localism in local media markets will be accounted for in future biennial reviews.

637 SBA asks us to issue a Further Notice of Proposed Rulemaking in this proceeding, claiming the *Notice* is not specific enough to comply with the Administrative Procedure Act or the Regulatory Flexibility Act.[1326] We disagree with SBA and deny its request. Contrary to the implication of SBA, the actual rules at issue in this proceeding are specifically identified in the *Notice* and well known to all interested parties – they are our current broadcast ownership rules. Congress has directed us to review those rules every two years to determine whether those exact rules remain necessary in the public interest. That we have done in this proceeding in accordance with the *Notice*. Further, Congress directed the Commission to eliminate or modify any of its broadcast ownership rules that no longer are necessary Again, it was explicit in the *Notice* that we might eliminate any rule that could not be justified in light of the current media marketplace. To the extent that we have eliminated rules herein, therefore, there has been no failure of notice. With respect to those rules that, having been found unnecessary, have been modified herein, the question is the familiar one – were the modifications a "logical outgrowth" of the issues identified in the *Notice*. We conclude that this *Order* and its accompanying rules are a logical outgrowth of the questions posed in the *Notice*. The modifications made herein are consistent with the

[1323] MMTC filed a motion requesting that we postpone our vote on this *Order* MMTC argues that because our Electronic Comment Filing System ("ECFS") was overloaded with filings immediately prior to our June 2, 2003 vote, the record does not accurately reflect all comments received in this proceeding and, therefore, parties are unable to respond to the complete record MMTC Motion for a Brief Postponement of the Vote (May 31, 2003) We deny the motion. The Reply Comment period closed Feb. 3, 2003, more than four months ago Nonetheless, in the interests of assembling a full record, the Commission has continued to accept comments, and more than 500,000 comments were filed in this proceeding, many of which were filed at the last minute. Given the large volume of last minute filings, it is inevitable that a small percentage would not be placed on our ECFS system or be available in the public reference room in sufficient time for replies Nonetheless, the record is complete, and MMTC's failure to file its comments or requests in a timely fashion is no excuse to delay the proceeding. Nickolas Leggett asks us to engage in detailed political science analysis of the impact of removal of ownership caps on the legitimacy of government and business Nickolas Leggett Nov 15, 2002 Comments at 4 We deny this request because it is unclear.

[1324] VCPP Comments at 1-2

[1325] *Fox Television*, 280 F.3d at 1042.

[1326] SBA March 13, 2002 Comments at 2-5; SBA April 9, 2003 Comments at 3-5.

issues and questions posed in the *Notice*, and take account of the full record in this proceeding. Finally, we take seriously the mandate of Section 202(h) to review our broadcast ownership rules every two years. It would be impractical to complete such a Herculean task, in this case, to review six different rules, and to complete that review in time to start another review, if we issued a separate notice detailing modifications to rules and initiated another comment period.

638. Children Now asks that we reserve our decision-making on media ownership until its research on the effects of media consolidation on children is complete and can be incorporated into our record.[1327] Laura Smith requests that we expand the scope of our public hearings on media ownership and that we conduct additional research before concluding this proceeding.[1328] We decline to further delay this proceeding. The public, industry, and government agencies alike have an interest in finality, economy, and the avoidance of unnecessary delay. The public is not served by bureaucratic inaction; industries suffer when rules that restrain behavior without cause continue in force; and agencies fail in their responsibility when they commit public resources to meaningless exercises of no decisional significance. As a corollary, agencies should not refrain from acting on an issue once a robust record has been developed. It is the agency's responsibility, in the first instance, to determine when that point has been reached.[1329]

639. In this case, we see no overriding need to augment the record, nor do we believe that the expenditure of additional time and resources in an effort to do so will provide us with a significantly more accurate or current assessment of the media markets. To the contrary, the record in the current proceeding is one of the most factually complete and thorough ever assembled in a Commission rulemaking In addition, the court in *Fox Television* made it quite clear that regulatory delay in the biennial ownership review process is causing hardship to the parties and should not be tolerated.[1330] Accordingly, we deny the requests of Children Now and Laura Smith.[1331]

D. Independent Producers.

640. *Independent Production Rules* The Coalition for Program Diversity ("CPD") asks us to take "content neutral action" by "adopting a 25% Independent Producer Rule that will insure [*sic*] that the prime time programming aired by the four networks is as diverse as possible."[1332] In a similar vein,

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[1327] Children Now Comments at 1-2 Also, on May 21, 2003, Children Now issued a study finding that, in the Los Angeles, California DMA, the number of hours of children's programming aired by television broadcast stations decreased by more than 50% between 1998 and 2003, and that the largest decreases in programming hours occurred at commonly owned stations. *See* Section VI *supra* for a discussion. *Children Now Report* 2, 5-6, 9

[1328] Laura Smith Reply Comments at 27-33

[1329] *United States v FCC*, 652 F.2d 72, 90-91 (D.C Cir. 1980) (en banc) ("Someone must decide when enough data is enough In the first instance that decision must be made by the Commission . . . To allow others to force the Commission to conduct further evidentiary inquiry would be to arm interested parties with a potent instrument for delay.").

[1330] *Fox Television*, 280 F.3d at 1039 ("retention of the Rules in the interim significantly harms both the networks and Time Warner").

[1331] We address other requests of Children Now *supra*

[1332] CPD Comments at i, 8-10, 34-37, Reply Comments of CPD at 9; *see also* Malla Pollack Comments at 2.

the Writers' Guild of America ("WGA") proposes a requirement that broadcast and cable national program services purchase at least 50 percent of the entertainment for their prime time schedules from independent producers.[1333] In essence, CPD and WGA ask us to re-impose some version of our prior financial interest/syndication rules, first adopted by the Commission in 1970.[1334] We reject these requests (collectively, the "Fin/Syn Proposals").

641. To begin with, there is substantial doubt as to whether we have adequate notice to adopt the Fin/Syn Proposals. In the *Notice*, we invited comment on, among other issues, whether diversity could be better promoted by alternatives to structural regulation, such as behavioral requirements and, if so, what behavioral requirements would be recommended.[1335] The Commission also sought comment on whether "the effects of the 1996 change in the national ownership cap [can] be separated from the effects of the repeal of the fin/syn and [prime time access] rules?" The Commission asked commenters to identify those effects.[1336]

642. Although we invited comment as to whether we should, in lieu of structural rules, adopt behavioral rules to serve our public interest goals, we did not propose a re-imposition of the fin/syn rules, or anything related. The Fin/Syn Proposals, therefore, are not squarely within the four corners of our *Notice*. Moreover, to the extent that we asked general questions about the effect of the repeal of our former fin/syn rules, or whether some behavioral rules might obviate structural regulation, we did not intend, nor do we think the *Notice* can be fairly read to suggest, that a fin/syn overlay would or could substitute for structural regulation as a means of protecting our desiderata -- localism, competition, and diversity Accordingly, we do not believe that the Fin/Syn Proposals are responsive to the *Notice*, or that the adoption of such rules could be thought to be a logical outgrowth of the *Notice*.

643. In any event, we are not inclined to adopt the Fyn/Syn Proposals. The original fin/syn rules prohibited a television network (defined at the time to include only ABC, NBC, and CBS) from syndicating television programming in the U.S., or from syndicating outside the U S. programming for which it was not the sole producer, or from having any option or right to share in the revenues from domestic or foreign syndication. These rules also prohibited a network from acquiring any financial or proprietary right or interest in the exhibition, distribution, or other commercial use of television programming produced by someone other than the network for distribution on non-network stations.[1337] In 1983, the Commission proposed repealing the rules based on, *inter alia*: (i) a 44% increase in the number of TV stations available to the average viewer since 1970; (ii) the dramatic increase in the availability of cable television, and (iii) evidence of vigorous competition among the television networks.[1338]

[1333] Joint Comments of Writers Guild of America, et al , at 3

[1334] Ex Parte Filing of ABC, Disney, FOX, NBC, Viacom (Apr 29, 2003) at 1 (referencing *Amendment of Part 73 of the Commission's Rules and Regulations with Respect to Competition and Responsibility in Network Television Broadcasting*, 23 F.C.C.2d 382 (1970))

[1335] *Notice,* 17 FCC Rcd at 18520-21 ¶ 49.

[1336] *Id.* ¶ 141.

[1337] *Schurz Communications, Inc*, 982 F 2d at 1045

[1338] *Amendment of the Syndication and Financial Interest Rules,* 94 F C.C 2d 1019, 1057-63 (1983)

644. In 1991, however, the Commission opted not to repeal the rules, but instead modified them. Among other things, the Commission imposed a new restriction on networks, which provided that "no more than 40 percent of a network's own prime-time entertainment schedule may consist of programs produced by the network itself."[1339] In 1992, the U.S. Court of Appeals for the Seventh Circuit vacated the rules.[1340] The Court criticized the Commission for not addressing earlier Commission findings, in 1983, that the networks lacked significant market power. The Court found that the development of cable, video recorders, and the advent of the Fox network buttressed the earlier findings.[1341]

645. In the proceedings on remand, the Commission decided to repeal, on a graduated basis, most of its fin/syn rules.[1342] In repealing the 40 percent cap, the Commission observed that the cap does not necessarily foster diversity.[1343] The Commission also noted that "the decline in network audience share, which largely explained the rule's relaxation in 1991, has continued unabated."[1344] On appeal, the Seventh Circuit affirmed that decision, stating that if the Commission ever decided to re-impose similar fin/syn restrictions on the networks, "it had better have an excellent, a compelling reason" to do so.[1345]

646. In 1995, the Commission removed the remaining fin/syn restrictions, finding that there was no "clear trend toward increased network ownership of [prime time entertainment programming] that is attributable to the relaxation of our fin/syn rules or that constitutes a cause for concern from a public interest standpoint."[1346] At the time, independent producers provided 80.97% of the prime time programming hours for ABC, CBS and NBC.[1347] Although there had been a decline in the number of packagers of programming included in the prime time schedules for ABC, CBS and NBC, the Commission believed that the decline could not be attributed to elimination of the fin/syn rules, but was "instead attributable to the inherent riskiness of prime time programming."[1348] Moreover, ABC, CBS, and NBC faced more, rather than less, competition in broadcast television due to the emergence of FOX and two additional broadcast networks (United Paramount and Warner Brothers).[1349] The Commission also reaffirmed its finding in 1993 that alternative video delivery systems, such as DBS and wireless

[1339] *Schurz Communications*, 982 F.2d at 1046.

[1340] *Id* at 1055

[1341] *Id.* at 1046, 1053.

[1342] *Evaluation of the Syndication and Financial Interest Rules,* 8 FCC Rcd 3282 (1993)

[1343] *Id.* at 3299 ¶ 38.

[1344] *Id* at 3303 ¶ 44

[1345] *Capital Cities/ABC, Inc v FCC*, 29 F.3d 309, 316 (7th Cir 1994).

[1346] *Review of the Syndication and Financial Interest Rules,* 10 FCC Rcd 12165 ¶ 21 (1995).

[1347] *Id.*

[1348] *Id.* at 12169 ¶ 20

[1349] *Id.* at 12170 ¶ 26.

cable, provided sufficient competition to the broadcast networks to obviate fin/syn restrictions [1350]

647. CPD now argues that, despite the growth of cable and DBS providers in the video programming distribution market, there still is a strong public interest supporting limitations on network programming because 43 million consumers receive only broadcast network television.[1351] CPD also points out that in 1992, 66.4 percent of the networks' prime time schedule consisted of programs produced and owned by independent producers. Today, they argue, only 24 percent of the four largest networks' prime time schedule is supplied by independent producers.[1352] CPD argues that the Commission should preserve 25 percent of the networks' prime time schedule for independent producers.

648. WGA asks that the Commission "adopt measures designed to insure [*sic*] that national program services on broadcast and cable television purchase at least 50% of their prime time programming from independent producers."[1353] WGA contends that consolidation in the market for video programming makes any appearance of diversity a mirage. Although there are 230 national cable programming networks, according to WGA, there are just 91 networks that can be considered major networks (defined by WGA as available in more than 16 million homes). Of these 91 networks, 80 percent (73) are owned or co-owned by 6 entities: AOL Time Warner, Viacom, Liberty Media, NBC, Disney and News Corporation.[1354]

649. Four major networks (ABC, CBS, FOX, and NBC, collectively the "Networks") filed a joint ex parte pleading opposing any cap on the amount of network programming a network may air during prime time. The Networks invoke much of the rationale that the Seventh Circuit used when it vacated the Commission's prior fin/syn rules.[1355] To those arguments, the Networks add that the broadcast networks' prime time audience share has dropped from 72 percent in 1993-1994 to 58.9 in 2001-2002.[1356] The Networks assert that CPD's argument ignores the fact that, whereas there were only three broadcast networks in 1970 when the Commission first adopted the fin/syn rules, there are now seven networks providing English language programming.[1357] The Networks also argue that the growth in use of the DVD player, personal video recorder, and the Internet continues to add to the diversity in video programming and continues to undermine any rationale for fin/syn rules.[1358] Even accepting WGA's assertion that six companies own many of the major cable networks, the Networks argue that the market for video programming is more diverse today because six is double the number of companies that owned

[1350] *Id* at 12171 ¶ 27.

[1351] CPD Reply Comments at 2.

[1352] *Id* at 4

[1353] WGA Comments at 3.

[1354] *Id.* at 10

[1355] ABC, NBC, Disney, Fox and Viacom Apr 29, 2003 Ex Parte at 2-3.

[1356] *Id.* at 2-5

[1357] *Id.* at 2-8.

[1358] *Id.* at 2-7.

broadcast networks when the fin/syn rules were adopted.[1359]

650. Although CPD and WGA appear to be correct that fewer of the programs in the Networks' prime-time lineup are produced by independent producers than at times in the past, the evidence in the record does not address whether the decline in the number of independently-produced programs is attributable to changes in the regulatory environment (*i.e.*, the elimination of the fin/syn rules) or to other changes that have taken place in the media business in the intervening years that have increased the risk of producing prime time programming.[1360]

651. Moreover, the reduction in independently produced prime time programming on a small subset of television networks is not, by itself, a public interest harm. Our concern is to promote the interests of consumers and viewers, not to protect the financial interests of independent producers. The record does not demonstrate that consumers and viewers are harmed as a result of network financial interests in the programming they carry, particularly in light of the quantity and variety of media outlets for programming in today's media marketplace.

652. In particular, the record does not convince us that an "access" rule for independent producers will advance viewpoint diversity. CPD's argument, for example, is premised on the notion that the Networks are gatekeepers;[1361] if they are not, there are other outlets for independently-produced fare and no basis to impose fin/syn restrictions To the extent that the Networks actually are gatekeepers, however, fin/syn rules cannot logically advance viewpoint diversity because the Networks, as gatekeepers, can filter messages at the distribution stage just as they can at the production stage. Adopting the Fin/Syn Proposals, therefore, is not likely to promote viewpoint diversity

653. Even if we were to adopt a broader definition of "diversity" to include general entertainment programming,[1362] a gatekeeper at distribution still may filter unwanted programming whether or not the programming is produced in-house. For example, if a network were to decide that its prime time lineup should consist only of "reality programming," or that it should target a particular audience demographic, there is no reason to believe that it could not give effect to those plans with independently-produced programming as easily as it could with programming produced by itself or an affiliated company – it simply would make known its programming intent and allow independent producers to fill the void. The Fin/Syn Proposals, therefore, cannot be justified on grounds of programming diversity.

[1359] *Id.*

[1360] "Whatever the pros and cons of the original financial interest and syndication rules, in the years since they were promulgated the structure of the television industry has changed profoundly." *Schurz Communications*, 982 F.2d at 1046 The Commission previously has questioned whether changes in the mix of programming on the prime time lineup can be attributed to regulatory changes or to business considerations. *See Review of the Syndication and Financial Interest Rules,* 10 FCC Rcd 12165 ¶ 20 (1995).

[1361] Ex Parte Filing of CPD (May 15, 2003) at 2.

[1362] Although CPD premised its proposal on the goals of promoting both source diversity and program diversity, its main arguments appear to be premised on a program diversity rationale. *See, e g*, CPD Reply Comments at 20 (arguing that its proposal would "substantially increase the possibility that more diverse genres of programming will emerge"). As discussed above, our core interest in this proceeding is in protecting viewpoint diversity; we generally rely upon market forces to deliver programming that will appeal to viewers.

654. Both CPD and WGA also fail to justify their definitions of the relevant market for purposes of their proposals. CPD, for example, has targeted its proposal only at the four major broadcast networks, and only at their prime time schedule However, aside from conclusory allegations that "the prime time television programming marketplace is a narrow, unique market,"[1363] CPD has provided no reason to exclude other video programming outlets and other day-times, were we inclined to adopt a fin/syn-like rule. Viewers today have more programming choices available to them over-the-air, through cable, satellite, or home video, than ever before.[1364] Indeed, WGA considers a much larger market for these purposes (although it, too, provides little in the way of support for its market definition), and other commenters have suggested that non-prime time broadcast hours should be included in any analysis relating to programming diversity[1365] Lacking the foundation of a sustainable market definition, the Fin/Syn Proposals cannot stand.[1366]

655. Finally, to the extent that the Fin/Syn Proposals are based on an assertion that the quality of independently-produced entertainment programming is superior to that of the Networks,[1367] we find the record devoid of evidence to that effect.[1368] We have no means or methodology to measure the quality of entertainment programming, and were we to favor one type or genre of programming over another, we would run squarely into the teeth of the First Amendment.[1369] It is up to consumers and viewers to determine what programming they want to watch, and networks, as they compete for viewers, must be responsive to those demands. It is not for this agency to intervene in the decisions that determine the content of programming (absent obscenity or indecency concerns)

656. When the Seventh Circuit affirmed the Commission's decision repealing all of the fin/syn rules, it questioned whether the rules "ever had much basis" and cautioned that, if the Commission ever decided to re-impose similar restrictions, "it had better have an excellent, a compelling reason" to do so.[1370] None appears on this record. Accordingly, we reject the Fin/Syn Proposals.[1371]

[1363] CPD Comments at 3-4.

[1364] *See* Joint Comments, Bruce M. Owen and Michael G. Baumann, Economic Study E, *Concentration Among National Purchasers of Video Entertainment Programming*, at 2.

[1365] NASA Comments at 63-64 (arguing that the 35% national cap should be retained to promote programming diversity during non-prime time).

[1366] *See Review of the Syndication and Financial Interest Rules*, 10 FCC Rcd at 12171 ¶ 27 (concluding that the fin/syn rules focused too narrowly on the broadcast networks to the exclusion of other distribution channels).

[1367] *E g*, CPD Reply Comments at i, 6, 13, WGA Comments at 10.

[1368] *Cf* MOWG Study No. 5, Program Diversity and the Program Selection Process on Broadcast Network Television by Mara Einstein (Sept. 2002).

[1369] To be considered content-neutral, regulations must have neutral means and ends. *See News America Publishing, Inc v FCC*, 844 F.2d 800 (D C Cir 1988) (strict scrutiny applied to structural regulations that had a direct effect on content and viewpoint), *Lutheran Church-Missouri Synod v FCC*, 141 F.3d 344, 354 (D C. Cir. 1998) (invalidating EEO regulations under strict scrutiny to the extent that they would implicate programming content)

[1370] *Capital Cities/ABC, Inc v. FCC*, 29 F 3d 309, 316 (7th Cir 1994)