WHEN "YES" MEANS NO: THE SUBJUGATION OF COMPETITION AND CONSUMER CHOICE BY EXCLUSIVE MUNICIPAL CABLE FRANCHISES

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INTRODUCTION

Cable television subscribers are plagued by regulations that prohibit consumer choice in selecting an individual cable television provider. The effects of these regulations are widespread because cable television has become a common fixture in many American households.[1] The regulations have been embedded in the industry since the introduction of cable television in 1948[2] and have taken many forms.[3] Initially, the government imposed regulations primarily due to the competitive effects that cable television had on local television stations.[4] As the technology developed and became more commonplace, the regulations evolved in a manner all their own.[5]

Classification of the cable television industry as a natural

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[1] A study sponsored by the Cable & Telecommunications Association for Marketing showed nearly two out of every three U.S. households had access to cable television. National Cable & Telecommunications Association, *The History of Cable Television*, *at* http://www.ncta.com (last visited Sept. 17, 2003).

[2] *Id.* "Cable television originated in the United States almost simultaneously in Arkansas, Oregon and Pennsylvania in 1948 to enhance poor reception of over-the-air television signals in mountainous or geographically remote areas." *Id.*

[3] *See infra* Part II (discussing The Communications Act of 1934 [hereinafter Communications Act], the Cable Communications Policy Act of 1984 [hereinafter 1984 Act], the Cable Television Consumer Protection and Competition Act of 1992 [hereinafter 1992 Act], and the Telecommunications Act of 1996 [hereinafter 1996 Act]).

[4] *See* National Cable & Telecommunications Association, *supra* note 1. The FCC responded to concerns from the broadcast industry by "expand[ing] its jurisdiction and plac[ing] restrictions on the ability of cable systems to import distant television signals." *Id.*

[5] The FCC restrictions led to "a 'freeze' effect on the development of cable systems in major markets, lasting into the early [19]70s." *Id.* *See infra* Part II (discussing the interplay between federal and local regulations).

monopoly stifles consumer choice.[6] Natural monopoly status creates an incentive for municipalities to award exclusive franchises to cable television providers. This status allegedly results in greater efficiencies for the industry[7] and increased revenue for the municipality.[8] Despite the supposed benefits of a natural monopoly, the lack of competition, in addition to hindering consumer choice, frequently leads to poor service.[9]

Competition is the current driving force behind technological change in the cable television industry.[10] The goal of competition is to make cable television the source for distributing digital sound, video, voice, and data communications to homes and offices.[11] Although the Telecommunications Act of 1996 ("1996 Act")[12] deregulated a wide array of sectors within the telecommunications industry,[13] the task of deregulating the cable industry remains incomplete.[14]

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[6] *See infra* Part I (examining the economic principles behind natural monopolies).

[7] *See* STEVEN E. LANDSBURG, PRICE THEORY & APPLICATIONS 356 (4th ed. 1999) (explaining that under conditions of natural monopoly, the firm's average cost curve is decreasing at the point it crosses market demand, so the firm could only survive if it is monopolized).

[8] Daniel E. Brenner, *Was Cable Television a Monopoly?*, 42 FED. COMM. L.J. 365, 399 (1990). "Among the benefits [provided to the community by the monopoly cable provider] was the cable franchise fee extracted from operators. The cable franchise fee is a charge made by a local or state government to pay for the cost of regulation." *Id.*

[9] Luis Puga, *Lawmakers Hear Cable Complaints, Question BPU*, PRESS OF ATLANTIC CITY, Nov. 22, 2002, *available at* http://www.pressofatlanticcity.com. Members of the New Jersey General Assembly Telecommunications and Utilities Committee questioned the practices of the state Board of Public Utilities oversight of the cable television industry after the Board received 19,633 complaints from customers during 2002, up from 13,617 in 2001. *Id.* "The complaints included rising bills in the expanded-basic service, poor reception, poor service, inaccurate billing and channels that subscribers don't want to pay for." *Id.*

[10] *Cable TV: Advanced Technologies*, Jones Telecommunications & Multimedia Encyclopedia, *at* http://www.digitalcentury.com/encyclo/update/catvtech.html (last visited Oct. 3, 2002).

[11] *Id.*

[12] Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (1996) (codified in scattered sections of 47 U.S.C.). *See infra* Part II (discussing the 1996 Act's impact on the cable industry).

[13] *Id.* The 1996 Act eliminated regulatory barriers and encouraged competition in nearly every sector of the communications landscape. Richard E. Wiley, *The Telecommunications Act of 1996*, *at* http://www.fed-soc.org/Publications/practicegroupnewsletters/telecommunications (last visited Aug. 28, 2002).

[14] *See infra* Part II (discussing the implications of "effective competition"); *Telecommunications Act of 1996*, Jones Telecommunications & Multimedia Encyclopedia [hereinafter Jones], *at* http://www.digitalcentury.com/encyclo/update/telcom1.html (last visited Oct. 3, 2002) (referencing the 1996 Act's

The recently settled[15] action between the Yankees Entertainment & Sports Network, LLC[16] ("YES") and Cablevision Systems Corporation ("Cablevision") provides a current example of the problems associated with exclusive franchises. Until the settlement, Cablevision refused to carry YES.[17] Cablevision customers were unable to switch to another cable provider in an attempt to receive YES because of the insurmountable impediment that exclusive franchises had created. The dispute between YES and Cablevision highlights the juxtaposition of a government-sanctioned monopoly in a free market economy. Consumer choice is sacrificed under monopoly conditions in favor of protecting a firm that presumably cannot survive under competitive pricing.[18]

This Comment analyzes the classification of the cable television industry as a natural monopoly, evaluates the consequences such a classification has on the regulatory scheme imposed on the industry, and reveals the viability of introducing competition into the industry. Part I provides a background of the economic concepts discussed throughout this Comment, such as natural monopolies and monopoly pricing. This section also discusses current events that have brought renewed relevance to this topic, in particular, the dispute between YES and Cablevision. Part II contemplates whether natural monopolies create the need for regulations or whether the regulations create natural monopolies. The checkered regulatory history of cable television demonstrates how uncertainty regarding cable television's role in society influenced initial congressional decision making. Similar trepidation hampered state and local governments when they gained jurisdiction over cable television and continue to plague the industry today.

Part III examines the rationale for the characterization of the

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consideration of satellite television as not being effective competition for cable systems, thus precluding those systems that compete with satellite providers from deregulation).

[15] Richard Sandomir, *Cablevision Agrees to Carry the YES Network*, N.Y. TIMES, Mar. 13, 2003, at D1 [hereinafter Sandomir I]. The YES Network and Cablevision reached an agreement on March 12, 2003 "with a one-year deal that will make the network's Yankees and Nets games available to Cablevision's nearly three million subscribers in the Bronx, Brooklyn, Westchester, New Jersey and Connecticut, starting March 31." *Id.* That agreement subsequently broke down, but New York State Attorney General Eliot Spitzer brokered the final one-year agreement in time for the start of the Yankees' season on March 31. Richard Sandomir, *Cablevision and YES Reach Agreement*, N.Y. TIMES, Apr. 1, 2003, at S2 [hereinafter Sandomir II].

[16] Complaint, Yankees Entm't & Sports Network, LLC v. Cablevision Sys. Corp. and CSC Holdings, Inc. (S.D.N.Y. 2002) (No. 02-CV-3242) [hereinafter *Yankees*].

[17] Sandomir I, *supra* note 15, at D4.

[18] *See* LANDSBURG, *supra* note 7, at 356-57.

cable television industry as a natural monopoly in the first place. The novelty of the technology was a significant factor at the time of the introduction of cable television because of the lack of suppliers and expertise. With those hurdles long since surpassed, the logic supporting cable television's classification no longer prevails. As a result, the classification must be modified.

Part IV presents examples of how the classification of industries as natural monopolies often suppresses consumer choice regarding rates and service. Although this Comment specifically targets the cable television industry, the effects are common throughout many industries providing typical household utilities.[19] Given the negative effects of natural monopolies, protecting a particular supplier cannot be the ideal solution when alternatives, such as a competitive market, exist for the video marketplace.

This Comment concludes that an obvious alternative arising from the core tenets of the American free-market system[20] is to remove the regulatory framework that grants exclusive franchises in the cable television industry and to permit true competition throughout the video marketplace. Economists have long lauded competition as the most effective means of preserving consumer choice.[21] Although the introduction of direct broadcast satellite ("DBS") television has added an element of competition to the video marketplace, the administrative component of purchasing DBS service is not yet at a level comparable to free market choice[22] to consider it a viable alternative. Even though it is not a perfect substitute, DBS has opened the door to the possibility of true competition, such as having two or more cable television providers in a single municipality, finally breaking the local cable monopoly. The emergence of a viable competitor to cable television supports the

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[19] Alexandra I. Metzner, *Were California's Electricity Price Shocks Nothing More Than a New Form of Stranded Costs?*, 52 AM. U. L. REV. 535, 536 (2002). California's electricity system suffered because it "was weak and was not properly servicing demand or maintaining sufficient electricity reserves; this was attributable to both wholesalers' lack of motivation to cut costs . . . and to the industry's function as a natural monopoly." *Id.* at 536 n.7.

[20] MARK S. MASSEL, COMPETITION AND MONOPOLY—LEGAL AND ECONOMIC ISSUES 16-17 (1962).

[21] *See, e.g.*, JOHN MAURICE CLARK, COMPETITION AS A DYNAMIC PROCESS 9-18 (1961); ANDREAS G. PAPANDREOU & JOHN T. WHEELER, COMPETITION AND ITS REGULATION 3-8 (1954).

[22] A 2002 industry estimate showed cable subscribership at approximately sixty-five million households and DBS subscribership at twenty million households. Ronald Grover & Tom Lowry, *As Satellite Dishes It Out, Cable TV Fights Back*, BUS. WK., Jan. 13, 2002, at 40.

idea of removing the last remnant of regulation in the video marketplace by eliminating exclusive municipal cable franchises.

I. BACKGROUND

A. *Relevant Legal and Factual Background*

On April 29, 2002, YES filed a complaint in the United States District Court for the Southern District of New York[23] against Cablevision in an attempt to compel Cablevision to carry all New York Yankees games that YES broadcasts.[24] Cablevision is the largest cable provider in the greater New York metropolitan area[25] ("region"), with customers in nearly one million subscriber households in New Jersey[26] and over three million subscriber households in the region overall.[27] The complaint alleged that Cablevision abused its monopoly power over the cable television market in the region,[28] protecting its own regional sports networks at the expense of the fledgling YES network.[29]

Cablevision is the majority owner and manager of the Madison Square Garden Network ("MSG") and Fox Sports New York ("FSNY").[30] The YES complaint alleged that prior to the creation of YES in 2001, MSG and FSNY were the only networks in the region "primarily devoted to providing live broadcasts of local professional teams and other sports programming of particular interest to greater New York metropolitan area sports fans."[31] Cablevision carried MSG and FSNY on its own systems and sold the channels to other cable systems in the region.[32] With the creation of YES, and the resulting competition in the local sports market, Cablevision refused to carry YES although it had always sold its own channels to other cable systems.[33] The agreements between YES and other cable providers included paying YES a monthly fee of $2 per subscriber to carry the

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[23] *Yankees*, at 1.

[24] Matthew Futterman, *Network Sues Over Yankees' Blackout*, THE STAR-LEDGER (Newark, NJ), Apr. 30, 2002, at 13.

[25] Matthew Futterman, *Nothing New on YES Front*, THE STAR-LEDGER (Newark, NJ), Mar. 30, 2002, at 30.

[26] *Id.*

[27] *Yankees*, at 3.

[28] Futterman, *supra* note 24, at 13.

[29] *Id.*

[30] Sandomir I, *supra* note 15, at D4.

[31] *Yankees*, at 3.

[32] Sandomir I, *supra* note 15, at D4.

[33] *Id.*

network on the expanded-basic level.[34] YES offered to discount that rate to reach an earlier settlement with Cablevision.[35] Prior to the final settlement, however, Cablevision refused to move from its position and settle the dispute.[36]

YES filed the complaint one month after reaching an agreement with AT&T Broadband, which entailed offering YES on basic programming to its 250,000 Connecticut subscribers.[37] At the time of that agreement, YES had arrangements with twenty-four cable providers in addition to the DBS company DirecTV.[38] This made YES available on basic programming of every major cable system in the region, except Cablevision,[39] bringing distribution of YES to approximately 5.3 million subscribers.[40] YES filed the lawsuit after eight months of delay in negotiations,[41] resulting in Cablevision's 2.9 million subscribers in the region[42] losing the ability to view 130 of the 162 Yankees games during the 2002 season.[43] Hopes for an end to the dispute during the 2002 baseball season diminished after Cablevision requested 660 days for trial preparation[44] and sent a representative to only one of the seven public forums held by a New York City Council panel.[45] Prior to the settlement with YES, a district court judge granted Cablevision its motion to dismiss an anti-competition claim brought by consumers in the New York area.[46] Conversely, the YES suit against Cablevision survived a motion to dismiss.[47] One week before the settlement, the New Jersey General

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[34] Futterman, *supra* note 24, at 18. As a result of the settlement, Cablevision was expected to pay a similar monthly fee per subscriber. Sandomir I, *supra* note 15, at D4.

[35] Richard Sandomir, *Wait Till Next Year, YES Says*, N.Y. TIMES, Aug. 22, 2002, at D5. YES Chairman Leo J. Hindery Jr. "offered to discount the first year from a monthly subscriber fee of $2 to $1.28 and the second year from $2.12 to $1.75." *Id.*

[36] *Cablevision Seeks a Dismissal*, N.Y. TIMES, June 11, 2002, at D2 [hereinafter *Cablevision*]. Cablevision had offered to pay a subscriber rate of only fifty-five cents. *Id.*

[37] Futterman, *supra* note 25, at 30.

[38] *Id.*

[39] *Id.*

[40] *Yankees*, at 2.

[41] Futterman, *supra* note 24, at 13.

[42] Futterman, *supra* note 25, at 30.

[43] *Id.* The remaining thirty-two games that season were available to most viewers on broadcast or basic cable channels WCBS, ESPN, or Fox. Steve Zipay & Harry Berkowitz, *180 Days Later, Standoff Continues*, N.Y. NEWSDAY, Sept. 29, 2002, at C19. Postseason games aired on Fox or ABC Family. *Id.*

[44] *Cablevision*, *supra* note 36, at D2.

[45] Zipay & Berkowitz, *supra* note 43, at C19.

[46] Moccio v. Cablevision Sys. Corp., 208 F. Supp. 2d 361 (E.D.N.Y. 2002).

[47] Yankees Entm't and Sports Network, LLC v. Cablevision Sys. Corp., 224 F.

Assembly passed a bill designed to compel Cablevision to broadcast YES on its system.[48]

The effects of the impasse damaged the bottom line of both parties. Cablevision reported 5,400 subscriber defections to DirecTV through April 30, 2002,[49] and 17,000 defections through June 30.[50] Projections of subscriber losses for the full-year ranged from 27,500 to 45,000.[51] YES estimated the net effect on Cablevision to be a loss of $360 million in value.[52] YES felt the impact of the dispute in a different respect. Due to the deflated number of subscribers, Yankees telecasts on YES averaged a 2.0 cable rating in the region, down thirty-three percent from Yankees telecasts on MSG during the 2001 season.[53] Diminished ratings hurt YES through the resultant decrease in advertising revenue.[54] Furthermore, the standoff had consequences extending beyond the baseball season, as YES obtained the broadcast rights to New Jersey Nets basketball games for ten years beginning with the 2002-03 season.[55] The Nets had previously been in a long-standing agreement with FSNY.[56]

B. The Economic Rationale of Natural Monopolies

The YES complaint referred to Cablevision's monopoly power over its "captive cable television customers."[57] Cablevision possesses this monopoly power due to the exclusive franchises that local franchising authorities awarded to cable operators.[58] The

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Supp. 2d 657 (S.D.N.Y. 2002). The motion was denied, except in regard to the claim under New York's Donnelly Act. *Id.* at 679.

[48] Tom Hester, *YES Network Wins Support in Assembly*, THE STAR-LEDGER (Newark, NJ), Mar. 4, 2003, at 13. A sponsor of the bill claimed that its main objective was to encourage a resumption of negotiations between Cablevision and the YES Network after sixteen months of bickering. *Id.*

[49] Sandomir, *supra* note 35, at D5.

[50] *Id.*

[51] *Id.* Cablevision estimated the number of subscriber losses to be from 30,000 to 45,000. *Id.* A cable industry official estimated it at 27,500. *Id.*

[52] *Id.* "Hindery said Cablevision's subscribers were worth an estimated $4,000 each, a figure based on what similar cable systems have sold for; if 90,000 have defected, . . . the company has lost $360 million in value." *Id.*

[53] Zipay & Berkowitz, *supra* note 43, at C19. Each rating point represents 73,000 homes. *Id.*

[54] *Id.*

[55] Richard Sandomir, *Nets Leave Cablevision and Join YES*, N.Y. TIMES, Aug. 9, 2002, at D4.

[56] *Id.*

[57] *Yankees*, at 1.

[58] *See* 47 U.S.C. § 541 (1996) (prohibiting exclusive franchises). *But see infra* Part III (explaining *de facto* exclusive franchises).

classification of the cable television industry as a natural monopoly produces exclusive cable franchises. A natural monopoly is "an industry in which each firm's average cost curve is decreasing at the point where it crosses market demand."[59] This phenomenon occurs when there are relatively large fixed costs[60] associated with developing a product, but low marginal costs[61] associated with distributing the product.[62] Consequently, most household utilities, such as electricity and cable television, are considered natural monopolies.[63] Under these conditions, if the utility were to price competitively, it would develop an operating loss and not survive.[64] Therefore, pursuant to the goal of promoting economic efficiency, such industries are classified as natural monopolies and typically afforded government regulatory protection against competition.[65] Specifically, in the cable television industry, once the company has its cables in place to transport the signal to its customer base (the cable company's fixed cost), the cost incurred by the company in delivering its service to each individual customer is extremely low.[66]

The telephone industry was once heavily regulated,[67] based upon

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[59] LANDSBURG, *supra* note 7, at 356. *See also* 2 HAROLD DEMSETZ, EFFICIENCY, COMPETITION, AND POLICY, THE ORGANIZATION OF ECONOMIC ACTIVITY 76 (1989) (defining natural monopoly as a situation where "because of production scale economies, it is less costly for one firm to produce a commodity in a given market than it is for two or more firms, then one firm will survive; if left unregulated, that firm will set price and output at monopoly levels").

[60] Fixed costs are items that remain the same "regardless of the level of output," often called "overhead." LEONARD W. WEISS, ECONOMICS AND AMERICAN INDUSTRY 41 (1961).

[61] "[M]arginal cost is the change in cost which will accompany a small change in output." *Id.* at 52-53.

[62] LANDSBURG, *supra* note 7, at 356. An example is a software manufacturer distributing their product over the internet with marginal cost at essentially zero. *Id.* In a competitive market, the software would sell at marginal cost and nearly be free; the market would not survive that pricing scheme. *Id.* A monopolist can instead sell for substantially more than marginal cost, earn enough to cover the fixed costs, and can remain in business. *Id.*

[63] *E.g.*, Lancaster Cmty. Hosp. v. Antelope Valley Hosp. Dist., 940 F.2d 397, 401 n.8 (9th Cir. 1991) (explaining the natural monopoly phenomenon in relation to cable television, electric utilities, and water works).

[64] *See* LANDSBURG, *supra* note 7, at 356-57.

[65] *Id.* at 418.

[66] Kenneth Katkin, *Cable Open Access and Direct Access to INTELSTAT*, 53 CASE W. RES. L. REV. 77, 84 (2002); *see also* Omega Satellite Prod. Co. v. City of Indianapolis, 694 F.2d 119, 126 (7th Cir. 1982) (detailing the costs incurred by cable television companies).

[67] *See* United States v. Western Electric Co., 1982-2 Trade Cases (CCH) ¶ 64,900 (Aug. 24, 1982) (requiring AT&T "to divest all 22 Bell operating companies providing local exchange telephone service").

a natural monopoly rationale similar to that of cable television, until Congress dramatically altered that regulatory landscape with the 1996 Act.[68] The 1996 Act overhauled and deregulated most of the communications industry.[69] For example, the 1996 Act removed restrictions imposed upon the telephone industry by the 1982 AT&T Consent Decree.[70] It also permitted the "Baby Bells"[71] to enter the long-distance telephone market,[72] while simultaneously permitting long distance carriers to enter the local market.[73] This deregulation resulted in competition in both the long distance and local telephone markets unseen since the AT&T break-up.[74]

In the newly deregulated telephone industry, customers electing to change their local provider can do so simply by calling their new provider of choice.[75] Although the service provider is switched with ease from the consumer's perspective, the switch requires more work on the part of the telephone companies.[76] Even so, the telephone companies have enough incentive to complete the switch.[77] Switching cable television providers can be accomplished through the same means as switching telephone service providers; yet, customers do not have the option to switch cable providers due to the barriers imposed by exclusive franchises. Although the economics of the services that telephone and cable television companies provide are unmistakably similar,[78] the 1996 Act did not effectively introduce competition into

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[68] *Supra* note 12.

[69] *See infra* Part II (analyzing the regulatory landscape).

[70] *Western Electric Co.*, 1982-2 Trade Cases (CCH) ¶ 64,900.

[71] This term is commonly used to refer to the twenty-two Bell operating companies providing local telephone service that were divested from AT&T in the 1982 consent decree. *See supra* note 67.

[72] *See* Wiley, *supra* note 13.

[73] *Id.*

[74] *Id.*

[75] In many cases, the new carrier may in fact call the consumers. *See Deregulated*, CONSUMER REP., July 2002, at 30 [hereinafter *Deregulated*] (lamenting the negative effects of deregulation "where incessant telemarketers interrupt your dinner but customer service won't answer the phone").

[76] Miles W. Hughes, *Telecommunications Reform and the Death of the Local Exchange Monopoly*, 24 FLA. ST. U. L. REV. 179, 211-12 (1996). After obtaining state authority to provide local telephone service, the new providers must negotiate with the incumbent for "interconnection and collocation with the existing local exchange network." *Id.* at 211. The new providers' expensive alternative to negotiation is to construct a local infrastructure of its own to provide service. *Id.* at 211 n.282.

[77] *Id.* at 212. Incumbent cable providers have incentives to complete negotiations because "the [1996] Act does not permit them to enter the long-distance market until effective competition exists within their local exchange territory." *Id.*; *see also* 47 U.S.C. § 271 (1996).

[78] Katkin, *supra* note 66, at 84.

the cable television industry through deregulation.[79]

II. A REVIEW OF THE VARYING LOGIC BEHIND THE REGULATIONS THAT SOLIDIFIED CABLE TELEVISION'S MONOPOLY STATUS

The checkered regulatory history of cable television illustrates the difficulty Congress has had in shaping a policy that best suits the technology. Congress's oft-changing regulation of cable television began in the early 1930s when radio entered mainstream America.[80] When public concern grew over its effects,[81] Congress responded by enacting the Communications Act of 1934 ("Communications Act").[82] The Communications Act regulated all wire and radio communications available at that time, namely transmissions by radio, telephone, and telegraph.[83] The Communications Act created the Federal Communications Commission ("FCC") as the body in charge of promulgating regulations over the aforementioned media.[84] Furthermore, the Communications Act gave the FCC jurisdiction over common carriers.[85] Nonetheless, the FCC initially declined to regulate cable television on the grounds that it did not fall within the statutory definition of common carrier.[86] This abdication by the federal government left cable television regulation to state and local governments, which they engaged in by franchising cable systems to use public ways for their distribution systems.[87]

The FCC reversed course in 1959 when cable television operators began including non-local signals on their cable systems.[88]

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[79] *See, e.g.*, Jones, *supra* note 14.

[80] Kent D. Wakeford, *Municipal Cable Franchising: An Unwarranted Intrusion into Competitive Markets*, 69 S. CAL. L. REV. 233, 239 (1995); *see also* 2 ERIK BARNOUW, THE GOLDEN WEB: A HISTORY OF BROADCASTING IN THE UNITED STATES 22-26 (1968).

[81] Wakeford, *supra* note 80, at 239.

[82] Communications Act of 1934, 48 Stat. 1064 (codified as amended at 47 U.S.C. §§ 151-614).

[83] Wakeford, *supra* note 80, at 239 n.26.

[84] *Id.* at 240.

[85] *See* 47 U.S.C. § 153 (1934) (defining common carriers as "any person engaged as a common carrier for hire, in interstate or foreign communication by wire or radio or in interstate or foreign radio transmission of energy, . . . but a person engaged in radio broadcasting shall not, insofar as such person is so engaged, be deemed a common carrier").

[86] Frontier Broad. Co. v. Laramie Cmty. T.V. Co., 24 F.C.C. 251 (1958) (dismissing complaint asserting that cable television systems are common carriers within the meaning of the Communications Act under the rationale that the signals received and distributed by the cable systems are determined by the system and not the subscriber).

[87] Wakeford, *supra* note 80, at 241.

[88] Thomas W. Hazlett, *Station Brakes: The Government's Campaign Against Cable*

While cable television had not previously affected local broadcasters, the FCC stepped in at that point to protect them from competition.[89] The FCC later refined its position in 1972,[90] stating that cable operators are neither broadcasters nor common carriers, but instead "cable is a hybrid that requires identification and regulation as a separate force in communications."[91]

The FCC, noting the deleterious effect of over-regulating a growing industry, almost immediately engaged in deregulation of cable television.[92] The FCC's new approach examined jurisdictional and technological limitations and eliminated duplicative, costly regulations.[93] Congress later followed suit with the Cable Communications Policy Act of 1984 ("1984 Act").[94] The 1984 Act codified the collective regulatory schemes of federal, state, and local governments.[95] Most notable was the explicit bifurcation of regulatory power that "vested local authorities with extensive control over granting cable franchises."[96] Because the 1984 Act mandated that new competitors obtain a municipal cable franchise before entering the market, municipal officials stifled competition by offering exclusive licenses to the highest bidder.[97] Additionally, the 1984 Act prohibited local telephone companies, the likeliest cable competitors,[98] from providing video service.[99] Therefore, with this near impenetrable protection from competition and the elimination of local rate controls, Congress enabled cable operators to exploit their monopoly power.[100]

Television, REASON, Feb. 1995, *available at* http://www.manhattan-institute.org/hazlett/rahazlett72.htm.

[89] *Id.* *See, e.g.*, Carter Mountain Transmission Corp. v. FCC, 32 F.C.C. 459 (1962), *aff'd*, 321 F.2d 359 (D.C. Cir. 1963) (holding cable television to be a communications common carrier).

[90] FCC Cable Television Rep. and Order, 36 F.C.C.2d 143 (1972).

[91] Wakeford, *supra* note 80, at 243 (citing Robert F. Copple, *Cable Television and the Allocation of Regulatory Power: A Study of Government Demarcation and Roles*, 44 FED. COMM. L.J. 1, 32 (1991)).

[92] *See* Duplicative and Excessive Over-Regulation of Cable Television, Rep. and Order, 54 F.C.C.2d 855 (1975).

[93] *Id.*

[94] Cable Communications Policy Act of 1984, Pub. L. No. 98-549, 98 Stat. 2779 (1984) (codified as amended in 47 U.S.C.).

[95] Wakeford, *supra* note 80, at 244.

[96] *Id.*

[97] Hazlett, *supra* note 88. Most municipal officials felt "as New York Mayor John Lindsay had when he remarked that cable franchises were like 'urban oil wells beneath our city streets.'" *Id.*

[98] *Id.*

[99] *Id.*

[100] *Id.* The 1984 Act was "sponsored by then-Rep. Timothy Wirth [from

A short time later, Congress again reversed course and passed the Cable Television Consumer Protection and Competition Act of 1992 ("1992 Act").[101] The 1992 Act, passed over President Bush's veto,[102] attempted to address some of the problems that remained after the 1984 Act.[103] Congress remained watchful of the cable television industry and again altered the regulatory landscape with passage of the 1996 Act. This legislation was designed, in part, to open "all telecommunications markets to competition."[104]

The 1984 Act freed systems from rate regulations when the FCC determined that they were subject to effective competition.[105] One deregulatory component of the 1996 Act updated the term "effective competition" from its initial statutory use by Congress.[106] The 1996 Act added a provision stating that once a local telephone company, or similar service, offers video programming comparable to the cable operator's service to that area, effective competition exists.[107] When

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Colorado], often called the congressman from TCI." *Id.* Tele-Communications Inc., the largest cable operator in the United States at that time, is headquartered in Denver. *Id.*

[101] Cable Television Consumer Protection and Competition Act of 1992, Pub. L. No. 102-385, 106 Stat. 1460 (1992) (codified as amended in 47 U.S.C.).

[102] Wakeford, *supra* note 80, at 244.

[103] *Id.* The pertinent provisions of the 1992 Act included the prohibition of exclusive municipal franchises due to their adverse effects on consumers and the establishment of price ceilings on rates. *Id.* The 1992 Act also included a "must-carry" provision that required "cable television systems to devote a portion of their channels to the transmission of local broadcast television stations." *Id.* at 245 n.66.

[104] H.R. CONF. REP. NO. 104-458, at 1 (1996), *reprinted in* 1996 U.S.C.C.A.N. 11. In regards to provisions in then existing legislation that prohibited telephone companies from providing video programming to subscribers in their service areas, the report noted three government agencies "the FCC, the Commerce Department's National Telecommunications and Information Administration and the Department of Justice's Antitrust Division" who "found that the statute impedes competition in the cable industry." *See* 47 U.S.C. § 533(b), *repealed by* 1996 Act, *supra* note 68, § 302(b)(1).

[105] *Id.*

[106] *See* Brenner, *supra* note 8, at 404 (describing the initial use of "effective competition").

[107] The 1996 Act, *supra* note 68, finds effective competition to exist where a multichannel video programming distributor [hereinafter MVPD] meets one of four tests within its franchise area:

> (A) fewer than 30 percent of households in the franchise area subscribe to the service of a cable system; (B) the franchise area is (i) served by at least two unaffiliated [MVPDs] each of which offers comparable video programming to at least 50 percent of the households in the franchise area; and (ii) the number of households subscribing to programming services offered by multichannel video programming services offered by [MVPDs] other than the largest [MVPD] exceeds 15 percent of the households in the franchise area; (C) a [MVPD] operated by the franchising authority for that franchise

the determination is made that effective competition exists, the municipality "may no longer regulate subscriber rates for the basic service tier."[108]

The 1996 Act's overall goal of competition is partially met through the interplay allowed between cable television and telephone service providers. Previously restricted by the AT&T break-up,[109] local telephone carriers can now provide long-distance service and, correspondingly, long-distance providers can offer local telephone services.[110] In addition, telephone companies can provide video programming and cable companies are allowed to provide local telephone service.[111] Although attempting to introduce competition in the video marketplace by permitting telephone companies to compete with cable television providers, the 1996 Act does not prohibit municipal cable franchising,[112] which remains the greatest impediment to competition. Thus, the 1996 Act has only partially achieved the goal of true competition in the cable television market.

Still, the 1996 Act does provide insight into the possible future of competition in the cable television industry. Commentators have considered the phenomenon of overbuilding as a costly, yet possible, method to introduce competition into the cable television industry.[113] In allowing competition in local telephone service, the 1996 Act requires incumbent local telephone companies to work with any new

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> area offers video programming to at least 50 percent of the households in that franchise area; or (D) a local exchange carrier or its affiliate (or any [MVPD] using the facilities of such carrier or its affiliate) offers video programming service directly to subscribers by any means (other than direct-to-home satellite service) in the franchise area of an unaffiliated cable operator which is providing cable service in that franchise area, but only if the video programming services so offered in that area are comparable to the video programming services provided by the unaffiliated cable operator in that area.

47 U.S.C. § 543(*l*)(1)(A-D) (1996).

[108] Gregory W. Stepanicich, *The Telecommunications Act of 1996: Responding to a New Regulatory Maze*, *at* http://www.rwglaw.com/Articles (last visited Oct. 3, 2002). Non-basic service tier regulation was set to expire on its own. *Id.* The term "service tier" means a cable service for which the operator charges a separate rate. 47 U.S.C. § 522(17) (1996).

[109] *See supra* note 67 (explaining the divestiture of the AT&T Bell operating companies).

[110] *See* Jones, *supra* note 14.

[111] *Id.*

[112] Stepanicich, *supra* note 108. While cities may continue to franchise and regulate cable services, they are prohibited from extending franchises to other telecommunication services. *Id.*

[113] *See, e.g.*, Brenner, *supra* note 8, at 404. Overbuilding involves "constructing a competing cable system over a territory already served by or franchised to another." *Id.*

local telephone companies to "provide interconnection, number portability, dialing parity, and access to rights-of-way."[114] Similar cooperation between cable television competitors could serve to eliminate some of the costs of overbuilding a cable system.

In regards to rights-of-way, the 1996 Act states that no municipality may prohibit any entity from providing interstate or intrastate telecommunications service.[115] Municipalities do retain a "safe harbor" provision[116] that allows them "to manage the public rights-of-way and to require fair and reasonable compensation from telecommunication providers on a competitively neutral and nondiscriminatory basis."[117] As a result of this provision, a statutory right grants competing cable providers the ability to purchase the use of public rights-of-way from the municipalities for use in their distribution systems. Exclusive franchise grants, however, frustrate the ability of a competing cable system to enter the market in the first place.

The variations in Congress's regulatory approach to cable television display its uncertainty about cable television's true classification and the potential fallacy in designating the cable television industry as a natural monopoly. Consequently, the monopoly status of cable results more from governmental action, such as municipal franchising, than from economic factors.[118] This conclusion warrants examination of the economic and political effects of the removal of the cable industry regulations to allow competition in the video marketplace.

III. DEBUNKING THE MYTH OF CABLE TELEVISION AS A NATURAL MONOPOLY AND THE JUSTIFICATION FOR THE FRANCHISING PROCESS

Generally, natural monopoly[119] conditions result in government regulation of an industry.[120] The supposition that cable television was

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[114] Jones, *supra* note 14.

[115] 47 U.S.C. § 253(a) (1996).

[116] § 253(c). One commentator noted that "an important addition to the 1996 Act . . . preserved the power of local agencies to manage the use of their public rights-of-way." Stepanicich, *supra* note 108.

[117] § 253(c).

[118] Quincy Cable T.V., Inc. v. FCC, 768 F.2d 1434, 1450 (D.C. Cir. 1985).

[119] Wakeford, *supra* note 80, at 260-61. Natural monopolies occur in markets "with inherent structural characteristics that make it more efficient for one operator to offer services in the absence of competition." *Id.* (citing Richard A. Posner, *Natural Monopoly and its Regulation*, 21 STAN. L. REV. 548, 548 (1969)).

[120] *Id.* at 261.

a natural monopoly materialized legislatively in municipalities[121] awarding exclusive[122] franchises.[123] This process was a financial boon for municipalities as the franchising process included rewards by way of franchise fees and other services.[124] Blinded by those rewards, municipalities ignored typical market considerations, specifically competitive pricing, during the franchising process.[125]

Case law exposes the judicial view of exclusive franchise grants as the inescapable outcome of a competitive market.[126] In this view, exclusive franchise grants that eliminate competition serve to avoid the "wasteful duplication of facilities."[127] This "wasteful duplication of facilities" is a product of the public ownership of the public rights-of-way[128] that provide the distribution system that operators compete to access.[129] One commentator's alternative solution permits private ownership of the distribution system running below each individual's property so that he could connect to whichever provider he preferred.[130] This scenario precludes the need for competing providers to incur unnecessary costs in entering the market and defeats the possibility of the duplication of facilities.

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[121] *Id.* at 246. The FCC concluded that "local governments are inescapably involved in the [franchising] process because cable makes use of streets and ways and because local authorities are able to bring a special expertness to such matters, for example, as how best to parcel large urban areas into cable districts." *Id.* (quoting FCC Cable Television Rep. and Order, 36 F.C.C.2d 143, 207 (1972)).

[122] Brenner, *supra* note 8, at 371. While franchises have been denominated "nonexclusive," cable franchises developed a monopoly status that "was accepted by federal and local authorities, by the participants in the franchise process, by the victorious cable operator, and by the public." *Id.*

[123] 47 U.S.C. § 522(9) (1996) (defining the term "franchise" as "an initial authorization, or renewal thereof . . . issued by a franchising authority, whether such authorization is designated as a franchise, permit, license, resolution, contract, certificate, agreement, or otherwise, which authorizes the construction or operation of a cable system"); *see also* 47 U.S.C. § 522(10) (defining the term "franchising authority" as "any governmental entity empowered by Federal, State, or local law to grant a franchise").

[124] Wakeford, *supra* note 80, at 247. "The local franchise boards recognized their ability to extort exorbitant services and favors in the process of granting a cable franchise." *Id.*

[125] Brenner, *supra* note 8, at 370.

[126] *See, e.g.*, Omega Satellite Prod. Co. v. City of Indianapolis, 694 F.2d 119, 126 (7th Cir. 1982) (stating that "[a]n alternative procedure [to the competitive free-for-all] is to pick the most efficient competitor at the outset, give him a monopoly, and extract from him in exchange a commitment to provide reasonable service at reasonable rates").

[127] *Id.*

[128] *See* 47 U.S.C. § 253(a) (1996).

[129] Brenner, *supra* note 8, at 395.

[130] DEMSETZ, *supra* note 59, at 81. This alternative allows the company owning the facility to sell it to the new provider. *Id.*

The public rights-of-way justification for franchising is also flawed with respect to the degree that the government's property interest is implicated.[131] Cable operators use public property by either digging a trench to lay the cable or sharing a utility or telephone easement.[132] The latter typically results in payment on the part of the cable operator to the public utility for the permission to occupy part of the easement that the government has already issued.[133] The former appears to implicate a government property interest only to the extent of the cost "borne by the municipality associated with such use."[134] The 1996 Act supports such a pricing rationale,[135] whose "pay-per-use" scheme weakens the justification for the extensive governmental control present in the franchising process.[136]

Despite the apparent contradiction of the *de jure* classification of cable television operators as a natural monopoly, the operators maintain their *de facto* monopoly status that began early in cable's inception. A large factor in the monopoly status of cable television operators is that no viable technology provided true competition to the array of services available through cable during the 1970s and early 1980s.[137] The further development of competing technologies and services over the next two decades, however, created viable alternatives that weakened cable's *de facto* monopoly status. Thus, after the 1996 Act permitted telephone companies to enter the video marketplace,[138] telephone companies and the improvement of DBS systems posed a significant threat to the monopoly status of cable television.[139]

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131 Wakeford, *supra* note 80, at 252.

132 *Id.*

133 *Id.*

134 *Id.* at 252-53.

135 *See* 47 U.S.C. § 253(c) (1996).

136 Wakeford, *supra* note 80, at 252-53. "[T]he right to impose a charge for the use of rights-of-way [does not] provide[] justification for regulatory authority over all other aspects of cable television." *Id.*

137 Brenner, *supra* note 8, at 400-01. The variety of available technologies included satellite master antenna television (SMATV), multipoint distribution service (MDS) and DBS. *Id.* SMATV was an alternative to cable, but was not in direct competition with cable. *Id.* SMATV was most often found in apartment buildings where the building owner had a choice between SMATV or cable, but the subscriber could not make that choice. *Id.* MDS was not a true competitor to cable because it only offered one channel initially, although it was later modified to have four-channel groups in each market. *Id.* DBS was not viewed as a viable alternative to cable due to the ten to twenty-foot satellite dishes required for reception. *Id.* It was not until the 1990s that smaller, more easily mountable dishes were introduced. *Id.*

138 *See supra* Part II (discussing the effect of the latest wave of deregulation).

139 Wakeford, *supra* note 80, at 269.

Telephone companies were uniquely positioned to compete with cable companies.[140] They appeared able to provide services at rates lower than were possible through overbuilding[141] and able to recover the costs of entry.[142] Those incumbent local exchange carriers, however, have exited the video business.[143] Electric and gas utilities are potential competitors to cable television, primarily due to already possessing "access to public rights of way, existing telecommunications facilities, and existing relationships with customers."[144] Despite these advantages, their entrance into the marketplace has been slow and is not expected to be widespread.[145] The reluctance of telephone companies and public utilities to enter the cable television market[146] allowed the emergence of DBS as the primary competition facing cable television operators.

DBS technology has a distinct advantage in competing with cable. Although their systems do incur fixed costs of entry, primarily from the need to place a satellite in orbit to distribute their signal to subscribers,[147] they can spread the cost of entry over a greater distribution area.[148] The new wave of DBS systems began in 1994 with

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[140] *Id.* The theory of telephone companies competing with cable providers "rests upon the assumption that a telephone company already has the infrastructure in place to provide cable programming to subscribers." *Id.* "Without needing to invest in the fixed costs required by cable, the telephone company could garner a distinct advantage over the cable competitor." *Id.*

[141] *See supra* note 113 (explaining the concept of overbuilding).

[142] Wakeford, *supra* note 80, at 269.

[143] In re Ann. Assessment of the Status of Competition in the Mkt. for the Delivery of Video Programming, Seventh Ann. Rep., 16 F.C.C.R. 6005, 6009 (2001) [hereinafter *FCC Seventh Ann. Rep.*]. Most chose to sell their MVPD systems and preferred instead to market DBS systems. *Id.* BellSouth, however, still operates some overbuild cable systems. In re Matter of Ann. Assessment of the Status of Competition in the Mkt. for the Delivery of Video Programming, Ninth Ann. Rep., 17 F.C.C.R. 26901, 26905 (2002) [hereinafter *FCC Ninth Ann. Rep.*].

[144] *FCC Ninth Ann. Rep.*, 17 F.C.C.R. at 26947.

[145] *Id.*

[146] *Id.* at 26904. The four largest incumbent local exchange carriers have largely exited the video business. *Id.* A few smaller local exchange carriers continue to offer, or are preparing to offer, MVPD service over existing telephone lines. *Id.* "[U]tilities are not yet widespread competitors in the telecommunications or cable markets. Mainly, it appears that utilities will provide MVPD competition in scattered localities." *Id.* at 26947.

[147] Wakeford, *supra* note 80, at 269. DBS systems are able to recoup their fixed costs of entry due to the large number of potential subscribers resulting from an orbiting satellite. *Id.* at 270. Additionally, the satellite has other potential uses outside of television programming. *Id.*

[148] *Id.* DBS operators can provide "coverage to a greater number of possible subscribers than an equivalent cable investment from an overbuild cable operator would provide." *Id.*

the launch of two competing providers, Direct Satellite Service and Primestar.[149] Initial subscribership to those DBS systems[150] left the industry with high hopes for the future.[151] Early hurdles prevented a quicker start to DBS truly competing with cable,[152] but they were overcome through legislative help that broadened the available service granted to providers[153] and through technological improvements that lowered the cost for consumers.[154] DBS thus obtained a foothold allowing it to exceed even the most optimistic expectations for market growth at its onset.[155]

A monopoly, in general, exists when there is only one seller of services with no close substitutes.[156] That single seller possesses the ability to affect market prices through its actions by way of its monopoly power.[157] With DBS service at the forefront, in addition to telephone and utility companies possibly competing for subscribers, alternative providers are moving into position to offer video services at competitive prices.[158] This trend affects the cable company's

[149] THOMAS W. HAZLETT & MATTHEW L. SPITZER, PUBLIC POLICY TOWARD CABLE TELEVISION: THE ECONOMICS OF RATE CONTROLS 195 (1997).

[150] *Id.* at 196. In its first year of operation, beginning July 1994, DirecTV achieved subscribership of 600,000 households, about half of which were homes passed by cable systems. Christopher Stern, *DBS and Cable Square Off at the FCC*, BROAD. & CABLE, July 10, 1995, at 42. The FCC defines "homes passed" as "the total number of households capable of receiving cable television service." *FCC Ninth Ann. Rep.*, 17 F.C.C.R. at 26909 n.11.

[151] HAZLETT & SPITZER, *supra* note 149, at 196. Industry forecasters predicted that DBS along with cable's other competitors, wireless cable and telephone company overbuilders, would reach "nearly one-third of cable's projected total" of subscribers by the year 2000. *Id.*

[152] In re Ann. Assessment of the Status of Competition in the Mkt. for the Delivery of Video Programming, Fifth Ann. Rep., Separate Statement of Comm'r Susan Ness, 13 F.C.C.R. 24284, 24483. Potential DBS subscribers through 1997 declined to sign up due to "high installation costs, significant costs to hook up additional TV sets, and the lack of broadcast television service." *Id.*

[153] *Id.* After 1997, the cost of installation plummeted, yet it remained expensive to add service to additional TV sets. *Id.*

[154] *FCC Ninth Ann. Rep.*, 17 F.C.C.R. at 26904. The FCC attributes part of the growth of DBS "to the authority granted to DBS operators to distribute local broadcast television stations in their local markets by the Satellite Home Viewer Improvement Act of 1999." *Id.*

[155] *Id.* As of December 2002, DBS subscribers represented 20.3 percent of all MVPDs. *Id.* Between June 2001 and June 2002, DBS subscribers grew at a rate significantly greater than the cable subscriber growth rate, "from almost 16 million households to about 18 million households." *Id.*

[156] Wakeford, *supra* note 80, at 260.

[157] LANDSBURG, *supra* note 7, at 344.

[158] Wakeford, *supra* note 80, at 266. The entrance of multiple cable providers, whether in a natural monopoly or a competitive system, results in heated competition to attract subscribers. *Id.* Such competition focuses the resources of the

monopoly power and challenges its status as a protected monopoly.

IV. THE ECONOMIC COSTS OF CABLE TELEVISION'S MONOPOLY STATUS MANIFESTED IN HIGHER RATES, POORER SERVICE, AND SUBJUGATION OF CONSUMER CHOICE

The most insidious effects of monopoly conditions are lower production[159] and higher costs[160] as compared to competitive conditions. In the cable franchising scheme, lower production manifests itself through a "misallocation of resources result[ing] in diminished satisfaction of society's wants."[161] The higher costs can be pecuniary and non-pecuniary.[162] While pecuniary costs associated with running a business occur under any economic condition, the consequences of cable franchising and monopoly conditions are higher costs or poorer service.[163] This system is unjustified because the costs passed on to consumers from the cable companies constitute an essentially needless wealth transfer from consumers to their municipality.[164]

Despite the costs associated with obtaining an exclusive municipal franchise, cable operators are willing participants in the municipal franchising process. The monopoly status created by an exclusive franchise permits cable operators to recoup their costs from consumers by charging higher rates[165] for their services.[166] Without competition, consumers are forced to pay higher rates if they wish to have cable television service, as they cannot elect to obtain service

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competitors on providing the most attractive services and fees to the consumers. *Id.*

[159] *Id.* at 281.

[160] LANDSBURG, *supra* note 7, at 344. Through its monopoly power, a monopolist can "affect the market price of its output." *Id.*

[161] Wakeford, *supra* note 80, at 282 (quoting Robert H. Lande, *Wealth Transfers as the Original and Primary Concern of Antitrust: The Efficiency Interpretation Challenged*, 34 HASTINGS L.J. 67, 72-73 (1982)).

[162] Wakeford, *supra* note 80, at 281. "Municipal governments impose fees upon . . . cable operators that would not be required in an efficient market." *Id.* These costs serve to create monopolies and prevent competition from offering their services. *Id.*

[163] *Id.* at 282. Consumers bear these costs through increases in the subscription rate or a reduced package of services available from the cable company. *Id.* (citing THOMAS W. HAZLETT & MATTHEW L. SPITZER, CABLE REGULATION AND THE FIRST AMENDMENT (1995)).

[164] *Id.* at 282.

[165] Cable price estimates for 2003 predicted a rise by an average of 5.4 percent starting in January. Grover & Lowry, *supra* note 22, at 40.

[166] As per the 1996 Act, rate regulations for large cable companies expired in 1999. Stepanicich, *supra* note 108. Cable rates have increased 45 percent since the 1996 Act. Holly M. Sanders, *Echostar Has 2nd-Qtr Profit After Adding Customers*, BLOOMBERG NEWS, Aug. 15, 2002, LEXIS, Nexis Library, Bloomberg News file.

from another company without moving to a different municipality.[167]

Customers bear non-pecuniary costs of cable monopolies in a variety of ways, including unpunctual responses to service calls[168] and fewer programming options. Programming options, which cable operators typically provide in several tiers,[169] vary at the operator's discretion.[170] It would appear elementary that a large number of video channels results in a correspondingly large number of program sources to choose from.[171] That reasoning is confounded by the dual function performed by a cable franchise holder.[172] In the programming sense, complications arise in circumstances of cross-ownership of programming channels and distribution services.[173]

In *Time Warner Entertainment Co. v. United States*,[174] the United States Court of Appeals for the District of Columbia Circuit upheld a constitutional challenge to two provisions of the 1992 Act. At issue were the "subscriber limits provision" that authorizes the FCC to "limit the number of subscribers a cable operator may reach,"[175] and the "channel occupancy provision" that "directs the [FCC] to limit the number of channels on a cable system that may be devoted to video programming in which the operator has a financial interest."[176]

In upholding the "subscriber limits provision," the court echoed

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[167] *See supra* Part III (discussing exclusive municipal franchises).

[168] Terrence Dopp, *Cable Providers Lash Out at Lawmakers*, THE EXPRESS-TIMES (Easton, PA), Oct. 17, 2002. The New Jersey Legislature had proposed a plan under which one component "would require companies to respond to all service complaints within three hours." *Id.*

[169] *FCC Ninth Ann. Rep.*, 17 F.C.C.R. at 26909 n.12. The FCC explained that in the tier structure

> [t]he primary level of cable television service is commonly referred to as "basic service" and must be taken by all subscribers. The content of basic service varies widely among cable systems but, pursuant to the Communications Act, must include all local television signals and public, educational, and governmental access channels and, at the discretion of the cable operator, may include other video programming services. One or more expanded tiers of services, . . . often known as expanded basic, also may be offered to subscribers. These expanded tiers of service usually include additional video programming channels.

Id.

[170] *See id.*

[171] Eli M. Noam, *Towards An Integrated Communications Market: Overcoming the Local Monopoly of Cable Television*, 34 FED. COMM. L.J. 209, 210-11 (1982).

[172] *Id.* at 211.

[173] *See Yankees*, at 3. For example, Cablevision is the majority owner and manager of MSG and FSNY. Sandomir I, *supra* note 15, at D4.

[174] 211 F.3d 1313 (D.C. Cir. 2000), *cert. denied*, 531 U.S. 1183 (2001).

[175] *Id.* at 1315; *see also* 47 U.S.C. § 533(f)(1)(A) (1996).

[176] *Time Warner*, 211 F.3d at 1315; *see also* § 533(f)(1)(B).

congressional concern about likely anticompetitive effects resulting from concentration in the media.[177] The court deferred to the substantial evidence presented in the congressional report accompanying the 1992 Act stating that "increases in the concentration of cable operators threatened diversity and competition in the cable industry."[178] In upholding the "channel occupancy provision," the court noted both the statutory aim of promoting diversity of available programming and the provision's content-neutral applicability.[179] In its analysis, the court focused on the incentive and ability of cable operators to favor their affiliated programmers, which imposes economic barriers to competition.[180]

Before *Time Warner*, the United States Supreme Court had upheld the "must-carry" provision of the 1992 Act in *Turner Broadcasting System, Inc. v. FCC*.[181] That provision required cable operators to carry local network signals on their systems.[182] The Court upheld the provision against petitioner's First Amendment claims,[183] concluding that it was narrowly tailored to render the burden imposed congruent to the benefits created.[184] The Court quoted its earlier opinion in *United States v. Midwest Video Corp.*,[185] stating that "increasing the number of outlets for community self-expression represents a 'long-established regulatory goal in the field of television broadcasting.'"[186]

The Court also identified "'a governmental purpose of the highest order' in ensuring public access to 'a multiplicity of information sources, [a]nd [a] Government . . . interest in eliminating restraints on fair competition. . . .'"[187] Those two goals should extend the justification of "must-carry" beyond merely requiring cable operators to carry local broadcast signals to also requiring the carrying of channels emanating from unrelated programmers. Presently, such an extension of the holding does not

177 *Time Warner*, 211 F.3d at 1316.
178 *Id.* at 1319-20.
179 *Id.* at 1321.
180 *Id.* at 1322.
181 520 U.S. 180 (1997) [hereinafter *Turner II*].
182 *See* 47 U.S.C. §§ 532-35 (1996).
183 *Turner II*, 520 U.S. at 224-25.
184 *Id.* at 215-16.
185 406 U.S. 649 (1972) (plurality opinion).
186 *Turner II*, 520 U.S. at 192-93 (quoting *Midwest Video Corp.*, 406 U.S. at 667-68).
187 *Id.* at 190 (quoting Turner Broad. Sys., Inc. v. FCC, 512 U.S. 622, 663-64 (1994) [hereinafter *Turner I*]).

exist.[188] In reality, cable operators possess the ability to "silence the voice of competing speakers with a mere flick of the switch."[189]

The Court noted that in enacting the 1992 Act, Congress attempted to address concerns regarding the "increasing concentration of ownership and control in the cable industry."[190] The Court reasoned that the "must-carry" and "subscriber limits" provisions preclude cable operators from using their "bottleneck [monopoly] power to exclude other providers of cable programming."[191] Further, the Court noted Congress's concern that cable operators might not let other programmers "say anything at all in the principal medium for reaching much of the public"[192] and that the two provisions thereby serve to promote competition in the industry.[193] Thus, the Court upheld Congress's stated aims for the channel occupancy provision: increasing the number of voices available to cable viewers and placing reasonable limits on the number of channels an operator could occupy.[194]

The aforementioned provisions of the 1992 Act attempted to resolve the problem caused by vertical integration in the cable industry.[195] Vertical integration occurs when a company uses its monopoly power over one aspect of the production chain to stifle

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[188] Congress has opposed an FCC ruling that would have granted the largest television stations the ability to grow by owning more stations. Stephen Labaton, *F.C.C. Media Rule Blocked in House in a 400-to-21 Vote*, N.Y. TIMES, July 24, 2003 at A1 [hereinafter Labaton I]. The proposed FCC rule sought to expand the cap on a single company's ownership of "television stations reaching 45 percent of the nation's households, but the House measure would return the ownership cap to 35 percent." *Id.* Supporters of the legislation against the FCC rule asserted that "further media consolidation would reduce the diversity of voices on the airwaves." *Id.* at C6. The rule was similarly opposed in the Senate. Stephen Labaton, *F.C.C. Plan to Ease Curbs on Big Media Hits Senate Snag*, N.Y. TIMES, Sept. 17, 2003 at A1.

[189] *Turner II*, 520 U.S. at 197 (quoting *Turner I*, 512 U.S. at 656).

[190] *Time Warner*, 211 F.3d at 1316 (referencing the Senate Report accompanying the final version of the 1992 Act, S. REP. NO. 102-92, at 32 (1991), *reprinted in* 1992 U.S.C.C.A.N. 1165, stating "there are special concerns about concentration of the media in the hands of a few who may control the dissemination of information").

[191] *Id.* at 1317.

[192] *Id.* at 1317-18 (citing *Turner I*, 512 U.S. at 656-57); *see also* Labaton I, *supra* note 188, at C6.

[193] *Id.* at 1318.

[194] S. REP. NO. 102-92, at 25, 80 (1991), *reprinted in* 1992 U.S.C.C.A.N. 1158, 1213.

[195] *Time Warner*, 211 F.3d at 1322. Legislative history accompanying the 1992 Act "document[s] Congress's concerns with affiliation between cable operators and cable programmers." *Id.* "The cable industry has become vertically integrated; cable operators and cable programmers often have common ownership. As a result, cable operators have the incentive and ability to favor their affiliated programmers. This could make it more difficult for noncable-affiliated programmers to secure carriage on cable systems." *Id.*

competition in another aspect that ordinarily would have been competitive.[196] The cable television industry can be viewed in three stages of production and distribution that includes manufacturers, wholesalers, and retailers.[197] Vertical integration in the cable television industry could occur when networks (the wholesalers) own a large amount of broadcast stations (the retailers).[198] The most direct solution to vertical integration separates the distribution role of a cable company from its programming function.[199] Such a divestiture need not occur, however, if the company is simply mandated to allow access by other programmers.

Addressing a different industry, the Supreme Court required an analogous access to competition in *United States v. Terminal R.R. Ass'n of St. Louis*[200] when it dealt with the Terminal Railroad Association consortium in the late 1800s.[201] Mindful of the waste that multiple railroad lines could cause, the Court required the consortium to provide access to its tracks and bridges to competing companies on "reasonable terms and regulations."[202]

The Court noted that joining two cities by more than one railroad line created an "unnecessary duplication of facilities."[203] As mentioned above, the courts used the same language to justify cable monopolies,[204] yet cable rulings varied from *Terminal R.R.* because they lacked the mandatory provision of access to competing companies. In the barest sense, the cable and railroad industries are similar with respect to the transportation of goods and services over their respective "lines." A ruling applying the *Terminal R.R.* "essential facilities doctrine"[205] to cable companies could invite competition

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[196] Christopher S. Yoo, *Vertical Integration and Media Regulation in the New Economy*, 19 YALE J. ON REG. 171, 176 (2002).

[197] *Id.* at 182.

[198] *Id.* at 183-84.

[199] Noam, *supra* note 171, at 216.

[200] 224 U.S. 383 (1912).

[201] Teague I. Donahey, Terminal Railroad *Revisited: Using the Essential Facilities Doctrine to Ensure Accessibility to Internet Software Standards*, 25 AM. INTELL. PROP. L. ASS'N Q.J. 277, 279 (1997). "In 1889, a group of railroad companies . . . formed the Terminal Railroad Association . . . in order to consolidate the various railroad facilities and thoroughfares in St. Louis, including the central train station . . . and every connecting railroad system within the city and on either side of the river." *Id.*

[202] *Id.* at 281 (quoting *Terminal R.R.*, 224 U.S. at 411).

[203] *Id.* at 286 (quoting *Terminal R.R.*, 224 U.S. at 393).

[204] *See* Omega Satellite Prod. Co. v. City of Indianapolis, 694 F.2d 119, 126 (7th Cir. 1982).

[205] Donahey, *supra* note 201, at 307-08. "The essential facilities doctrine . . . is generally understood to have its origins in *Terminal Railroad*." *Id.* The doctrine mandates access to the essential facilities of a monopolist when that monopolist

while still allowing the incumbent company to remain.[206]

The tale of cable industry regulation parallels the experience of regulation of the railroad industry. After World War II, railroads faced competition primarily from the trucking industry.[207] The trucking industry offered distinct advantages over the railroad industry,[208] which left the railroad industry behind the technological curve.[209] Unfortunately, railway regulation continued to persist for some time after these developments[210] until Congress finally scaled the regulations back in 1980.[211] Cable monopolies face a similar wave of competing technologies[212] advancing upon their monopoly power and have had their share of deregulation.[213] This deregulation is a beacon of hope for the future of competition in the video marketplace. As the railroad example demonstrates, the regulatory mechanism might do more harm than good by producing more inefficiency than it eliminates.[214]

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possesses a "bottleneck" monopoly. *Id.*; *see also* MCI v. AT&T, 708 F.2d 1081 (7th Cir. 1983).

[206] *Terminal R.R.*, 224 U.S. at 411. The Court preserved "to the public [the] system of great public advantage." *Id.*

[207] Donahey, *supra* note 201, at 303 (citing THEODORE E. KEELER, RAILROADS, FREIGHT, AND PUBLIC POLICY 28 (1983)). The trucking industry was also regulated, but deregulation began in 1980. *Id.* at 304. In the first six years of deregulation, the number of carriers doubled and prices fell between 28 and 56 percent. *See* Robert Crandall & Jerry Ellig, *Economic Deregulation and Customer Choice: Lessons for the Electric Industry*, The Center for Market Processes, George Mason University, *at* http://www.mercatus.org/research/dereg_summary.html (March 12, 2003).

[208] *Id.* Notable advantages were increased efficiencies and lower costs. *Id.*

[209] Donahey, *supra* note 201, at 304.

[210] Lawrence W. Reed, *Deregulation: Coming to a Utility Near You*, THE FREEMAN, Vol. 47, No. 8, Aug. 1997, *available at* http://www.libertyhaven.com. Railroad regulation "stifled competition, boosted costs, reduced management flexibility, and left railroads unable to compete effectively with alternative . . . modes of transportation." *Id.* The delay in railroad deregulation is attributed to the cumbersome regulatory scheme and the railroad industry's support for the regulation that ensured their profit margins, despite prevailing questions of service quality. Donahey, *supra* note 201, at 304-05. *See* GABRIEL KOLKO, RAILROADS AND REGULATION, 1877-1916 (1965); Bruce B. Wilson, *Railroads, Airlines, and the Antitrust Laws in the Post-Regulatory World: Common Concerns and Shared Lessons*, 60 ANTITRUST L.J. 711, 711-16 (1991).

[211] Donahey, *supra* note 201, at 304. *See* Staggers Rail Act of 1980, Pub. L. No. 96-448, 94 Stat. 1895 (codified as amended in scattered sections of 45 and 49 U.S.C.). Since deregulation, "prices have declined 44 percent [and] delivery time has improved dramatically." Reed, *supra* note 210.

[212] *See* Donahey, *supra* note 201, at 304 n.102; *see also supra* Part III (discussing the competing technologies).

[213] *See supra* Part II (discussing statutory deregulation of the cable television industry).

[214] Donahey, *supra* note 201, at 305.

V. CONCLUSION

Competition is the method best suited to drive down prices, to increase quality of service, and to offer options to consumers.[215] The long overdue deregulation of the telecommunications sector injected competitive effects that have impacted the cable television industry. Cable companies, however, continue to possess exclusive municipal franchises that prevent customers from selecting among alternate providers. The absurdity of this problem is evident when customers living across the street from each other are afforded different opportunities by virtue of living in separate municipalities.

Fortunately for disheartened consumers, choices have recently begun to emerge. Through technological advances, DBS companies have positioned themselves as cable's biggest competitor. While DBS subscribership has yet to rise to a level necessary to consider it a true competitor to cable, that level may soon be reached. DBS has siphoned off nearly one million cable customers in 2002,[216] and the industry is expected to continue to grow in 2003.[217] DBS has thus been able to enter the marketplace despite the cable companies' present monopoly position. The loss of cable company subscribers to DBS providers[218] indicates the tenuous justification for cable monopolies. The dispute between YES and Cablevision displays how cable companies continue to fight to maintain their position, to the detriment of consumers.

Without the intervention of the New Jersey Legislature, New York City Mayor Bloomberg,[219] and New York State Attorney General Eliot Spitzer,[220] Cablevision customers seeking to view Yankees and Nets telecasts would still be in a difficult position. Although the settlement ended the stalemate, it merely created a temporary solution specific to this local dispute and provided no permanent solution for the industry. In a competitive market, customers could simply cancel their Cablevision subscription and select another video provider. Exclusive municipal franchises, however, preclude the selection of another cable provider. Even worse, the alternative

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[215] Wakeford, *supra* note 80, at 285. Commentators contend that "under the contestable market theory, . . . cable operators will provide the same rates and services as if they were faced with direct competition." *Id.*

[216] Grover & Lowry, *supra* note 22, at 40.

[217] Ronald Grover & Tom Lowry, *Media: Return of the Dealmakers*, BUS. WK., Jan. 13, 2003, at 126.

[218] *Id.* The forecasts for 2003 had DBS increasing their subscribership by 3 million customers at cable companies' expense. *Id.*

[219] Sandomir I, *supra* note 15, at D1.

[220] Sandomir II, *supra* note 15, at S2.

presented by DBS, to forego any cable service whatsoever, may not appeal to all consumers[221] or the consumers may not yet benefit from these advantages.[222]

Deregulation, despite its advantages, is not a complete solution to the problems created by regulation. The telephone industry experienced per-minute rate decreases following deregulation, but that reduction was a result of regulated cuts in telephone access charges.[223] Cable television subscription rates have skyrocketed under deregulation.[224] In a rare positive aspect, regulation provided an additional benefit to consumers in helping to foster the Internet.[225] Nonetheless, cable television regulation imposes many burdens, and an overhaul of the regulation can better serve the community's interests.[226]

By no means are cable companies the villains in the present situation. They simply had the benefit of monopoly status in the past and are now faced with a changing industry. The concept of competition in the video marketplace requires consumer choice and infers that incumbent cable companies remain an important player in the video programming marketplace.[227] Competition will force the

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[221] Grover and Lowry, *supra* note 22, at 40. "[Cable companies are] pushing higher-margin services—especially high-speed Internet access—that satellite can't yet offer." *Id.*

[222] *See States with Direct-To-Home Dish Penetration of Fifteen Percent or More, July 2001*, *at* http://www.skyreport.com (last visited Oct. 3, 2002). As of 2001, Vermont ranked first with 41.62% of television households having satellite television penetration. *Id.* "The only significant remaining impediment to [DBS] deployment is the inability of . . . DBS operators to reach residents living in large apartment buildings." Yoo, *supra* note 196, at 208 n.153; *see also* In re Ann. Assessment of the Status of Competition in the Mkt. for the Delivery of Video Programming, Eighth Ann. Rep., 17 F.C.C.R. 1244, 1300-05 (2002).

[223] *Deregulated*, *supra* note 75, at 32. Access charges are the fees "regulated local phone companies on each end of an interstate call charge long-distance carriers to connect through the local equipment." *Id.*

[224] *Id.* at 33.

[225] *Id.* at 32. This occurred, "according to the GAO, by barring AT&T and the 'Baby Bells' from providing data-processing and information services and thus stifling competition, and by a Federal Communications Commission not to impose access charges on Internet service providers, keeping costs down." *Id.*

[226] *Health of the Telecommunications Sector: A Perspective from the Commissioners of the Federal Communications Commission: Hearing Before the Subcomm. on Telecommunications and the Internet of the House Comm. on Commerce and Energy*, 108th Cong. 38 (2003) (statement of Kathleen Q. Abernathy, Commissioner, Federal Communications Commission). Commissioner Abernathy commented that "[t]hese dramatic changes [in telecommunications] compel us to analyze whether our existing rules best serve the public interest." *Id.*

[227] J. Gregory Sidak & Daniel F. Spulber, *Deregulation and Managed Competition in Network Industries*, 15 YALE J. ON REG. 117, 127 (1998).

incumbents to adapt to a new marketplace because rate increases and poor service quality are not feasible business decisions when a competitor can attract customers by offering more favorable service options. Competition has changed the landscape of the market, but "[t]he job is not yet done."[228] As competition continues to embed itself in the industry, the future for the video marketplace looks bright for customers and providers alike. Officially breaking the monopolistic stranglehold that cable companies enjoy over consumers by eliminating exclusive cable franchises would significantly brighten that picture.

[228] *Cable and Video: Competitive Choices: Hearing Before the Subcomm. on Antitrust, Business Rights, and Competition of the Senate Comm. on the Judiciary*, 107th Cong. 19 (2001) (statement of Robert Sachs, President & CEO, National Cable Television Association).