

# CM CINNAMON MUELLER

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**Jeremy M. Kissel**  
Admitted in Illinois, Florida and District of Columbia

April 16, 2010

Ms. Marlene Dortch  
Secretary  
Federal Communications Commission  
445 12th Street, S.W.  
Washington, D.C. 20554

**Via ECFS**

**Re: American Cable Association ("ACA") Notice of Ex Parte Presentation; In the Matter of Applications of Comcast Corporation, General Electric Company, and NBC Universal, Inc., to Assign and Transfer Control of FCC Licenses; MB Docket No. 10-56**

Dear Ms. Dortch:

Pursuant to Section 1.1206 of the Commission's rules, we are electronically filing this letter in the above-referenced docket as notice of an April 15, 2010 meeting between the Commission staff identified in *Exhibit 1*, and the representatives of ACA listed in *Exhibit 2*.

During the meeting, Professor William P. Rogerson presented the information on the slides attached hereto as *Exhibit 3*, and answered staff questions.

Sincerely,



Jeremy M. Kissel

cc (via email): Sherrese Smith  
William Lake  
Paul de Sa  
William Freedman  
Jamila Bess Johnson  
Neil Dellar  
Erin McGrath  
James Bird  
Deborah Broderson  
Marcia Glauberman  
Virginia Metallo  
Daniel Shiman  
Paul LaFontaine  
Judith Herman

Clarence Bush  
Rebekah Goodheart  
Donald Stockdale  
Jennifer Tatel  
Matthew M. Polka  
Ross J. Lieberman  
William P. Rogerson  
Chris C. Cinnamon  
Thomas W. Cohen

## **Exhibit 1**

Sherrese Smith, Office of the Chairman  
William Lake, Media Bureau  
Paul de Sa, Office of Strategic Planning and Policy Analysis  
William Freedman, Media Bureau  
Jamila Bess Johnson, Media Bureau  
Neil Dellar, Office of General Counsel  
Erin McGrath, Wireless Telecommunications Bureau  
James Bird, Office of General Counsel  
Deborah Broderson, Media Bureau  
Marcia Glauberman, Media Bureau  
Virginia Metallo, Office of General Counsel  
Daniel Shiman, Media Bureau  
Paul LaFontaine, Office of Strategic Planning and Policy Analysis  
Judith Herman, Media Bureau  
Clarence Bush, Office of Inspector General  
Rebekah Goodheart, Media Bureau  
Donald Stockdale, Wireline Competition Bureau  
Jennifer Tatel, Media Bureau

## **Exhibit 2**

Matthew M. Polka, ACA, President and Chief Executive Officer

Ross J. Lieberman, ACA, Vice President of Government Affairs

William P. Rogerson, Professor of Economics, Northwestern University, Consultant to ACA

Chris C. Cinnamon, Cinnamon Mueller, Outside Counsel to ACA

Thomas W. Cohen, Kelley Drye, Outside Counsel to ACA

**Exhibit 3**



# **Presentation to the FCC on the Proposed Combination of Comcast- NBC Universal**


**April 15, 2010**

***American Cable Association***



## Overview of Presentation

- **Competitive Harms Post-Combination**
  - Horizontal Competitive Harm
  - Vertical Competitive Harm
- **Current Program Access Rules and Arbitration Conditions of Past Mergers Provide Inadequate Relief for Vertical Harms**



# Post-Combination Combined Lines of Business

- **NBC Programming**
  - NBC network with 10 O&O NBC affiliates in major metropolitan areas
  - Telemundo network with 15 O&O affiliates in major metropolitan areas
  - National cable networks (prime time rank):
    - USA (1), Syfy (20), MSNBC (25), Bravo (31), mun2 (34), Oxygen (41), CNBC (65)
- **Comcast Programming**
  - Group of 10 RSN's serving many of the most important metropolitan areas
  - National cable networks (prime time rank):
    - E! Entertainment (38), TV One (53), Versus (56), Style (64), Golf Channel (69), G4 (73)
- **Comcast MVPD services**
  - Largest cable operator, serving 23.8 million customers in 39 states
  - Largest residential broadband operator, serving 15.7 million customers



# Competitive Harms Post-Combination Overview

- **The Comcast/NBC merger has both horizontal and vertical components and each component creates a separate and distinct competitive harm**
- **Horizontal Harm** (due to the combination of NBC's programming assets with Comcast's programming assets)
  - By controlling a much larger block of highly demanded programming, the merged entity will be able to charge higher programming fees to MVPDs
  - These higher fees will be passed on to subscribers in the form of higher subscription prices
  - The simple model we present explains why combined control of more programming can result in higher prices
  - Initial evidence shows that this effect can be significant in programming markets
- **Vertical Harm** (due to combination of NBC's programming assets with Comcast's cable assets)
  - When NBC sells programming to MVPDs that compete with Comcast, this reduces Comcast's profit
  - The merged entity will take this effect into account
  - This will result in the merged entity charging higher prices for its programming to MVPDs that compete with Comcast
  - These higher programming prices will be passed on to subscribers in the form of higher subscription prices



# **Competitive Harms Post-Combination**

## **Horizontal Harms: Theory**

- **Combination of programming assets will significantly increase market power of the combined entity in programming markets**
- **MVPDs that purchase programming will pay higher prices and be burdened with more restrictive terms and conditions for this programming which will be passed on to subscribers**
- **Regions in which the effects of the proposed combination will be most serious**
  - **Regions served by both an NBC O&O and a Comcast RSN**
  - **Regions served only by a Comcast RSN**



# Competitive Harms Post-Combination

## Horizontal Harms: A Simple Example

- One MVPD purchases two networks
- Value of networks to MVPD  
Profit with one network = \$1.00; Profit with two networks = \$1.50
- Remark: Marginal profit of adding first network = \$1.00  
Marginal profit of adding second network = \$.50
- Suppose that the programmer can charge a price equal to the marginal effect of its programming on the MVPD's profit
- Case #1: Two different programmers each offer one of the networks
  - Each programmer can charge \$.50 for its network
  - Total cost of networks = \$1.00
- Case #2: A single programmer owns both of the networks
  - The programmer can charge \$1.50 for the bundle
  - Total cost of networks = \$1.50
- Note that the same logic applies even if the programmers can extract only a fraction of the marginal profit, e.g. , suppose that programmers can extract the share  $\alpha$  of the marginal profit where  $\alpha$  is between 0 and 1
  - Case #1: Each programmer charges  $\alpha \times \$0.50$  for a total of  $\alpha \times \$1.00$
  - Case #2: The programmer charges  $\alpha \times \$1.50$  for the bundle
- Standard practice in economics literature is to set  $\alpha = \frac{1}{2}$



# Competitive Harms Post-Combination

## Horizontal Harms: Evidence

There are numerous instances of programmers combining or colluding to extract additional rents...

- **“Corpus Christi Consent Decree” (1996)**
  - The DOJ filed an antitrust complaint against several broadcasters in a market for engaging in a combination to increase the price of retransmission rights. The consent decree found that the broadcasters had restrained competition and enjoined them from agreeing to bargain jointly.
- **Suddenlink *ex parte*, December 14, 2009**
  - “Where a single entity controls retransmission consent negotiations for more than one Big 4 station in a single market, the average retransmission consent fees Suddenlink pays for such entity's Big 4 stations (in all Suddenlink markets where the entity represents one or more stations) is 21.6% higher than the average retransmission consent fees Suddenlink pays for other ‘Big 4’ stations in those same markets.”
- **DirectTV/Dish/Insight *ex parte*, December 14, 2009**
  - “A station that controls the availability of NBC programming in a market has market power, but a station that simultaneously controls both NBC *and* FOX programming in that market has far greater market power.”
- **Empirical Evidence of ACA Members**



# Competitive Harms Post-Combination

## Horizontal Harms

### TV Markets with both NBC O&O and Comcast RSN

Chicago\* (3,501,010) #3

Philadelphia (2,955,190) #4

Dallas-Ft. Worth\* (2,544,410) #5

San Francisco-Oakland-San Jose\* (2,503,400) #6

Washington, DC (Hagerstown) (2,335,040) #9

Miami-Ft. Lauderdale\* (1,538,090) #17

Hartford-New Haven (1,010,630) #30

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**7 TOTAL MARKETS (16,427,770) [14.30%]**

Based on 2010 Total U.S. TV Homes: 114,866,380 Households

NOTE: All TV markets above include a Comcast system, except Dallas

\*TV Market also includes Telemundo O&O

# Competitive Harms Post-Combination

## Horizontal Harms

### TV Markets with Comcast RSN and without NBC O&O

Atlanta	Lafayette, IN
Augusta-Aiken	Memphis
Baltimore	Meridian
Boston (Manchester)*	Monroe-El Dorado
Champaign-Springfield-Decatur	Monterey-Salinas
Charleston, SC	Nashville
Charlottesville	Panama City
Chattanooga	Peoria-Bloomington
Chico-Redding	Portland, OR
Colorado Springs-Pueblo	Providence-New Bedford
Denver*	Richmond-Petersburg
Eugene	Roanoke-Lynchburg
Ft. Myers-Naples-Grand Junction-Montrose	Rockford-Freeport
Ft. Wayne	Sacramento-Stkton-Modesto
Harrisburg-Lancaster-Lebanon-York	Salisbury
Harrisonburg	Savannah
Hattiesburg-Laurel	Seattle-Tacoma
Houston	South Bend-Elkhart
Huntsville-Decatur	Spokane
Jackson, MS	Springfield-Holyoke
Jacksonville	Tallahassee-Thomasville
Johnstown-Altoona-State College	West Palm Beach-Ft. Pierce
Knoxville	Wilkes Barre-Scranton

NOTE: Total # of TV homes in the DMAs with a Comcast RSN and without an NBC O&O stations is 27,889,120 or 24.28% of all homes. All TV markets above include a Comcast system. \*TV market also includes Telemundo O&O.

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# Competitive Harms Post-Combination

## Vertical Harms: Theory


- **All programmers, including NBC, use the threat of withdrawal of programming as a lever to negotiate higher programming prices from MVPDs**
- **Any change in circumstances that lowers the cost to NBC of withdrawing programming will increase the credibility of its threat to withdraw programming and therefore will increase its ability to force MVPDs to accept higher programming prices**
- **Comcast's combination with NBC reduces the cost to the merged entity of withdrawing programming from rivals of Comcast cable**
  - **When Comcast withdraws programming from rival MVPDs, some customers will switch to Comcast and Comcast earns profits on the customers who switch**
  - **These profits offset the cost to Comcast of withdrawing programming and therefore reduce the net cost of withdrawing programming**
- **As a consequence, because of the combination, Comcast will be able to bargain for higher programming prices for programming previously owned by NBC than NBC would otherwise be able to negotiate on its own**
- **Consumers will be harmed by the takeover because these higher programming prices will be passed through to them**

# Competitive Harms Post-Combination

## Vertical Harms

### TV Markets with Comcast Cable Systems

Albuquerque-Santa Fe	Harrisburg-Lancaster-Lebanon-York	Pittsburg
Atlanta	Harrisonburg	Portland, OR
Augusta-Aiken	Hartford-New Haven	Providence-New Bedford
Baltimore	Hattiesburg-Laurel	Quincy-Hannibal-Keokuk
Boston (Manchester)	Houston	Richmond-Petersburg
Burlington-Pittsburg	Huntsville-Decatur	Roanoke-Lynchburg
Champaign-Springfield-Decatur	Indianapolis	Rockford-Freeport
Charleston, SC	Jackson, MS	Sacramento-Stkton-Modesto
Charlottesville	Jacksonville	Salisbury
Chattanooga	Johnstown-Altoona-State College	Salt Lake City
Chicago	Knoxville	San Francisco-Oakland-San Jose
Chico-Redding	Lafayette, IN	Savannah
Colorado Springs-Pueblo	Lansing	Seattle-Tacoma
Denver	Miami	South Bend-Elkhart
Detroit	Meridian	Spokane
Eugene	Minneapolis-St. Paul	Springfield-Holyoke
Flint-Saginaw-Bay City	Monroe-El Dorado	Tallahassee-Thomasville
Fresno-Visalia	Monterey-Salinas	Tri Cities, TN/VA
Ft. Myers-Naples-Grand Junction-Montrose	Nashville	Tucson
Memphis	New York	Washington, DC
Ft. Wayne	Panama City	West Palm Beach-Ft. Pierce
Grand Rapids	Peoria-Bloomington	Wheeling-Steubenville
	Philadelphia	Wilkes Barre-Scranton



# **Analysis of Vertical Effects: Flaw with Simply Calculating Stand-Alone Profitability of Program Withdrawal**

- **FCC test to assess competitive harms in the News Corp/Direct TV vertical merger focused on stand-alone profit from temporary or permanent program withdrawal**
- **News Corp Methodology**
  - Calculate effect on profit (S) by examining loss in programming profit from withdrawal (L) and gain in MVPD profit due to customer switching (G) ( $S=G-L$ )
  - FCC concludes that a sufficient condition for a vertical merger to create significant competitive harms is that it creates a situation where the value of switching exceeds the loss of programming profit ( $S>0$ )
- **Flaw in News Corp Methodology**
  - The condition –  $S>0$  – is sufficient but not necessary for there to be competitive harm
  - Competitive harm arises to the extent the vertical combination causes programming prices to rise
  - A vertical combination will cause programming prices to rise to the extent that it increases the programmer's opportunity cost of providing programming to MVPDs that it competes with, which can occur even if  $S<0$
  - The better approach is to measure directly the increased opportunity cost and therefore the extent to which prices will rise
- **Subsequently, FCC used Methodology Similar to “Better Approach” in Adelphia/Comcast/TimeWarner**



# Analysis of Vertical Effects: Flaw with Simply Calculating Stand-Alone Profitability of Program Withdrawal – An Example

## The Situation:

- One seller and one buyer
  - Seller already owns the good
  - The good is of no value to the seller and there is only one possible buyer
  - Good is worth \$200 to the buyer
- What price will the buyer and seller negotiate?
    - If seller could make a take-it-or-leave-it offer to the buyer, he would offer \$200, and it would be accepted
    - If buyer could make a take-it-or-leave-it offer to the seller, he would offer \$0, and it would be accepted
    - Economic theory suggests that in general the price the buyer and seller negotiate will be somewhere between the lowest price the seller would accept and the highest price the buyer would pay –

$$p = (1 - \alpha) \$0 + \alpha \$200$$

where  $\alpha$  is a parameter between 0 and 1 interpreted as the strength of the seller's bargaining power

- In the absence of any other information, it is reasonable to set  $\alpha$  equal to  $\frac{1}{2}$ . (Nash Bargaining Solution)

$$p = \$100$$



# Analysis of Vertical Effects: Flaw with Simply Calculating Stand-Alone Profitability of Program Withdrawal – An Example

- Now suppose that the seller owns another business that competes with the buyer's business and that the seller's profits in the other business will be reduced by \$50 if he sells the good to the buyer
- Predicted price from Bargaining Theory:  
Lowest price seller will accept = \$50  
Highest price buyer will pay = \$200  
$$p = \frac{1}{2} \$50 + \frac{1}{2} \$200$$
$$= \$125$$
- The fact that the minimum price the seller will accept goes up by \$50 results in him being able to negotiate a price that is \$25 higher
- This is true even though the stand alone profitability of withdrawal does NOT become positive
  - Stand-alone profitability of withdrawal before the change  
= -\$100
  - Stand alone profitability of withdrawal after the change  
= -\$100 + \$50  
= -\$50



# **Analysis of Vertical Effects:**

## **Flaw with Simply Calculating Stand-Alone Profitability of Program Withdrawal – An Example**

- **Costs would have to rise to over \$100 before the stand alone profit from withdrawal would become positive**
- **Example**
  - **Suppose costs rise to \$120**
  - **Stand alone profit from withdrawal =  $-\$100 + \$120$  or  $\$20$**
- **NewsCorp approach to estimating vertical harm**
  - **Any merger that raised costs by \$100 or less would not cause any significant harm**
- **ACA approach (similar to Adelphia) to estimating vertical harm**
  - **A merger that raised costs by  $\$x$  would likely result in a price increase of  $\$x/2$**
- **The main point:**
  - **The stand alone profitability of withdrawal is positive if costs rise above the current price level**
  - **It is certainly true that prices will have to rise if costs rise above the current price level**
  - **However, significant increases in cost will generally cause significant increases in prices even if the costs do not rise by enough to make the stand alone cost of withdrawal positive**



# Analysis of Vertical Effects: Estimation of Price Increases from Comcast/NBCU Vertical Combination

- The Players
  - One vertically integrated firm consisting of a programmer and an affiliated MVPD
  - One unaffiliated MVPD
- Notation:  $n$  -- number of subscribers to unaffiliated MVPD  
 $\pi_M$  -- profit that affiliated MVPD earns per subscriber  
 $d$  -- fraction of unaffiliated MVPDs subscribers that will leave the MVPD if the program is withdrawn  
 $\alpha$  -- fraction of the leaving customers that switch to the affiliated MVPD
- The cost of providing programming to the unaffiliated MVPD is equal to the lost programming profit of the affiliated MVPD  
$$= d\alpha\pi_M n$$
- Let  $C$  denote the per subscriber cost created by vertical integration  
$$C = d\alpha\pi_M$$
- Let  $\Delta P$  denote the induced price change. Following the Nash Bargaining Model  
$$\Delta P = C/2$$
$$= d\alpha\pi_M/2$$



# Analysis of Vertical Effects: Estimation of Price Increases from Comcast/NBCU Vertical Combination

- To estimate plausible ranges of values for the price increase caused by the combination using the formula --

$$\Delta P = d\alpha\pi_M/2$$

we need to determine plausible ranges of values for three parameters:

- $\pi_M$  -- Profit that affiliated MVPD earns per subscriber
  - $d$  -- Fraction of unaffiliated MVPD's subscribers that will leave the MVPD if the program is withdrawn
  - $\alpha$  -- Fraction of the leaving customers that switch to the affiliated MVPD
- Precise determination of the most accurate possible range of values for each parameter will require careful review of all available evidence, including the non-publicly disclosed information provided by Comcast and will need to be done on a market-by-market basis



## **Current Program Access Rules Provide Inadequate Relief for Vertical Harms**

- **Program access rules place no restriction on quantity discounts**
- **Can avoid any constraint on the prices it charges its competitors by raising the internal transfer price**
- **No automatic right to continued carriage of programming while case is pending**
- **Lack of certainty that Program Access rules apply to rights for provision of online services**



# **Arbitration Conditions of Past Mergers Provide Inadequate Relief for Vertical Harms**

- **Very costly, an especially important problem for ACA members**
- **Arbitration applies only to RSNs and retransmission consent but not to national cable networks**
- **The “quantity discounts” loophole is not clearly blocked**