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Hearing on “Examining the Comcast-Time Warner Cable Merger and the Impact on Consumers”

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Mr. Chairman, Ranking Member Grassley, and Members of the Committee, I am grateful for the opportunity to offer my views on the impact that the proposed merger between Comcast and Time Warner Cable would have on consumers. Concerns focus on two distinct markets: (1) the market for the distribution of traditional cable television and (2) the market for broadband Internet access. In short, established principles of antitrust and communications law dictate that the merger is unlikely to harm consumers in either market. In fact, technological and economic changes are transforming the markets in ways that should make the prospect of anticompetitive harms even more remote.

I. Traditional Multichannel Video

The first relevant market involves the distribution of traditional cable networks. In this market, cable operators enter into three types of transactions. First, they pay television networks such as ESPN, Nickelodeon, and the Disney Channel for the rights to retransmit video programming. Second, they collect subscription fees from consumers who wish to view that programming. Third, they receive revenue from local advertisers who wish to reach local subscribers. Although each market should be analyzed separate, the end conclusion is the same in each case, that is, none of these markets is structured so that the merger is likely to harm consumers.

A. End-User Subscriptions

With respect to subscribers, cable operators in different cities serve different geographic markets and as a result do not compete with one another. In short, consumers would have the same number of choices of multichannel video providers the day after merger that they did the

day before. Thus, a merger between cable operators serving different cities should not affect the prices that subscribers pay for cable television subscriptions.¹

B. Video Programmers

The geographic scope of the market in which cable operators contract with video programmers is very different from the one in which cable operators contract with subscribers. As both the Federal Communications Commission (FCC) and the U.S. Court of Appeals for the D.C. Circuit have recognized, video programmers do not really care if they reach viewers in any particular metropolitan area. Instead, their primary concern is whether they can reach a sufficient number of customers to achieve minimum viable scale.² The proper geographic scope of this market is thus national. For them, it is national reach, not local reach that matters.³

Any arguments that that the merger would create anticompetitive harms to video programmers must overcome one potentially insuperable obstacle. On two occasions, the FCC attempted to institute rules prohibiting cable operators from controlling more than 30% of the nation's multichannel video subscribers in order to protect the interests of video programmers. On both occasions, the courts invalidated the rules because the FCC's rationale for imposing the 30% limit was arbitrary and capricious. In both cases, the court indicated that the available evidence suggested that cable operators could control much larger shares of the national market without harming video programmers, driven largely by the advent of competition from direct broadcast satellite (DBS) providers, such as DirecTV and the Dish Network.⁴

Given that the merging parties have committed to reduce their holdings so that the resulting company will control no more than 30% of the national market, these court decisions essentially foreclose arguments that anticompetitive harms to video programmers would justify blocking the merger. Indeed, the courts' analyses were based on the competitive environments that existed in 2001 and 2009. Since that time, these markets have become even more competitive. The number of multichannel video subscribers has increased from 96 million to 101 million by 2012.⁵ Thus, even under the specious justification for the 30% threshold rejected by the courts, the percentage of the national market that one cable operator can control should rise above 30% without causing any harm to video programmers. Since that time, Verizon's FiOS and AT&T's U-verse networks have expanded their customer bases. Internet-based video platforms such as Netflix, Amazon, Hulu, Google, Roku, and Apple have emerged as significant market players. In addition, the costs of program acquisition have risen sharply, as program providers have increased their bargaining power.

These considerations suggest that the merger would not create an industry structure that would raise concerns about anticompetitive harms to video programmers under established principles of antitrust and communications law. Even if such concerns had merit, however, they

¹ See Christopher S. Yoo, *Vertical Integration and Media Regulation in the New Economy*, 19 YALE J. ON REG. 171, 222 (2002).

² See *Comcast Corp. v. FCC*, 579 F.3d 1, 4, 7 (D.C. Cir. 2009) (citing Commission's Cable Horizontal and Vertical Ownership Limits, Fourth Report and Order and Further Notice of Proposed Rulemaking, 23 FCC Rcd. 2134, 2162 (2008)); *Time Warner Entm't Co. v. FCC*, 240 F.3d 1126, 1131 (D.C. Cir. 2001) (citing Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992, Third Report and Order, 14 FCC Rcd. 19098, 19114–16 ¶¶ 40–41 (1999)).

³ Yoo, *supra* note 1, at 227.

⁴ See *Comcast*, 579 F.3d at 6–8; *Time Warner Entm't*, 240 F.3d at 1132.

⁵ See Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming, Fifteenth Report, 28 FCC Rcd. 10496, 10499 ¶ 3 (2013) [hereinafter Fifteenth Video Competition Report].

are properly addressed by the program carriage and access rules that the FCC has developed to address just these problems. Commissioners of the Federal Communications Commission (FCC) and commentators have long criticized the use of merger conditions as a mechanism for making policy.⁶ Traditional notice-and-comment rulemaking promotes public participation. By their nature, merger conditions restrict conduct permitted by the existing rules (otherwise the restriction would be imposed by general regulation rather than by the order clearing the merger). The problem is that they are imposed outside of the normal regulatory processes, and even when orders clearing the merger are subject to notice and comment, the resolution of the issues is more likely to be driven by the issues raised by a particular transaction and less likely to yield a clear statement of agency policy.

In many cases, merger conditions address conduct that is not the result of the merger, and in most, if not all, cases, these issues addressed by the merger conditions are the subject of ongoing proceedings before the FCC. The use of company-specific adjudications to address issues that confront the entire industry threatens to skew the competitive landscape and raises serious issues of fairness. Moreover, merger conditions often cannot be appealed, because the voluntariness of the commitment may well immunize it from meaningful judicial review.

At best, the use of the merger review process to impose conditions represents a source of delay and uncertainty that reduces the industry's ability to adjust to a rapidly changing and increasingly challenging technological and economic landscape. At worst, it represents a form of backdoor regulation that hurts consumers, singles out individual companies for restrictions that could not necessarily withstand the rigors of normal regulatory processes, and undermines democratic values as well as the integrity of agency processes.

C. Local Advertising

Finally, the merger is unlikely to harm the market for local advertising. The reason is simple: although cable television *networks* receive significant amounts of national advertising, the limited reach of local cable *operators* limits them to local advertising. The fact that local advertising occurs in different geographic markets means that, as was the case with cable

⁶ See, e.g., Applications of AT&T Inc. and Centennial Communications Corp., Memorandum Opinion and Order, 24 FCC Rcd. 13915, 13972 ¶ 141 (2009); Verizon Communications Inc. and MCI, Inc., Memorandum Opinion and Order, 20 F.C.C.R. 18433, 18573 (2005) (separate statement of Abernathy, Comm'r); Applications for Consent to the Transfer of Control of Licenses and Section 214 Authorizations by Time Warner Inc. and America Online, Inc., Transferors, to AOL Time Warner Inc., Transferee, Memorandum Report and Order, 16 F.C.C.R. 6547, 6713 (2001) (Powell, Comm'r, concurring in part and dissenting in part); Applications of Ameritech Corp., Transferor, and SBC Communications Inc., Transferee, Memorandum Opinion and Order, 14 F.C.C.R. 14712, 15197-200 (1999) (Powell, Comm'r, concurring in part and dissenting in part); *id.* at 15174-96 (Furchtgott-Roth, Comm'r, concurring in part and dissenting in part); Application of Worldcom, Inc. and MCI Communications Corp. for Transfer of Control of MCI Communications Corp. to Worldcom, Inc., Memorandum Report and Order, 13 F.C.C.R. 18025, 18166 (1998) (separate statement of Powell, Comm'r); *id.* at 18159 (separate statement of Furchtgott-Roth, Comm'r). For commentators' criticisms of the merger conditions, see Rachel Barkow & Peter Huber, *A Tale of Two Agencies: A Comparative Analysis of FCC and DOJ Review of Telecommunications Mergers*, 2000 U. CHI. LEGAL F. 29, 54, 62-66, 69-81; Harold Furchtgott-Roth, *The FCC Racket*, WALL ST. J., Nov. 5, 1999, at A18; Bryan Tramont, *Too Much Power, Too Little Restraint: How the FCC Expands Its Reach Through Unenforceable and Unwieldy "Voluntary Agreements,"* 53 FED. COMM. L.J. 49, 51-59 (2000); Daniel E. Troy, *Advice to the New President on the FCC and Communications Policy*, 24 HARV. J.L. & PUB. POL'Y 503, 505-09 (2001); Philip J. Weiser, *Institutional Design FCC Reform and the Hidden Side of the Administrative State*, 61 ADMIN. L. REV. 675, 708-11 (2009); Christopher S. Yoo, *New Models of Regulation and Interagency Governance*, 2003 MICH. ST. DCL L. REV. 701, 704.

television and broadband Internet subscribership, the merger will not cause any reduction in competition. FCC data indicates that cable television represents a minor share of local advertising revenues.

Figure 1: Local Advertising Revenues by Sector (\$million)

Sector	2011 act.	Share	2012 proj.	Share
Broadcast television	10,308	15%	11,802	17%
Cable television	4,164	6%	4,867	7%
Radio	11,264	16%	11,405	16%
Internet	11,602	17%	12,274	17%
Daily newspaper	16,915	25%	15,720	22%
Regional sports networks	842	1%	925	1%
Mobile	974	1%	2,064	3%
Telco	161	0%	230	0%
Other	12,313	18%	11,061	16%
Total	63,543	100%	70,348	100%

Source: Fifteenth Video Competition Report, *supra* note 5, at 10597 tbl.20.

Given the minor role that cable television plays in local advertising markets, it is hard to see how the merger could lead to anticompetitive harms. Moreover, the large amount of innovation that is occurring is likely to make the market for local advertising increasingly competitive in the near future.

II. Broadband Internet Access

With respect to broadband Internet access, the merged company would engage in two types of transactions. First, it would collect subscription fees from consumers who wish to access the Internet. Second, it would contract to interconnect with other Internet service providers to receive traffic that other end users and edge providers would like to send to current Comcast and Time Warner Cable subscribers and to terminate the off-network traffic that Comcast and Time Warner Cable subscribers generate. For reasons, I discuss below, the proposed merger is even less likely to create anticompetitive harms in the market for broadband Internet access than in the market for traditional multichannel video.

A. End-User Subscriptions

As was the case with traditional multichannel video, the lack of any overlap in the areas served by Comcast and Time Warner Cable again makes it unlikely that the merger would affect the prices charged to subscribers.

In addition, for reasons I detail in my recent article in the *Harvard Law Review*, the number of options that end users enjoy is increasing rapidly. Take digital subscriber lines (DSL), for example. Although many commentators have written DSL off for dead, a number of new technologies, including IP DSLAMs, pair bonding, and vectoring, are increasing the bandwidth that DSL can deliver. AT&T's Velocity IP initiative is expanding the reach of its

DSL network and increasing download speeds to 45 Mbps, with 90% receiving 75 Mbps and 70% receiving 100 Mbps.⁷ CenturyLink is following a similar strategy.

Those who have pointed to Verizon's decision not to expand its FiOS coverage any further to suggest that fiber-to-the-home (FTTH) is moribund outside of its current service area did not count on Google Fiber. After beginning in Kansas City and expanding to Provo and Austin, Google recently announced its intention to extend FTTH coverage to thirty-four additional cities.

In addition, wireless broadband providers are in a race to buildout LTE. Although some commentators have questioned whether LTE can deliver the speeds needed to become viable substitute to fixed-line broadband, industry studies indicate that LTE achieves an average download speed of 12 Mbps and peak download speeds of 50 Mbps when viewers only need 8 Mbps to view high-definition television (HDTV). In addition, the LTE market allows for competition among multiple providers. Verizon completed its LTE buildout in mid-2013 and now serves 96% of the U.S. population. AT&T's LTE network reached 85% of the U.S. population by the end of 2013 and plans to reach 96% by the end of 2014. Sprint and T-Mobile each reached roughly two-thirds of the U.S. population by the end of 2013 and are hurrying to finish their deployments. And waiting in the wings is the next-generation technology known as LTE Advanced, which is already delivering of 150 to 300 Mbps in South Korea and Australia. It thus comes as no surprise that 10% of U.S. households have abandoned fixed-line service and rely entirely on mobile devices for their Internet access. This number is only likely to increase in the future.⁸

B. Peering and Transit

Cable operators also enter into contracts with other Internet service providers (ISPs) to exchange traffic originating or terminating on other networks. Typically, the originating ISP is the only one to receive direct payment from end users. Because the terminating ISPs also incur costs, the traditional rule was that the originating ISP would make what is known as a transit payment to compensate the terminating ISP for the costs it incurs serving the originating ISPs customers. If traffic is roughly symmetrical, ISPs can reduce costs by foregoing monitoring and billing for the exchange of traffic and instead calling it a wash, a practice commonly known as settlement-free peering. Such arrangements make economic sense only if the traffic exchanged is symmetrical. If traffic becomes out of ratio, peering contracts typically call for transit-style payments. Thus, although peering is often misrepresented as zero-price interconnection, it is more properly regarded as a form of barter and is conditional on an even exchange.

Consider what would happen if one of the parties to a peering contract suddenly increased the amount of traffic that it was handing off to the other party for termination. The terminating ISP would have to incur significant costs to terminate the traffic. Certainly, the originating ISP would like the terminating ISP to bear all of the costs of doing so. Conversely, the terminating ISP would like the originating ISP to pay for the costs, as required by the typical peering contract. Both parties benefit from delivering greater value to the end users. The usual solution would be for both parties to bear part of the costs.

Indeed, this is exactly what appears to be occurring in the recent interconnection agreement between Comcast and Netflix. Netflix has been a spectacular success, growing to

⁷ Christopher S. Yoo, *Technological Determinism and Its Discontents*, 127 HARV. L. REV. 915, 919 (2014).

⁸ *Id.* at 923–26.

roughly one-third of all primetime Internet traffic in the U.S. Like any for-profit company, it would prefer it if the ISPs bore as much of the burden of the additional costs of carrying this traffic as possible. Indeed, that is the gist of its Open Connect program, which requires ISPs to terminate Netflix traffic for free. Some ISPs have embraced Open Connect. Others have resisted. All of this is a natural part of healthy bargaining process. As in the typical case, both sides reached an interconnection agreement that divides the costs. The terms represent nothing more than a garden-variety bargain over price that characterizes every arms-length economic transaction.

Although some have suggested that such interconnection agreements represent network neutrality violations, network neutrality only applies to how traffic is handled *within* an ISP's network. It does not apply to how the traffic arrives at an ISP, which inevitably travels by paths of different lengths and incurs different costs as it traverses a system composed of 30,000 separate networks tied together through arms-length interconnection agreements. Indeed, this is why the Open Internet Order specified that it does not apply to interconnection agreements⁹ and why FCC Chairman Julius Genachowski made clear that the Open Internet Order does not apply to interconnection disputes, such as the prior dispute between Comcast and Level 3.¹⁰

The Comcast-Netflix interconnection agreement appears to be nothing more than a typical case of such bargaining. The agreement reduces Comcast's costs. The impact on Netflix is ambiguous: while it now must pay Comcast to terminate its traffic, it no longer needs to pay the third-party ISP on which it previously relied to reach Comcast in a classic case of efficiencies through cutting out the middleman. Although some have suggested that this might lead to a net reduction in Netflix's costs, that information is confidential and cannot be verified. In any event, interconnection represent a trivial revenue stream for Comcast and a tiny portion of Netflix's cost structure, which is dominated by program acquisition costs, which means that the transaction is unlikely to have any material effect.¹¹

In addition, interconnection in the Internet space is fundamentally different from carriage agreements in cable television. In cable television, the failure to come to an agreement means that subscribers cannot receive particular content. With respect to the Internet, multiple ways to reach consumers always exist. In fact, Comcast maintains 40 settlement-free peering relationships and over 8,000 paid transit relationships. That means that edge providers will always have some way to reach Comcast customers even if they are unable to reach an direct interconnection agreement. The only bargaining advantage that Comcast would enjoy is the difference between the direct interconnection terms and the cost of Netflix's next-best interconnection option. Although some have speculated that Comcast might still be able to discriminate against Netflix traffic flowing over other paths, that traffic is mixed with the traffic of other end users, which would require Comcast to inspect all of the traffic coming through that connection, which would be unrealistic and prohibited by Comcast's commitment to abide by the terms of the Open Internet Order.

As an added benefit, absent the interconnection agreement, all of Comcast's customers would have had to bear the costs of Netflix's increase in traffic regardless if they used Netflix or

⁹ Preserving the Open Internet, Report and Order, 25 F.C.C.R. 17905, 17944 n.209 (2010).

¹⁰ *Network Neutrality and Internet Regulation: Warranted or More Economic Harm than Good?*, Hearing before the Subcomm. on Communications and Technology, H. Comm. on Energy and Commerce, 102d Cong., 1st Sess. 102 (2011), available at <http://www.gpo.gov/fdsys/pkg/CHRG-112hhr65940/pdf/CHRG-112hhr65940.pdf>.

¹¹ Dan Rayburn, *Here's How the Comcast & Netflix Deal Is Structured, with Data & Numbers*, STREAMING MEDIA BLOG, Feb. 27, 2014, <http://blog.streamingmedia.com/2014/02/heres-comcast-netflix-deal-structured-numbers.html>.

not. The interconnection agreement promotes fairness by ensuring that those who derive the benefits are the ones who end up paying for it. The elimination of zero-cost pricing also avoids the problems that arise when edge providers have no incentive to economize on the volume of traffic they send, as well as address the legal concerns raised by Judge David Tatel in his decision in *Verizon v. FCC*.¹²

Any remaining concerns should be eliminated by the fact that Comcast has committed to abide by the terms of the FCC's Open Internet Order even though it was struck down by the courts. In fact, the merger would extend this benefit to all of Time Warner Cable's customers as well.

Conclusion

In closing, it bears keeping in mind how dynamic and unpredictable this sector has been. Consider February 29, 2000, when Time Warner was before this Committee to discuss its merger with America Online. What many predicted would be the end of history ended up simply being the end of \$200 billion in Time Warner shareholder value. In addition, just a few short years ago, many argued that fiber-to-the-home would soon consign the cable industry to the dustbin of history. These episodes underscore how easy it is to hypothesize problems that never materialize and how easy it is to forget that innovation and willingness to undertake commercial risk have created greater consumer benefits than anyone could have anticipated.

¹² *Verizon v. FCC*, 740 F.3d 623, 658 (D.C. Cir. 2014).