Testimony of

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NCTA
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NATIONAL CABLE & TELECOMMUNICATIONS ASSOCIATION
VIDEO COMPETITION IN 2005:
NEW CHOICES FOR CONSUMERS
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Mr. Chairman, members of the Subcommittee, my name is Kyle McSlarrow and I am President and CEO of the National Cable & Telecommunications Association. NCTA is the principal trade association for the cable television industry in the United States. It represents cable operators serving more than 90 percent of the nation's 66 million cable television households and more than 200 cable program networks, as well as equipment suppliers and providers of ancillary cable services. NCTA's member companies provide consumers with a wide variety of quality services, including video (digital and analog), High Definition Television (HDTV), high speed access to the Internet (cable modem service), and telephone service (both traditional circuit-switched and Voice over Internet Protocol).

Thank you for inviting me to testify today about the state of competition in the video marketplace. You have asked specifically whether the video marketplace in 2005 offers consumers "more consolidation or new choices." The answer is clearly new choices.

The video marketplace is more competitive than ever before. Just ten years ago, cable was a one-way analog video service which enjoyed 95 percent of the multichannel television market. Today, it is only one of many interactive broadband platforms that provide a variety of voice, video, and data services - many of them digital. Thanks to fierce competition from two Direct Broadcast Satellite (DBS) providers, EchoStar and DirecTV, cable's market share has fallen to 69 percent. And now the Regional Bell Operating Companies (RBOCs) are entering the fray, bringing with them an annual revenue stream of $150 billion - about three times that of the cable industry.

There is a fierce battle going on today between cable, satellite, and telephone companies to provide television households with state-of-the art video services - and new providers are entering the field every day, including Internet-based services, video cell phone providers, wireless computer manufacturers, and consumer electronics suppliers. Consumers are the beneficiaries of this highly competitive landscape, where they enjoy a wide array of advanced video services, diverse programming, and the ability to choose from among at least three multichannel providers.

Evidence of a highly competitive marketplace can be found not only in the choices available to consumers but also in the conduct of cable operators and their competitors. When DBS began to offer consumers an alternative with more channels, more pay-per-view movies, and digital audio

and video, cable operators embarked on a $100 billion, nationwide upgrade of their facilities (see Appendix A). With additional capacity and digital capability, cable operators began to offer new tiers of digital programming, along with video-on-demand and digital video recording capability. Cable expanded its video services to offer high definition television programming. Cable also increased the quality and diversity of its programming and pioneered commercial high-speed Internet service.

The availability of bundled video, data, and voice services and the introduction of interactive broadband services by cable operators prompted a competitive response from other industries. Telephone and DBS companies, for example, joined forces to offer their own packages of video, voice, and data services. Today, Verizon and SBC are investing billions of dollars to enter the video marketplace while cable is seeking to develop Voice over Internet Protocol (VoIP) service to better compete with the incumbent telephone companies.

The bottom line is that these are all signs of a competitive marketplace: several different providers of a wide array of services vie with each other for customers, each trying to differentiate themselves with unique offerings while trying to match those of their competitors.

II. CABLE FACES VIGOROUS COMPETITION IN THE VIDEO MARKET

Today, consumers can choose from a variety of multichannel video providers. The Federal Communications Commission (FCC) reported in January 2005 that "almost all U.S. consumers have the choice between over-the-air broadcast television, a cable service, and at least two direct broadcast satellite (DBS) providers." In some areas, the FCC found, "consumers also can choose to receive service via one or more emerging technologies, including digital broadcast spectrum, fiber, and video over the Internet." The net result is that "consumers today have viable choices in the delivery of video programming, and they are exercising their ability to switch among MVPDs." In addition, "through the use of advanced set-top boxes and digital video recorders, consumers are now able to maintain more control over what, when, and how they receive information."

DBS continues to increase its share of MVPD customers, while cable fights back to maintain and enhance the value and attractiveness of its service. Cable also competes with a host of other video delivery media, including broadband service providers (BSPs), utilities, municipal overbuilders, Internet video providers, broadcasters and home video outlets. As a result of this competition, 28.3 million consumers (more than one out of four video subscribers) now obtain multichannel video programming from some company other than their local cable operator.

Subscribers to Multichannel Video Program
Distributors (MVPDs), March 2005

Subscribers (in Millions)	Percent of Total MVPD Subscribers
DBS (high power satellite) 25.40	27.43%
C-Band (low power satellite) 0.30	0.32%
MMDS (microwave) 0.10	0.11%
SMATV (private apt/condo) 1.10	1.19%
Broadband Competitors 1.40	1.51%
Non Cable MVPD 28.30	30.56%
Cable 64.30	69.44%

Total MVPD 92.60 100.00%

Sources: NCTA estimates based on data from Kagan Research LLC, Kagan Media Money, and Nielsen Media Research.

Direct Broadcast Satellite

DBS and cable presently compete for every customer, old and new. DBS companies currently have more than 26 million customers compared with none 11 years ago. The two nationwide DBS providers now serve more than 27 percent of all multichannel video households and their penetration is 25 percent or greater in at least 25 states. In the second quarter of 2005, surpassing analysts' predictions, DirecTV increased its subscriber base by a record 505,000 net customers, while EchoStar grew by 325,000 customers. DirecTV now has more customers (14.67 million) than all but one cable operator (Comcast). EchoStar, the second largest DBS provider with 11.46 million subscribers, ranks third among all MVPDs. Cable made significant gains in digital cable and high speed Internet customers in 2005, but its share of multichannel video customers has fallen below 70 percent.

DBS operators continue to experience strong subscriber growth in virtually every market where they offer local channel service. Indeed, DirecTV and EchoStar report that their total number of subscribers increased from 23.16 million to 26.13 million between June 2004 and June 2005, an increase of 12.8 percent. According to Strategy Analytics, "DBS has robbed cable of the slow-but-steady growth it enjoyed up until the late 1990s, but its broader impact has been to expand the total base of multichannel TV homes."

The Government Accountability Office (GAO) testified in 2005 that "DBS penetration rates have been and remain highest in rural areas, but since 2001, DBS penetration has grown most rapidly in urban and suburban areas, where the penetration rates were originally low... In short, over the 2001 to 2004 time frame, the DBS penetration rate grew about 50 percent and 32 percent in urban and suburban areas, respectively, compared with a growth rate of 15 percent in rural areas." As the following chart shows, DTH penetration of television households, as of August 2005, exceeded 30 percent in 10 states, 20 percent in 37 states, and 15 percent in 46 states.

States with Direct-To-Home (DTH) Dish Penetration
of Fifteen Percent or More (August 2005)

State	Penetration Rate	State	Penetration Rate
Vermont	41.59%	Arizona	25.09%
Utah	38.08%	South Carolina	25.01%
Montana	37.91%	Oregon	24.84%
Idaho	36.90%	Wisconsin	24.10%
Wyoming	35.49%	South Dakota	23.40%
Mississippi	33.59%	North Dakota	23.31%
Missouri	33.52%	Illinois	23.09%
Arkansas	32.08%	Alaska	22.70%

Georgia 30.75% Nebraska 22.59%
Colorado 30.09% Washington 22.54%
Oklahoma 29.17% Maine 22.40%
New Mexico 29.13% Michigan 22.25%
Alabama 27.40% Florida 21.97%
Indiana 27.18% Kansas 21.97%
Iowa 26.92% Ohio 18.34%
California 26.67% Nevada 18.29%
Tennessee 26.39% Louisiana 18.27%
Virginia 26.08% Maryland 17.79%
North Carolina 26.04% Delaware 17.56%
Texas 26.03% New York 16.57%
West Virginia 25.88% New Hampshire 16.50%
Kentucky 25.82% New Jersey 15.57%
Minnesota 25.31% Pennsylvania 15.16%

Source: SkyTRENDS SkyMAP, August 2005; www.skyreport.com; TV Household data from A.C. Nielsen.

In order to respond to the competition posed by DBS, cable has invested $100 billion in new equipment and facilities since passage of the Telecommunications Act of 1996 (Appendix A provides details on cable's investment and deployment of new services and technology). As a direct result of DBS's numerous channels and all-digital technology, cable has invested heavily in new digital services and introduced digital tiers - including HDTV, interactive program guides, video-on-demand, personal video recorders, and CD quality, commercial-free music channels. Cable's upgrades have provoked a competitive response from DBS, which is good for consumers. For example, DirecTV's CEO Chase Carey acknowledges that many cable operators have improved their video service in recent years, "which is why we have to continue to improve." In an effort to keep pace with cable's video-on-demand movie offerings, DirecTV and EchoStar have stepped up marketing and promotion of their pay-per-view movie services. In addition to EchoStar's stand-alone pay-per-view channels, the company's Dish on Demand service launched January 2005 with 30 titles downloaded to subscribers using the company's DISHPlayer Digital Video Recorder (DVR). DirecTV has promoted its pay-per-view business with discounts on recent Hollywood releases. EchoStar is rolling out the first portable DVR device, called the Pocket-Dish, in an effort "to get a leg up in its battle with cable and satellite TV rivals." EchoStar is also purchasing Cablevision's satellite assets. It has also teamed up with Frontier, a telecommunications provider, to offer a bundled package of satellite television, Internet and telephone service in 24 states. This is in addition to the joint marketing arrangements DirecTV and EchoStar have with Bell companies.

Broadband Service Providers and Municipal Overbuilders
Although DirecTV and EchoStar are cable's largest MVPD competitors at this time, cable operators continue to face competition from other facilities-based providers in major U.S. markets. Broadband service providers (BSPs) - which include independent, municipal, and CLEC overbuilders - are offering bundles of video, voice, and data services over a single

network. RCN, the largest BSP, has 371,000 cable subscribers and ranks as the twelfth largest MSO. It operates in major metropolitan areas, including San Francisco, Chicago, Boston, New York, and Washington, D.C. RCN's video, telephone, and high speed data service passes nearly 1.5 million homes.

Wide Open West (WOW), the fourteenth largest MSO, serves an estimated 292,500 subscribers, and passes an estimated 1.4 million homes. Knology Holdings, the twenty-first largest MSO, reports 179,800 cable subscribers, and passes 780,000 subscribers. Grande Communications, the thirtieth largest MSO, provides cable service to 85,400 subscribers and passes more than 325,000 homes.

Municipally-owned cable systems, in selected areas, also continue to compete with cable systems and other MVPDs. According to a survey by the American Public Power Association (APPA) of its members, conducted at the end of 2004, 102 municipally-owned utilities offered cable TV service. The APPA survey also reported that 81 municipally-owned utilities were offering cable modem or DSL service, and 52 municipal utilities offered telephone service.

Mobile Video

In just the last year, video programming distributors have introduced video over wireless phones and other portable devices. Verizon Wireless rolled out V Cast, a service that offers video programming to cellular telephone users, in February 2005. V Cast currently provides news updates, sports highlights, celebrity news, stock quotes and market information, weather, and games for $15 per month. Its television-like video, at high bit rates, allows customers to download music videos and other high quality content. It is also reportedly working on its own original, reality programming.

Sprint Corporation began broadcasting live video over its wireless phones in August 2004. Sprint PCS customers can now see news, video clips, and other content real time over their cell phone. MobiTV, a video service available to Sprint PCS, Cingular, and several regional carriers' customers, sends programs to cell phones and currently has 300,000 subscribers. Qualcomm recently introduced its TV-cell phone service, MediaFlo.

The drive to deliver TV content to portable devices is picking up steam, as some providers prepare to launch Hollywood films and short format cinema in the near term. HBO and Cingular Wireless are reportedly considering a wireless content distribution arrangement. In addition to making the network's existing programming available, HBO may create new entertainment channels for the service.

Meanwhile, Sony's new portable PlayStation game device, known as PSP, is another mobile video play. It is capable of downloading TV shows and video information. It has been called "a plasma screen in your pocket."

Cable operators are beginning to add wireless options to their bundle of services. Time Warner Cable, for example, began testing cell phone service in partnership with Sprint in Kansas City. Digital video recorders and video-on-demand services have fueled consumer awareness and appetite for the technology for watching TV shows whenever you like. It seems inevitable that video providers would offer the ability to watch TV wherever you like. Although still a nascent service, one survey predicts that about 125 million consumers will be watching mobile television on their wireless phone in five years.

Internet Video

The video landscape is marked not only by intense rivalry among cable, satellite and telephone

providers but also Internet-based video delivery systems. Consumers now have new ways to access video content - from digital cell phones and other portable devices to interactive websites to enhanced in-home consumer electronics and computer equipment with high definition DVD or streaming video-capability. Not surprisingly, Internet companies such as Yahoo and Google have declared themselves to be media companies offering multiple services to compete with cable.

As one observer put it, the ethos of New TV can be captured in a single sweeping mantra: anything you want to see, any time, on any device." Another stated it this way:
It's the key battleground in what promises to be one of the most bruising - and important- global corporate fights in the next couple of years. Telephone giants, cable titans, computer companies and consumer electronics makers are all vying to provide the next generation of high-tech entertainment - a single network or gadgets that lets you view photos, listen to music, record DVDs and tune into whatever TV programs you want to watch, whenever you feel like watching them.

There is no denying that this proliferation of new delivery modes - the combination of digital communications and computers with entertainment and immediate access to worldwide information - is making all industry players compete more aggressively to stay in the game. As one media analyst recently said, "from an investment standpoint, I don't think we've ever before seen such a competitive landscape."
The FCC has recognized that video provided over the Internet has grown and promises to become an increasingly strong participant in the video programming marketplace. Growing consumer demand for compelling content on the Internet combined with a burgeoning variety of broadband platforms is spurring this growth. As broadband Internet offers broadcast-quality video, consumers are increasingly turning to Internet-based means of accessing video content, including downloading movies and other high value video content traditionally available only through broadcast, cable, satellite or home video outlets. Libraries of video content, containing thousands of hours of video programming, are becoming available to consumers on a personalized, customized basis.

Internet companies are providing their own unique content or partnering with other established content providers and video distributors. New entrants, like Akimbo Systems, offer a mix of established TV programming and unique content via the Web. Akimbo charges $10 a month and offers about 1600 programs, some for an extra fee. The company's chief executive predicts that Akimbo "will do what eBay has done for retailing." Google, Yahoo! and Microsoft are developing video search engines to harness video content via their portal service. Over the past year, Yahoo! predicted a one billion subscriber base for its multiple media services by decade's end. BitTorrent, an Internet file-sharing method enables video enthusiasts to trade video files online. iFilm and other websites offer video clips to millions of customers. Wi-FiTV, a broadband Web site that features more than 200 TV channels from around the world, recently began service.
Program networks are enhancing their Internet presence to gain viewers and advertising dollars. These web "channels" contain specially made programming, short videos targeting niche interests, and repackaged TV content. MTV Overdrive, a mix of news, live performances and on-demand music videos launched in April. Networks such as Home & Garden Television, Food Network, CNN, Fox News Channel, and MSNBC are offering more video content on their sites.

According to one analyst, Internet advertising is headed toward a 25 percent increase over the last year, to upwards of $8.8 billion in 2005.

AOL saw a jump of 120 percent in its on-demand video streaming in 2004 and drew in five million viewers for its exclusive live coverage of the July 2, 2005, Live 8 concert. ManiaTV.com, the interactive television website, had 1.6 million users in July alone.
As Internet companies and website operators grow their video on-line businesses, consumer electronics manufacturers are developing ways to exploit the World Wide Web via equipment. Toshiba and Matsushita, for example, offer digital TVs that allow users to download and store online video, along with DVD recording capability. PC makers are developing new "media center" PCs that can play and record movies, television and music accessed on-line. As described by PC magazine online, "there is going to be a big battle for dominance in people's living rooms. What we've seen is a mini-explosion of set top boxes for Internet television." This flurry of announcements and deals in recent months shows that all players in the video marketplace are positioning themselves to compete in the IPTV arena.

Broadcasting
Broadcasters are still formidable competitors to cable and other multichannel providers. The competition for viewers is manifested in the battle for advertising dollars. After a 10-year decline in viewers aged 18 to 49, the broadcast networks posted an increase in this key demographic for the 2004-2005 television season. It all came down to the big four broadcast networks' crop of breakout hit shows. Some network shows turned in performances "akin to the days before cable became a serious competitor." This has boosted advertising commitments for the coming year on all broadcast networks.
While the broadcast share of television viewing has declined in recent years as television viewers have increasingly opted for the multitude of choices available on cable, broadcast television remains a potent force. Broadcasting's share of the viewing day continues to exceed 40 percent. Moreover, approximately 15 percent of television households do not subscribe to any multichannel service. These television households continue to find broadcast television alone or in combination with non-MVPD video sources (such as DVDs) to be their preferred means of receiving video programming - and a significant percentage of MVPD households include television sets that are not connected to multichannel service.

Home Video
In the heated battle for consumers' time and entertainment dollars, DVDs, video cassettes and laser discs continue to provide competitive alternatives to MVPD viewing options. There are approximately 47,000 DVD titles available for purchase or rental today, compared to 30,000 a year ago. Consumers spent $24.5 billion renting or purchasing DVD and VHS last year, while generating $9.4 billion in domestic box office revenue. In addition to theatrical releases, many highly popular previously broadcast television series are now available in DVD format, frequently accompanied by major advertising campaigns. Popular cable network shows are also available on DVD.
The growth in sales of DVD-formatted programming has been facilitated by gains in the sale of DVD hardware. U.S. consumers purchased 37 million DVD players in 2004, an eight percent increase over the previous year. During the first half of 2005, nearly 14 million DVD players

were sold to consumers, more than a six percent increase over the same period last year. Household penetration is expected to reach 80 percent by year-end 2005, with over 45 percent of DVD owners having more than one player. When accounting for computers with DVD-ROM drives and DVD-enabled video game consoles, an estimated 79 million households currently have the capability to play DVD, approaching three-fourths of all U.S. TV households.
With regard to DVD software, on-line provider Netflix recently teamed with retail giant, Wal-Mart, to offer their customers access to more than 40,000 titles of video programming. Overall, consumers spent $15.5 billion in 2004 on DVD sales, an increase of 33 percent over 2003, while revenues from DVD rentals increased 26 percent over 2003, as consumers spent more than $5.7 billion.

III. TELEPHONE COMPANY ENTRY INTO VIDEO

Now that DBS has transformed the video marketplace so that virtually all television households have choice, it is easy to forget that only a decade ago, it was the large local telephone companies that were promising to provide a competitive alternative to cable - just as cable operators were promising to provide a competitive alternative to the telephone companies. Congress took these promises seriously. The Telecommunications Act of 1996, by removing barriers to the telephone companies' entry into cable and cable's entry into the provision of local exchange service, was intended to promote the convergence of voice, video, and data services in a competitive marketplace.
The cable industry took its promise seriously, too. Over the last decade, cable operators have invested $100 billion to upgrade their facilities. In addition to providing a wealth of new video programming alternatives - including digital tiers, video-on-demand, and high definition television - cable now offers robust high-speed Internet service and telephone service. Meanwhile, during most of that period, the telephone companies' promises to enter the video marketplace went unfulfilled.
Now, however, the telephone companies are reviving their plans to provide multichannel video programming services. Telephone companies are not only touting their proposed video offerings but are actively deploying facilities and beginning to make video service available. For example, SBC is spending $4 billion over the next three years to install fiber optic cable to serve up to 18 million homes and plans to deliver television services using Internet protocol (IP) technology. Verizon is spending $6 billion over five years to lay fiber direct to the home to reach up to 16 million households in its service areas.
Although there is already vigorous competition in the video marketplace, the prospect of a major new competitor with the resources of the Bell Operating Companies should be beneficial to consumers - as long as competition is governed by marketplace forces and is not artificially skewed by rules and regulations that unfairly give some competitors an unfair advantage over others. (As noted above, these "new entrants" have annual revenues of $150 billion - about three times those of "incumbent" cable operators.) The marketplace will impel competitors - old and new - to innovate in the development of new services and in the packaging and pricing of their offerings to maximize value to consumers.

IV. LIKE SERVICES SHOULD BE TREATED ALIKE

To the extent that telephone companies intend to offer many of the broadcast signals and cable program networks currently available to cable subscribers, there is a comprehensive federal

regulatory framework already in place - Title VI of the Communications Act - to govern their video activities. Some telephone companies argue, however, that they should not be subject to the same regulatory framework as other cable operators. They maintain that compliance with the obligations and requirements of Title VI would impede their ability to compete as quickly as possible in the video marketplace.

It is not unreasonable to consider, from time to time, whether existing regulations and requirements continue to serve important governmental purposes - for all competitors subject to those regulations. For example, economic regulations (such as rate regulation) that are imposed on entities presumed to have market power may serve no purpose if that market power has been eroded by marketplace competition. Other regulations may have nothing to do with market power and may, in the case of Title VI, represent a consensus of policymakers regarding the social obligations that should apply to all providers of video programming because of the unique role and importance of television in our society. In those cases, it is reasonable to reconsider whether the social obligations continue to make sense and whether the particular requirements and obligations are necessary, in a competitive environment, to ensure that such obligations are met.

If those obligations and responsibilities do continue to make sense, they should be shared by all competing providers of like services. If not, then there is no basis for imposing them on any of the competitors. To arbitrarily subject some competitors to obligations and burdens not imposed on others would only serve to distort the competitive marketplace.

Congress included in Title VI a self-correcting mechanism that removes the burdens of economic regulation from cable operators that face "effective competition." Rate regulation, uniform pricing, "buy-through" restrictions and other provisions in Section 623 of the Act do not apply to new entrants, including telephone companies, because those competitors face "effective competition" from the existing cable operators as soon as they enter the marketplace.

In addition, Congress amended Title VI in 1992 to bar exclusive cable franchises and to prohibit franchising authorities from unreasonably refusing to grant additional competitive franchises. A telephone company or other potential new entrant whose application for such a franchise has been denied for reasons that it believes to be unreasonable may appeal such a denial in federal or state court.

Therefore, the requirement that telephone companies obtain a franchise is not a barrier to competitive entry. If telephone companies were simply to agree to the same franchise obligations as existing cable operators, a franchising authority would be hard pressed not to grant a franchise expeditiously. What the telephone companies urge, however, is that they not be subject to the same social obligations and responsibilities as competing cable operators.

In particular, telephone companies object to being required, like other cable operators, to offer service throughout a community. Section 621 of the Communications Act directs franchising authorities to "assure that access to cable service is not denied to any group of potential residential cable subscribers because of the income of the residents of the local area in which such group resides." In addition to this restriction on economic "redlining," most franchising authorities require cable operators to build out their facilities to serve all but the most sparsely populated areas of their communities.

Section 621 requires franchising authorities to allow franchise applicants "a reasonable period of time to become capable of providing cable service to all households in the franchise area" - but this is not sufficient for the telephone companies. They claim that build-out and anti-redlining obligations are unwarranted barriers to entry that will keep them from offering their competitive

services.
It is clearly not the just the costs of construction that the telephone companies are worried about - although some areas may, in fact, be more costly to serve than others. What they have also recognized is that some areas of the community are likely to generate substantially more revenue than others, wholly apart from the costs of serving them. Thus, as SBC, for example, has explicitly told prospective investors, their objective is to serve only the "high value" areas of the community without offering service to the "low value" areas.
If the telephone companies were allowed to serve only the most lucrative areas of communities that cable operators were required to serve in their entirety, competition would not be enhanced but would suffer. Consumers in the areas that the telephone companies chose not to serve would pay the highest price for such disparate regulatory treatment. Appendix B by Michael G. Baumann of Economists Incorporated explains why this would be the case.
The effect of a mandatory build-out requirement is generally to make service available to areas that would not otherwise be served - otherwise, there would be no need for the rule. To recoup and subsidize the costs of deploying facilities and serving these areas - the areas that SBC would call "low value areas" - cable operators are likely to rely on revenues from areas that cost less to serve and/or where customers purchase more options (the "high value areas"):
With cable systems, it is often the case that there are differences in the costs of serving different geographic areas. While programming costs per subscriber do not vary by area, the per-subscriber cost of maintaining the physical plant may be higher in some areas. In addition, due to variations in household income and demand, certain geographic areas may generate larger revenues per subscriber as a result of the programming and other services purchased. The revenues from subscribers in these high value areas may be of critical importance to the cable operator in covering the costs of upgrading and expanding the entire cable system. In effect, the revenue from these areas cross-subsidizes the cost of upgrading other areas.

Cross-subsidization cannot be sustained if a significant competitor is allowed to construct facilities and provide service only in the areas where costs are lowest and/or expected revenues are highest. As Baumann points out, proponents of allowing such cream-skimming by telephone companies envision a result in which "all consumers are better off because the incumbent's price is lower everywhere and some consumers have the added choice of subscribing to the entrant's service." But this is not a viable outcome.
Since the telephone company will, as the result of cream skimming, have lower per-subscriber costs and higher per-subscriber revenues than the competing cable operator, it will be able to charge less than that operator - and this will likely force him to lower his price in the area served by the telephone provider. However, the operator cannot simply lower prices across the board, making everybody better off:
Without the ability to finance the cross-subsidies needed to support the low value areas, the incumbent's situation has to change. The actual outcome will depend on the degree to which the incumbent's ability to subsidize the low value area is reduced and what, if any, regulatory relief is provided. While one cannot predict with certainty what will happen given the variation in conditions across franchises, some groups of consumers, particularly those in the low value areas, will likely be harmed in the long run.

Facing effective competition from DBS providers and telephone companies, cable operators will no longer be subject to uniform pricing constraints. One alternative might simply be to raise

prices in the higher-cost areas that the telephone companies choose not to enter. But this may not be a viable alternative. Operators may not be able to raise prices in those areas without losing more revenue than they gain - either because of competition from DBS or because customers are simply unwilling or unable to pay such higher prices for any multichannel subscription service. In that case, as Baumann explains, allowing a significant new entrant to cream skim the "high value" areas of a community may threaten the quality - or the continued existence - of cable service in the "low value" areas that the new entrant chooses to ignore. It may even unfairly threaten the competitive viability of the cable operator throughout the community:

The incumbent may be able to maintain, but not upgrade, the current level of service in the low value area. Alternatively, the incumbent may not be able to continue to serve all of the low value areas. Finally, the incumbent may be at such a disadvantage relative to the entrant that it will eventually exit the entire franchise area.

In these circumstances, exempting new entrants from the build-out and anti-redlining obligations imposed on existing operators would actually pose a greater threat to fair marketplace competition than imposing such obligations - especially in a video marketplace in which consumers are already enjoying the benefits of vigorous competition among cable operators and two strong DBS services. Moreover, it would directly undermine President Bush's policy goal of promoting ubiquitous competitive broadband availability throughout the nation, including areas that might otherwise be underserved by 2007. As Baumann points out,

[i]f identical regulations are applied to both the incumbent and the entrant, whether both firms survive or only one firm survives, and which one, is left to the competitive forces of the marketplace. Admittedly, the competition in the marketplace is subject to the constraint of universal service, but in the end all potential customers will have the ability to get cable service. Alternatively, if constraints apply only to the incumbent, then which firm or firms survive is not a function solely of the competitive marketplace, but is influenced by the asymmetric enforcement of governmental regulations. And, in the end, it is possible that many fewer customers will get cable service.

Mr. Chairman, one can construct an intellectually coherent argument that a desire for something akin to universal service requires a build-out requirement that is applied to all providers. One can also construct an intellectually coherent argument that universal service is no longer a social goal that trumps the free market, and therefore no build-out requirements should apply to any providers. But the one policy proposal that is illogical and counterproductive is to pretend a build-out requirement is an important goal, but then place that burden on one provider and free another to cherry pick customers: neither universal service nor free market competition is achieved in such a case.

V. CONCLUSION

As Congress takes up possible amendments to the Telecommunications Act of 1996, we urge you to treat like services alike, preferably in a deregulatory environment. We will do the rest to raise private risk capital, invest in new technology, offer better customer service, create innovative programming, compete with other multichannel video providers, and serve the needs of consumers by providing the best choices available in the market for video, voice, and data services.