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Federal Communications Commission (F.C.C.)

Eighth Annual Report

IN THE MATTER OF ANNUAL ASSESSMENT OF THE STATUS OF COMPETITION IN THE MARKET FOR THE DELIVERY OF VIDEO PROGRAMMING

CS Docket No. 01-129

FCC 01-389
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By the Commission: Commissioner Martin issuing a statement.

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IV. COMPETITIVE RESPONSES

196. In this section, we describe a number of cases where the incumbent cable operator faces competition from a new entrant. We report information gathered through comments filed in this proceeding, petitions filled with the Commission for a determination of effective competition, trade press reports, articles, and other publicly available sources.

197. Between July 2000 and June 2001, the Bureau granted 16 petitions for effective competition, representing 240 communities, based on competitive entry from LECs or their affiliates, DBS, and municipal operators. These communities represent approximately two percent of all cable subscribers. The differences between competition and general market responses based on technological advances, improved marketing, and new service opportunities are not always easy to distinguish. However, in communities where head-to-head competition is present, the incumbent cable operator has generally responded to competitive entry in a variety of ways, such as by lowering prices, providing additional channels at the same monthly rate, improving customer service, adding new services, or by challenging the legality of the entrant's activities.

198. For example, in Boston, Massachusetts, in response to RCN's entry, the incumbent cable operator in Boston, Cablevision of Boston ("Cablevision"), "moderated" its regional rate increase in the Boston area and agreed to improve its commitment to public and educational channels. [FN617] RCN, a wholly owned subsidiary of RCN Telecom Services Inc., initially entered the Boston area market in 1996 as an OVS operator. [FN618] It was granted a 15-year cable franchise by the City of Boston on July 27, 1999. By September 1999, RCN served a total of 11,000 subscribers in the Boston metropolitan area, including 5,000 subscribers in the City of Boston. [FN619] By comparison Cablevision serves about 140,000 subscribers in Boston. [FN620]

199. RCN contends that, because of its entry to the Boston area, the City of Boston was able to negotiate a franchise renewal with Cablevision that imposed obligations on the incumbent more favorable to the public than would otherwise have been possible. [FN621] The franchise agreement requires Cablevision to upgrade its system capacity within three years to offer more channels, as well as local telephone and high-speed Internet access. [FN622] Initially Cablevision took steps to prevent RCN from going forward by filing a lawsuit against RCN and the city. [FN623] Furthermore, RCN contends that Cablevision created a barrier to entry by refusing RCN access to inside wiring in MDUs in the Boston area. [FN624]

200. Lower monthly rates and added or improved services were also found in a number of other communities where the incumbent cable operator faced new entrants. For example, in Duluth, Georgia, the incumbent Rifkin & Associates, Inc./Cable Equities of Colorado, Ltd. ("Rifkin") faced aggressive advertising aimed at its subscribers, accompanied by extensive press coverage in the local media, from new entrant BellSouth Interactive Media Services, Inc. ("BIMS"). [FN625] In response to aggressive competition from BIMS, Rifkin upgraded its system and added 19 new channels -- nine new expanded basic channels, a low priced, three-channel new product tier, and seven PPV channels. [FN626]

201. Similarly, RCN contends that in Somerville, Massachusetts, upon its entry, Time Warner, the incumbent, announced a rate freeze for only that area where it faced competition. [FN627] In suburban Philadelphia, as a result of RCN's entry, Comcast, the incumbent, began to offer "rate locks" and service improvements in the towns where it faced competition. [FN628] In the Washington, D.C., area, as a result of entry by Starpower, an RCN affiliate, Comcast, the incumbent cable operator, reduced a previously proposed rate increase. RCN also contends that in anticipation of its entry in Fairfax County, a suburb of Washington, D.C., the incumbent Cox announced an upgrade of its plant. [FN629]

202. In some situations questions have been raised regarding the techniques used by incumbent service providers to forestall competition. In Scottsboro, Alabama, the Scottsboro Electric Power Board ("Scottsboro") began construction of a new, municipally owned cable television system in Scottsboro because of widespread dissatisfaction with Falcon Cablevision ("Falcon"), the incumbent cable operator. [FN630] In late 1999, Charter Communications ("Charter") acquired Falcon's operation in Scottsboro. After acquiring the system, Charter began to engage in a course of conduct that, according to Scottsboro, is designed to terminate Scottsboro's efforts to compete in the market and, moreover, to signal other would-be competitors that attempts to enter other Charter markets would lead to similar predatory practices. [FN631]

203. Since beginning in April 2000, Charter offered a special rate of $19.95 per month for one year. It then allowed some customers to continue subscribing at that rate for a second year. In May 2000, Charter added one month of free service to the $19.95 rate. [FN632] Scottsboro contends that Charter's special rates are available only to Scottsboro's customers and are not available to all potential subscribers in Scottsboro. [FN633]

204. According to Scottsboro, Charter normally charges $24.95 per month for its expanded basic service, which includes 200 channels comprised of 16 premium movie channels, 45 digital music channels, 16 educational channels, and 14 PPV channels. A digital receiver with remote and Charter's on-screen guide are also included. Furthermore, Charter offers a $200 "bounty" to switch from Scottsboro to Charter, and an additional $200 if subscribers take its Internet service. In addition, Charter

established a system under which it retired subscribers' old debts. Scottsboro states that Charter's special offerings have induced about 36 percent of Scottsboro's customers to switch to Charter.

205. Charter counters that Scottsboro has easy access to every citizen because of its advantageous position as a municipally owned-cable system; it also has wide public support, low capital costs, and the incumbent system against which it formerly competed was in dire need of an upgrade. According to Charter, it upgraded the system after purchasing it from Falcon, and the system is now able to provide cable modem service and digital programming at competitive rates. [FN634] Charter admits that it has conducted "win back" campaigns, but claims that such campaigns are widespread among cable television operators. It also denies that it has set its prices at predatory rates and maintains that its actions and pricing policies have benefited subscribers in the community because they now enjoy lower monthly charges for improved services. [FN635]

206. Knology submits that Charter has engaged in similar behavior against its systems in West Point, Georgia, and Montgomery, Alabama. [FN636] Knology has provided cable service in West Point since 1998. [FN637] In 1999, Charter purchased the incumbent cable system from Marcus Cable. After Knology entered the market, several rounds of lowering prices occurred until both providers were charging about $20 for expanded basic service. Knology contends that Charter did not offer the same discounted rates in nearby communities. According to Knology, in nearby communities, Charter's prices ranged to more than $35 per month for expanded basic, more than the national average of $32.25. [FN638] In addition, earlier this year, Charter began offering a "bounty" of $200 and free installation to any consumers that switched from Knology to Charter. Knology states that, for customers taking advantage of this offer, the effective cost of cable service was reduced to less than $4 per month. [FN639] In Montgomery, Knology purchased an existing competitive system in 1997. [FN640] When Charter acquired the incumbent cable system in 2001 from AT&T Broadband, it immediately lowered the price of its digital tier and offered consumers $300 to switch from Knology to Charter. According to Knology, Charter recently began to offer a "digital complete basic" service for less than $23 per month, which includes all analog expanded basic services, 50 channels available only on the digital tier, and 50 channels of digital music. In addition, Charter will forgive old debts to Charter or the system's previous owner. Knology alleges that Charter's discounts and giveaways have reduced its prices below costs, even if only programming costs are considered. Knology contends that Charter is taking a significant loss on each new customer it takes from its competitors, but it will be able to recoup its losses once it has driven its competitors out of the market. [FN641]

207. In previous Reports, we have examined responses to head-to-head competition. In communities where cable operators have faced competition for a substantial period of time, the initial competitive response generally gives way to a more mature form of competition that benefits both subscribers and operators. In Omaha, Nebraska, where Cox and Qwest have been competing for the past six years, both offer a bundle of video, telephony, and high-speed Internet access services to entice new customers and retain old ones. [FN642] For example, Qwest's phone customers pay $28.95 per month for 59 channels of basic cable service and $39.95 per month for cable modem service. For its part, Cox charges $33.95 per month for its 70 channel basic cable service and its cable modem service is $5.00 lower than Qwest's charge for cable modem service. As result of this competition, cable penetration in the area has increased and "churn" has stabilized. [FN643]

208. As the cases presented above suggest, subscribers usually benefit from "head-to-head"

competition. In communities where "head-to-head" competition has been sustained for a long period of time, customers generally receive lower monthly rates and better service, while operators generally enjoy higher penetration rates and lower churn rates. Commenters report that, however, in some cases, particularly where a new entrant may appear vulnerable for financial or other reasons, the initial response of a large incumbent MSO to competition may be motivated by anticompetitive animus rather than legitimate business concerns. [FN644] Further, commenters informed us that, because of the difficulty and cost of pursuing antitrust remedies, it may be that the target of anticompetitive conduct is without practical remedy. [FN645]

209. The allegations made in the comments of Scottsboro and Knology highlight the difficulties of new entrants that, for whatever reason, are capable of competing only within a confined geographic region. The vast resources of a large MSO may simply prove too much if brought to bear in a targeted fashion against a single system entrant. Moreover, we are concerned about the signal such targeting may send to others who would compete in the MVPD market, and particularly to the financial markets to which a new entrant may well be dependent for resources. However, it is not clear that we have specific statutory authority to address these kinds of problems directly. There has been some suggestion that our authority to prohibit anticompetitive acts or unfair practices under section 628 of the Act would reach targeted and predatory competitive responses. [FN646] Alternatively, it may be that we would have to seek additional authority from Congress in order to combat such practices, which tend to limit competition and discourage new entry.

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