

DEPARTMENT OF JUSTICE
Antitrust Division

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October 17, 2003

Robert E. Marsh, Esq.
Corporate Counsel Group, LLP
4144 Pennsylvania Ave.
Kansas City, MO 64111

Re: Business Review Letter Request by The National Cable Television
Cooperative, Inc.

Dear Mr. Marsh:

This letter is written in response to your request on behalf of The National Cable Television Cooperative, Inc. ("NCTC") for the issuance of a business review letter pursuant to the Department of Justice's business review procedure, 28 C.F.R. § 50.6. You have requested a statement of the Department's current antitrust enforcement intention with respect to a proposed new procedure to be used by NCTC when it negotiates on behalf of its members for their purchases of cable television programming offered by national networks.

NCTC's members are cable television systems, which deliver multiple channels of video programming to consumers through wired connections. Cable systems generally are franchised to serve discrete geographic areas. In most such areas, there is only one cable television system, but competition from overlapping systems does occur in some places. Most cable systems are owned by large multiple systems operators ("MSOs"). Some systems remain independent, however, or are owned by relatively small group owners. Most of the video programming distributed by cable television systems is provided to the systems by national programming networks.

According to the information you have provided, NCTC's membership is composed primarily of independent cable systems and smaller MSOs. NCTC has approximately 1000 cable system owners, who in turn own or operate cable systems serving approximately 6500 communities. NCTC's members altogether serve about 14.4 million subscriber households, approximately 15.8% of all households in the United States that subscribe to multichannel video

programming distribution (“MVPD”) services. NCTC’s members who actively participate in its existing joint purchasing program serve about 9.3 million subscriber households, approximately 10.2% of all U.S. MVPD subscriber households.¹ NCTC member systems range in size from fewer than 100 subscribers to almost 190,000. The average size of the members’ systems is approximately 2,000 subscribers, and the median is 350.

The great majority of the cable systems owned or operated by NCTC’s members serve geographically distinct areas, and thus do not compete with the systems of other NCTC members. NCTC reports that only 55 communities, or fewer than one percent of the communities served by NCTC’s active members, are served by more than one active NCTC member. NCTC also provides the results of a survey of the 149 member cable systems who serve the 55 communities. The returned survey forms show that at least 114,000 subscribers are located in areas served by more than one active NCTC member cable system. Extrapolating from these results based upon the response rate, NCTC concludes that about 316,000 subscribers are in these overlap areas. That number in turn represents only about 3.4 percent of the total number of subscribers--9.3 million--served by NCTC’s active member cable systems.

NCTC was formed in 1985 as the Mid-America National Cable Television Cooperative, Inc. Then, as now, the cooperative’s principal purpose was to gain efficiencies for its members by the joint purchasing of cable network programming. The cooperative proposed to negotiate master contracts with programmers, to which the cooperative’s individual members could then subscribe. In response to a request by the Mid-America National Cable Television Cooperative, the Department issued a favorable business review letter for the cooperative as it was then envisioned. U.S. Dep’t of Justice Business Review Letter to Mid-America National Cable Television Cooperative, Inc., 1985 WL 71884, (Aug. 30, 1985). The Department concluded that the arrangement was unlikely to create competitive concerns, in part because members of the cooperative were individually free to participate or not participate in any master purchase contract.

NCTC now believes that it can gain greater efficiencies for its members by adopting procedures somewhat different from those envisioned at the time of the Department’s 1985 letter. NCTC states that the current procedures hinder NCTC’s ability to negotiate volume discounts because NCTC, unlike a large MSO, cannot guarantee any volume of participation in a master contract, as the members decide whether to participate only after the contract has been

¹ To calculate these percentages we approximate the number of United States MVPD subscriber households by adding together the number of cable television subscriber households as of May 2003, i.e. 71,897,250, and the number of direct broadcast satellite subscriber households as of December 2002, i.e. 19,401,000. NCTA Industry Overview, Industry Statistics, at <ncta.com/industry_overview/indStats.cfm>. SBCA Media Center Facts & Figures, at <sbca.com/mediaguide/factsfigures.htm>. The resulting number is not a precise accounting, but is close enough to estimate the relative size of NCTC members’ subscriber base compared to all MVPD subscribers.

negotiated. NCTC contends that because members cannot obtain discounts as significant as direct broadcast satellite ("DBS") firms or large MSOs, they are at a competitive disadvantage in competing against these providers.

NCTC now proposes to adopt a new set of procedures. Members who wish to participate in a new master contract with a program supplier may state their reserve prices before negotiations are undertaken. If the contract price that is then negotiated equals or falls below an individual member's stated reserve price, that member must participate in the contract. If the member's reserve price is not met, the member will be free to try to negotiate its own contract with the program supplier at a price equal to or below that set by the master contract. That member may also still choose to participate in the master contract. If NCTC is not successful in negotiating a master contract with the program supplier, each member may try to negotiate its own contract with the program supplier at a price equal to or below its own specified reserve price. If the member is not successful in doing so, it must refrain from carrying the relevant programming network for some period of time. NCTC will determine how long this time will be, but does not intend the period to last longer than two years.

Members who elect not to participate in these new procedures remain free to negotiate their own individual contracts with the relevant program supplier. They may also choose to participate in the master contract that is ultimately negotiated. An employee of NCTC who is not affiliated with any of its members will manage negotiation of the master contracts and the members' commitment agreements. Communications between NCTC and its individual members regarding negotiations for specific master contracts and the preceding commitment agreements will be kept confidential, and not made available to other members. NCTC will not reveal to any of its members the identities of any member who participates or proposes to participate in any specific master contract. Members will not be allowed to condition their commitment agreements upon another member's commitment agreement or participation in the master contract.

Based on the representations made in your submissions, the information submitted in support of NCTC's request and the information obtained during our review, the Department does not believe that NCTC's proposed joint purchasing procedures will have anticompetitive effects. All NCTC's members together serve only about 15.8% of the nation's MVPD subscribers. Even if all NCTC's members participated in master contracts for all national cable programming, the members' purchases of that programming almost certainly would not constitute such a significant percentage of all purchases in the relevant market that concerns would be raised about monopsony power. U.S. DEP'T OF JUSTICE & FEDERAL TRADE COMM'N, STATEMENTS OF ANTITRUST ENFORCEMENT POLICY IN HEALTH CARE (1996), Statement 7. Available at <http://www.usdoj.gov/atr/public/guidelines/1791.htm> (One condition for an antitrust safety zone for joint purchasing arrangements among health care providers is that purchases account for less than 35 percent of the total sales of the purchased product in the relevant market.)

We also believe that NCTC's proposed procedures will not appreciably facilitate price

collusion among NCTC's members in the sale of multichannel video programming distribution services. With respect to the overwhelming majority of NCTC member cable systems, there is no danger that NCTC's procedures will facilitate retail price collusion because those cable systems do not compete with each other in the sale of MVPD services to consumers. NCTC estimates that almost 97% of its active members' subscribers reside in areas served by only one active NCTC member cable system.

Several factors in the NCTC proposal mitigate any competitive concerns with respect to collusion in overlap areas served by the remaining NCTC members. First, although two competing cable systems may both participate in NCTC, neither system will know which programming the other is buying through NCTC. The safeguards that NCTC has outlined preclude competitively sensitive information about who participates in contracts from being disseminated to other members. NCTC has also adopted safeguards to prevent members from using the activities of the cooperative to share their reserve prices or from conditioning their participation in a contract on whether another member agrees to the contract. In addition to programming costs, cable systems' cost structure can vary significantly due to the size and technical characteristics of the systems. Second, those members who compete for a group of customers with another member generally face competition from other MVPD providers who can serve the same customers, such as DBS providers. The two major DBS providers are not members of NCTC. The likelihood that collusion will occur, therefore, is reduced by the presence of other significant competitors who are not part of the joint purchasing arrangement. Finally, any attempt by NCTC members who compete with each other to use the NCTC process to negotiate contract terms that facilitate collusion, by for example standardizing terms, is unlikely to be successful. Contracts are negotiated by persons who are not associated with any member, and in addition, NCTC will attempt to enter contracts that serve the interests of all its members, the vast majority of whom face no competition from other members.

NCTC's proposed new procedures, we believe, do not substantially change the voluntary character of participation in the purchasing program. NCTC members remain free to decline to participate in any master contract for a particular program network, albeit they effectively now may be required to decline before any new negotiation is undertaken. Even in a voluntary arrangement, the Department has previously recognized, members of a joint purchasing cooperative may be asked to commit to purchase voluntarily specified volumes of an input at specified prices. *See* U.S. Dep't of Justice, Business Review Letter to Containers America LLC (Mar. 8, 2000) *available at* <http://www.usdoj.gov/atr/public/busreview/4287.htm>.

Finally, we note that to the extent the contemplated changes to the joint purchasing procedures result in lower programming costs to members that are passed along to consumers, the proposed conduct could have procompetitive effects.

For these reasons, the Department has no current intention to challenge the NCTC's proposed procedures for jointly negotiating national cable programming contracts for its active members. This letter expresses the Department's current enforcement intentions, and is predicated on the accuracy of the information and assertions that you have presented to us. If the

conditions you have presented are substantially changed—if, for example, a major MSO or a DBS provider were to join NCTC or there were other significant changes to NCTC's active membership—the conclusions we have drawn would no longer necessarily apply. In accordance with its normal practice, the Department reserves the right to bring an enforcement action in the future if the actual activities of NCTC or its members prove to be anticompetitive in any purpose or effect in any market.

This statement is made in accordance with the Department's business review procedure, 28 C.F.R. § 50.6. Pursuant to its terms, your business review request and this letter will be made publicly available immediately, and any supporting data will be made publicly available within thirty days of the date of this letter, unless you request that any part of the material be withheld in accordance with Paragraph 10(c) of the business review procedure.

Sincerely,

R. Hewitt Pate
Assistant Attorney General