TV Smackdown!

Cable vs. Broadcast

by Thomas W. Hazlett

MAY 5, 2000 - Unlike the performers of the World Wrestling Federation, the overweight guys running Time Warner and Disney really are trying to hurt one another. And after Time Warner yanked ABC stations from its cable systems earlier this week, it wasn't just executives calling for blood. Some 3.5 million hysterical subscribers cried foul; regulators declared the cable system in violation of federal law; and investors sent shares in both companies tumbling. Even as a temporary truce was called, inquiring minds want to know just how we ended up with such a showdown.

The broadcaster-cable death match goes back decades, fueled by regulations that have alternately given one industry an advantage over the other. Television broadcasters initially had the edge, after a 1952 Federal Communication Commission decision bestowed them with a rich triopoly. Competitors just couldn't obtain the airwaves necessary to compete with the Big Three networks. When cable began filling the channel void, it was suppressed by an FCC that wanted to protect the companies it regulated.

When cable finally broke loose of FCC shackles in the late 1970s, it looked as though it would infuse broadcasting with a good measure of competition. But along the way, cable discovered its own regulatory booby traps and used them to create local monopolies. The 1984 Cable Act, written largely by the National Cable TV Association, mandated that cable systems have municipal franchises (typically one per town) and blocked telephone companies from competing in video.

The outcome set the stage for today's controversy. A handful of local TV stations ended up in direct competition with a local monopoly cable system. A wrestling match ensued over how to divvy the spoils when the local cable station retransmitted broadcast signals.

Historically, cable systems simply grabbed local TV signals and rebroadcast them on basic cable, paying only a nominal royalty. TV broadcasters fumed over the cable industry's legal right to "steal" broadcast programs and turn around to sell them for a monthly fee.

The 1992 Cable Act, the result of a successful lobbying campaign by broadcasters, reversed this state of affairs. Each TV station had two options. One choice was to claim "must carry" status, forcing local cable to carry its signal for free. The second option was to negotiate with cable systems for retransmission, selling the signal for whatever the market would bear. Going the latter route meant giving up must-carry rights.

Broadcasters thought they'd get a bundle from cable operators. Instead, when the policy went into effect in 1993, cable systems refused to cough up anything close to the $1 or $2 a month per subscriber that broadcasters had estimated their signals (based on viewing audiences) were worth. Cable operators understood that while local TV signals were valuable to cable systems, cable system carriage also was valuable to broadcasters. Hard-nosed bargaining ensued.

When the dust settled, some interesting deals were struck, and TV stations did go on cable. Fox, for instance, gave its broadcast stations to cable systems that also agreed to carry its start-up cable network, F/X. But very little cash actually flowed from cable operators to broadcasters -- pennies on the dollars the broadcasters had anticipated.

The current tug-of-war finds Disney demanding that Time Warner place the Disney Channel (currently a premium service) and its two new channels, Toon Disney and the Soap Opera Channel, on basic cable. Otherwise, says Disney, no "Monday Night Football," no "Who Wants to Be a Millionaire?" and no "Nightline." Disney may feel emboldened by Time Warner's political vulnerability: America Online has offered a huge premium for Time Warner's stock, but the merger must be approved by the Justice Department and the FCC. Facing millions of irate, Regis Philbin-deprived cable subscribers, Time Warner looks less a sympathetic takeover target than a rapacious monopolist.

Which brings up the competition question. Had the cable market not grown up surrounded by local monopoly licenses, paltry spectrum allocations from the FCC, and federal bans on cable and telecommunications cross-ownership, then customers -- and TV programmers -- would have an easier time avoiding Time Warner's roadblocks. There isn't much that is "natural" about cable's monopoly, as an entirely new group of competitors are finally free to demonstrate.

Direct broadcast satellite, now provided by DirectTV and EchoStar, has attracted an astounding 12 million subscribers in five years. While cable still has 65 million subscribers, DBS is growing at 40% a year. It will grow faster if broadcasters and cable operators engage in scorched-earth bargaining, snatching away popular programs.

Lawmakers, who in November 1999 boosted DBS competition to cable by (finally) allowing dish owners to receive local signals, attached a poison pill to the measure. The must-carry policy was waived for DBS, but only until 2002. Then it kicks in again, destroying DBS's ability to provide lucrative local programming.

Under the current waiver EchoStar (with 500 channels of capacity) and DirectTV (with 320 channels) are free to offer subscribers the most popular local channels and forget low-rated ones. This allows each system to provide packages of four local channels (affiliates of ABC, NBC, CBS and Fox), plus one national PBS feed, across the country. With just 81 channel slots, for instance, DBS can offer local stations in the top 20 markets, creating robust competition to cable in most households. Yet with the must-carry rule, DBS systems would be forced to carry all local signals if they carry any. With nearly 1,600 TV stations, DBS channels would be swamped.

These days, cable systems that unsuccessfully challenged must-carry rules all the way to the Supreme Court in 1997 are coyly embracing them. Stephen Keating's recent book, "Cutthroat: High Stakes and Killer Moves on the Electronic Frontier," reports that cable operators "immediately recast the ruling as reason to deliver all 1,600 broadcast stations by satellite into the respective local markets."

Today that dish offers customers the easiest exit from cable's monopoly power. Must-carry rules for DBS will soon block that escape. Broadcasters, also fearing DBS competition and eager to force free carriage, are ironically allied with their old cable foes in promoting DBS must-carry. Strange bedfellows caught in an ugly embrace? I'll bet you won't see that "Movie of the Week" on either Disney 's ABC or Time Warner's TNT.

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