ITIF | INFORMATION TECHNOLOGY & INNOVATION FOUNDATION

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of

Application of Charter Communications, Inc., Time Warner Cable Inc., and Advance/Newhouse Partnership for Consent to the Transfer of Control of Licenses and Authorizations	)))))))	MB Docket No. 15-149

Comments of ITIF

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Information Technology and Innovation Foundation
1101 K Street NW, Suite 610
Washington, DC 20005

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INTRODUCTION AND SUMMARY

The Information Technology and Innovation Foundation ("ITIF")[1] appreciates this opportunity to comment on the proposed acquisition of Time Warner Cable and Bright House Networks by Charter Communications. ITIF supports this transaction with the belief that the deal presents few competitive concerns while offering significant public interest benefits. The increased scale of the combined company will not only allow Charter to gain efficiencies to reduce costs, but to also better able to deploy new technologies to a broader customer base and allow a larger platform for actors throughout the supply chain to offer new products and services. Considering the pace of innovation and change in this sector, regulators should be cautious of focusing principally on narrow purported benefits of increased competition over allowing a dynamic market to innovate and invest at an appropriate scale.

This acquisition poses few competition concerns. There is virtually zero reduction in horizontal competition as these companies do not compete in any single market. A combination also does not present significant vertical issues. With only 17 percent of the video market, a combined company presents no fear of monopsony power, and, furthermore, stronger negotiating power in purchasing content should not be feared, as customers will ultimately benefit. Vertical competition issues in the broadband space are also not cause for alarm. Charter has demonstrated a willingness to go above-

[1] Founded in 2006, ITIF is a 501(c)(3) nonprofit, nonpartisan research and educational institute—a think tank—focusing on a host of critical issues at the intersection of technological innovation and public policy. Its mission is to formulate and promote policy solutions that accelerate innovation and boost productivity to spur growth, opportunity, and progress.

and-beyond to accommodate online video distributors (OVDs), and, furthermore, there are dozens of various ways to get traffic into an access network like Charter's, alleviating any real concerns about vertical competition in broadband.

The Commission should not overlook the significant technological and economic benefits that would come from a combined, larger company. The improved ability to quickly scale new innovations throughout the country as well as the ability to better recoup the large capital investment needed to innovate, improve, and maintain a large cable plant mean that this transaction is likely in the public interest.

THE PROPOSED TRANSACTION PRESENTS FEW COMPETITIVE CONCERNS

The proposed transaction between Charter, Time Warner Cable, and Bright House Networks does not present any concerns around competition, either horizontal or vertical. Rather, the transaction is likely to enhance competition, especially in enterprise services.

The proposed transaction does not reduce horizontal competition

Charter, Time Warner Cable, and Bright House Networks do not overlap in any geographic markets. Without any reduction in horizontal competition, this transaction becomes much simpler to analyze. There are obvious dynamic and productive efficiencies to be gained by a larger network. For example, it will be easier to recoup the large capital investments needed to maintain, operate, and upgrade a large access network. It will also be easier to support more research and development into better network operation and the development of new functionalities. A larger network will accrue other scale economies related to advertising, overall management, and network operations. Given that there is competition in the broadband markets, clearly at least some of these efficiencies will flow back to consumers in the form of lower prices or improved services.

This transaction will not reduce the number of options consumers have for either video programming or broadband access. The opportunity to gain significant efficiencies without any reduction in competition should be celebrated as a boon to the public interest. Rather than addressing these facts, the minimal opposition to this merger seen so far appears to come from groups who reflexively oppose any consolidation, even when clearly in the public interest, holding what can be charitably termed a “small is beautiful” ideology when it comes to communications networks and ISPs.

The effects on vertical competition will be minimal

Although the vertical effects of a potential transaction are less straightforward than the horizontal, the increased concentration from a combined company is unlikely to compromise upstream or downstream markets. Here the Commission should consider the effect of the acquisition on both the video content and broadband or interconnection markets.

Looking first at the traditional pay-television market, it is important to recognize how dynamic this market is. DBS providers, with nation-wide footprints, are strong competitors and maneuvering to supplement their already popular offerings with broadband. Likewise ILEC offerings like Verizon's FiOS and AT&T's U-verse provide substantial and growing competition in the video (as well as broadband) market. AT&T is investing aggressively in its U-verse offering, expanding its video footprint, and is seeing exceptional subscriber growth with its improved broadband speeds.[2] Furthermore, major wireless carriers are developing LTE broadcast technologies that will continue to improve the ability of wireless to compete in the video as well as broadband services.[3] And of course this market is in the midst of rapid change with the rise of online video distribution. This is a complex and dynamic market; regulators should move cautiously as it develops.

The combined company would only have about 17 percent of the pay TV market—far from a monopsony for video programming, and far below the FCC's historical 30 percent cap vacated in 2001 and 2009.[4] Recent negotiations have made it clear much of the power still lies on the content side. For example, analysts point to the 2013 CBS blackout on Time Warner Cable as a major factor in what was the steepest quarterly loss of subscribers in television history.[5] Distributors know that

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[2] AT&T has recorded several consecutive quarters of U-verse broadband net adds that were above 600,000 – in Q1 2014, for example, U-verse broadband net adds were 634,000. *See* AT&T Newsroom, 2014 Q1 Earnings, http://about.att.com/story/att_first_quarter_earnings_2014.html.

[3] *See, e.g.* Jeff Baumgartner, "Verizon CFO: LTE Multicast 'Pivotal' to Mobile Video," Multichannel News (Aug. 12, 2014) http://www.multichannel.com/news/technology/verizon-cfo-lte-multicast-pivotal-mobile-video/383137; for an introduction to the technology and its business case, *see* Qualcomm, "LTE Broadcast – A revenue enabler in the mobile media era" (Feb. 2013), https://www.qualcomm.com/media/documents/files/lte-broadcast-a-revenue-enabler-in-the-mobile-media-era.pdf.

[4] *See* FCC, "The Commission's Cable Horizontal and Vertical Ownership Limits," Fourth Report and Order and Further Notice of Proposed Rulemaking, 23 FCC Rcd 2134, 2143 (2008).

[5] *See, e.g.,* Brian Stelter, "Time Warner Left Bruised in Fee Battle with CBS," *New York Times* (Oct. 31, 2013) http://www.nytimes.com/2013/11/01/business/media/time-warner-reports-record-quarterly-loss-of-tv-subscribers.html?_r=0.

consumers demand a variety of content, and evidence strongly shows that denying it to them, for however long, is dangerous.

Moreover, any increased power of the combined ISP to negotiate lower content fees should ultimately benefit consumers. Content costs are a major factor in the increase in cable prices over the years; the pressures for consolidation in the cable industry are due in some part to rising programming costs. Here we are not so worried about small independent programs making onto the carrier (distributors have incentives for variety and increasingly content providers also have over-the-top options), but the appropriate pressure to control costs of large, popular shows and regional sports programming. Customers will benefit from a combined company's ability to negotiate lower programming fees.

Consumers are also increasingly turning to over-the-top services for video. Recent comments from both Department of Justice and FCC officials have made clear that concerns around the effect of cable consolidation on OVD development contributed to the abandonment of the proposed Comcast-Time Warner Cable transaction.[6] Thankfully, this proposed transaction raises few concerns about a combined company's ability or incentive to affect downstream broadband services and providers.

First of all, it is not clear why Charter would have any interest at all in harming OVDs. Such efforts would fly in the face of the virtuous cycle driving broadband investment. Charter has every interest to attract broadband subscribers—attempts to foreclose streaming video options would only harm its reputation and make its broadband product less attractive. It is also worth noting that Charter does not have any substantial interests in nationwide programming.

Even assuming, arguendo, that Charter wanted to restrict OVDs it is unclear how it could do so. The company would serve fewer than 30 percent of national high-speed broadband customers, as defined by the Commission for the purpose of section 706 jurisdiction (a speed far higher than required for streaming high-definition video). This relatively small size would fall short of that needed to foreclose OVDs, which enjoy access to global markets.

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[6] *See e.g.,* Bill Baer, "Video Competition: Opportunities and Challenges," Remarks as Prepared for the Duke Law Center for Innovation Policy Fall Conference on The Future of Video Competition and Regulation (Oct. 9, 2015) *available at* http://www.justice.gov/opa/file/782401/download.

These issues are played out most explicitly in interconnection agreements. While this area is complicated by the rightly confidential nature of interconnection agreements, and the Commission is right to seek confidential information related these agreements, ITIF is confident, given the economics of interconnection, that a combined company would not pose an anti-competitive threat to broadband services or other Internet providers.

First of all, Charter has gone above-and-beyond with its commitment to offer settlement-free peering through 2018.[7] Although this move has won accolades, most notably from groups opposed to past cable mergers, ITIF is skeptical that general policies of settlement-free peering offer sound economics to see continued growth and expansion of broadband facilities. It is good to see Charter is able to support this peering policy for now, as it speaks well to their plans for growth in network capacity, but it is unlikely that such a policy is economically sustainable long-term.

We urge the Commission to allow flexibility in the interconnection market and not seek to extend these types of commitments, and certainly should not seek to make settlement-free peering the expected norm. Terminating traffic on an access network is not without costs, and, like any normal bargaining process, parties should be left to discover the best way to efficiently allocate those costs. Where the flow of traffic is imbalanced, and costs of capacity are one-sided, a fee for interconnecting traffic has always been normal. Allowing healthy negotiation over allocation of costs, without tipping the scales, is the best way to see continued expansion in capacity throughout the network. Some dispute resolution process may be helpful when interconnection negotiations break down, as the public can be affected, but these circumstances are quite rare.

In fact, there is little concern that access networks will be able to leverage their last-mile status to extract anti-competitive rents from interconnection arrangements because of simply how many paths there are into the network. Access networks are already well interconnected with the rest of the Internet – these simply are not like the terminating monopolies of old where you had to get equipment into a central office in order to interconnect.

Persistent confusion stems from the comparison of modern IP networks to the arbitrage problem of "terminating access monopoly" created by telephone regulations of the un-modernized Title II. Here, OVDs have considerable market power and a great deal of cachet—users would be furious if

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[7] *See* Samuel L. Feder, Letter (July 15, 2015) http://apps.fcc.gov/ecfs/document/view;NEWECFSSESSION=13vPVm1GMFKxLLY35syBzTspYBkFyxzHMKhBpB7TT9hGrjHLV595!1736751079!-973180750?id=60001115477.

broadband providers attempted to collect "tolls" similar to access charges. In fact, users would be furious even if a late-night comic inaccurately told them this was the case.

Furthermore, numerous possible arrangements will allow for a great deal of flexibility for edge providers to find the most economically efficient route onto the combined company's network. There are already several CDNs that have negotiated deals to deliver large amounts of data within these networks, and numerous transit providers compete fiercely to provide access to the Internet. It has been well established that the highly-competitive transit market functionally provides a price ceiling to deliver data to a last-mile access network.[8] This is a key point – the highly competitive transit and CDN markets will continue to provide an alternative to paid interconnection.

A LARGER COMBINED COMPANY CAN BETTER SERVE CONSUMERS

The Commission should not overlook the significant technological and economic benefits that would come from a combined, larger company. A larger footprint and increased economies of scale will allow the company to spread high fixed costs over more customers. Not only do these costs include the important capital expenditures required to expand, maintain, and upgrade parts of its network, but also the expenses of developing innovative new offerings, developing marketing materials, ensuring network security, overall management, and other services. An expanded footprint allows the company to spread these fixed costs over a larger revenue base, thus increasing firm and economy-wide productivity.

Charter has been a leader with its cable technology, rapidly shifting to all-digital distribution. It has consistently worked to improve its plant, offering steadily increasing network capacity over the years. Not only will the transaction bring these improvements to Time Warner Cable's larger network, it will also see continued focus on customer-centered upgrades.

Many innovations in this sector are moving to the fast-paced, iterative design process of software. There is pressure to transition network equipment to software defined networking (SDN) with generalized components and a control plane abstracted into software. Here software-based innovations can be very quickly scaled throughout entire networks, meaning a combined company would be in a better position to not only innovate more quickly, but, more importantly, scale those

[8] *See* David Clark et al., "Interconnection in the Internet: the policy challenge," 39th Research Conference on Communication, Information and Internet Policy, (Aug. 2011).

innovations out to more consumers with lower fixed costs than if separate companies were developing and deploying them.

While it is unfortunate that some of the benefits of SDN and related network functions virtualization (NFV) innovations will likely not be seen on consumer networks due to the Commission's Open Internet Order, these technologies, combined with Charter's larger geographic reach and customer base, will likely see aggressive competition from cable for enterprise customers in coming years.

Some critics of the proposed transaction point to poor customer service ratings of these companies as a reason to reject the deal. Ignoring the fact that these issues are not merger specific, it is important to remember that these are complex industries where much can go wrong. As ITIF has pointed out, consumer ratings of UK broadband offerings are similarly low, despite a much larger number of providers and much more competition due to separation of wholesale and retail networks (e.g., Open Reach).[9] Consumers rightfully have high expectations but often under-appreciate the difficulty in managing an large, advanced network, some of which is out "in the wild," strung on poles or buried underground where much can go wrong. There are also often problems in the computers or routers of the consumer, over which access networks have no control. Indeed, other complex, network industries, such as airlines, also rank low in customer satisfaction and broadband providers consistently rank low across the world. Notwithstanding that this merger would not change the competitive pressures on the combined company, consumer satisfaction is simply not a good ground to question this transaction.

CONCLUSION

Charter, Time Warner Cable, and Bright House Networks operate in complex network industries that depend on both scale and innovation. Regulators should be cautious about interfering on the basis of allocative efficiency presumptions without considering the longer term benefits from increased productive and dynamic efficiency generated by the merger. The proposed transaction offers no or little concern over reduction in competition, but by offering increased scale without reducing competition, the deal is without doubt in the public interest.

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[9] Adams Nager, "How to Misuse American Customer Satisfaction Index Data to Try to Block a Merger," *The Innovation Files* (Mar. 24, 2014), http://www.innovationfiles.org/how-to-misuse-american-customer-satisfaction-index-data-to-try-to-block-a-merger/.

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Doug Brake
Telecommunications Policy Analyst
Information Technology and Innovation Foundation
1101 K Street NW, Suite 610
Washington, DC 20005