

DISSENTING STATEMENT OF COMMISSIONER ROSCOE B. STAREK, III
In the Matter of
Time Warner Inc., et al.
File No. 961 0004

I respectfully dissent from the Commission's decision to accept a consent agreement with Time Warner Inc. ("TW"), Turner Broadcasting System, Inc. ("TBS"), Tele-Communications, Inc. ("TCI"), and Liberty Media Corporation. The proposed complaint against these producers and distributors of cable television programming alleges anticompetitive effects arising from (1) the horizontal integration of the programming interests of TW and TBS and (2) the vertical integration of the TBS's programming interests with TW's and TCI's distribution interests. I am not persuaded that either the horizontal or the vertical aspects of this transaction are likely "substantially to lessen competition" in violation of Section 7 of the Clayton Act, 15 U.S.C. § 18, or otherwise to constitute "unfair methods of competition" in violation of Section 5 of the Federal Trade Commission Act, 15 U.S.C. § 45. Moreover, even if one were to assume the validity of one or more theories of violation underlying this action, the proposed order does not appear to prevent the alleged effects and may instead create inefficiency.

Horizontal Theories of Competitive Harm

This transaction involves, *inter alia*, the combination of TW and TBS, two major suppliers of programming to multichannel video program distributors ("MVPDs"). Accordingly, there is a straightforward theory of competitive harm that merits serious consideration by the Commission. In its most general terms, the theory is that cable operators regard TW programs as close substitutes for TBS programs. Therefore, the theory says, TW and TBS act as premerger constraints on each other's ability to raise program prices. Under this hypothesis, the merger eliminates this constraint, allowing TW -- either unilaterally or in coordination with other program vendors -- to raise prices on some or all of its programs.

Of course, this story is essentially an illustration of the standard theory of competitive harm set forth in Section 2 of the 1992 *Horizontal Merger Guidelines*.¹ Were an investigation pursuant to this theory to yield convincing evidence that it applies to the current transaction, under most circumstances the Commission

¹ U.S. Department of Justice and Federal Trade Commission, *Horizontal Merger Guidelines*, § 2 (1992), 4 Trade Reg. Rep. (CCH) ¶ 13,104 at 20,573-6 *et seq.*

would seek injunctive relief to prevent the consolidation of the assets in question. The Commission has eschewed that course of action, however, choosing instead a very different sort of "remedy" that allows the parties to proceed with the transaction but restricts them from engaging in some (but not all) "bundled" sales of programming to unaffiliated cable operators.² Clearly, this choice of relief implies an unusual theory of competitive harm from what ostensibly is a straightforward horizontal transaction. The Commission's remedy does nothing to prevent the most obvious manifestation of postmerger market power -- an across-the-board price increase for TW and TBS programs. Why has the Commission forgone its customary relief directed against its conventional theory of harm?

The plain answer is that there is little persuasive evidence that TW's programs constrain those of TBS (or vice-versa) in the fashion described above. In a typical FTC horizontal merger enforcement action, the Commission relies heavily on documentary evidence establishing the substitutability of the parties' products or services.³ For example, it is standard to study the parties' internal documents to

² In the *Analysis of Proposed Consent Order to Aid Public Comment* (§ IV.C), the Commission asserts that "the easiest way the combined firm could exert substantially greater negotiating leverage over cable operators is by combining all or some of such 'marquee' services and offering them as a package or offering them along with unwanted programming." As I note below, it is far from obvious why this bundling strategy represents the "easiest" way to exercise market power against cable operators. The easiest way to exercise any newly-created market power would be simply to announce higher programming prices.

³ The *Merger Guidelines* emphasize the importance of such evidence. Section 1.11 specifically identifies the following two types of evidence as particularly informative: "(1) evidence that buyers have shifted or have considered shifting purchases between products in response to relative changes in price or other competitive variables [and] (2) evidence that sellers base business decisions on the prospect of buyer substitution between products in response to relative changes in price or other competitive variables."

To illustrate, in *Coca-Cola Bottling Co. of the Southwest*, Docket No. 9215, complaint counsel argued in favor of a narrow product market consisting of "all

determine which producers they regard as their closest competitors. This assessment also depends frequently on internal documents supplied by customers that show them playing off one supplier against another -- via credible threats of supplier termination -- in an effort to obtain lower prices.

In this matter, however, documents of this sort are conspicuous by their absence. Notwithstanding a voluminous submission of materials from the respondents and third parties (and the considerable incentives of the latter -- especially other cable operators -- to supply the Commission with such documents), there are no documents that reveal cable operators threatening to drop a TBS "marquee" network (e.g., CNN) in favor of a TW "marquee" network (e.g., HBO). There also are no documents from, for instance, TW suggesting that it sets the prices of its "marquee" networks in reference to those of TBS, taking into account the latter's likely competitive response to unilateral price increases or decreases. Rather, the evidence supporting any prediction of a postmerger price increase consists entirely of customers' contentions that program prices would rise

branded carbonated soft drinks" ("CSDs"), while respondent argued for a much broader market. In determining that all branded CSDs constituted the relevant market, the Commission placed great weight on internal documents from local bottlers of branded CSDs showing that those bottlers "[took] into account only the prices of other branded CSD products [and not the prices of private label or warehouse-delivered soft drinks] in deciding on pricing for their own branded CSD products." 5 Trade Reg. Rep. (CCH) ¶ 23,681 at 23,413 (Aug. 31, 1994), *vacated and remanded on other grounds, Coca-Cola Bottling Co. of the Southwest v. FTC*, No. 94-41224 (5th Cir., June 10, 1996). (The Commission dismissed its complaint on September 6, 1996.)

following the acquisition. Although customers' opinions on the potential effects of a transaction often are important, they seldom are dispositive. Typically the Commission requires substantial corroboration of these opinions from independent information sources.⁴

Independent validation of the anticompetitive hypothesis becomes particularly important when key elements of the story lack credibility. For a standard horizontal theory of harm to apply here, one key element is that, prior to the acquisition, a MVPD could credibly threaten to drop a marquee network (e.g., CNN), provided it had access to another programmer's marquee network (e.g., HBO) that it could offer to potential subscribers. This threat would place the MVPD in a position to negotiate a better price for the marquee networks than if

⁴ For example, in *R.R. Donnelley Sons & Co., et al.*, Docket No. 9243, the Administrative Law Judge's decision favoring complaint counsel rested in part on his finding that "[a]s soon as the Meredith/Burda acquisition was announced, customers expressed concern to the FTC and the parties about the decrease in competition that might result." (Initial Decision Finding 404.) In overturning the ALJ's decision, the Commission cautioned: "There is some danger in relying on these customer complaints to draw any general conclusions about the likely effects of the acquisition or about the analytical premises for those conclusions. The complaints are consistent with a variety of effects, and many -- including those the ALJ relied upon -- directly contradict [c]omplaint [c]ounsel's prediction of unilateral price elevation." 5 Trade Reg. Rep. (CCH) ¶ 23,876 at 23,660 n.189 (July 21, 1995).

Also, in several instances involving hospital mergers in concentrated markets, legions of third parties came forth to attest to the transaction's efficiency. The Commission has discounted this testimony, however, when these third parties could not articulate or document the source of the claimed efficiency, or when the testimony lacked corroboration from independent information sources. I believe that the Commission should apply the same evidentiary standards to the third-party testimony in the current matter.

those networks were jointly owned.

Here, the empirical evidence gathered during the investigation reveals that such threats would completely lack credibility. Indeed, there appears to be little, if any, evidence that such threats ever have been made, let alone carried out. CNN and HBO are not substitutes, and both are carried on virtually all cable systems nationwide. If, as a conventional horizontal theory of harm requires, these program services are truly substitutes -- if MVPDs regularly play one off against the other, credibly threatening to drop one in favor of another -- then why are there virtually no instances in which an MVPD has carried out this threat by dropping one of the marquee services? The absence of this behavior by MVPDs undermines the empirical basis for the asserted degree of substitutability between the two program services.⁵

Faced with this pronounced lack of evidence to support a conventional market power story and a conventional remedy, the Commission has sought refuge

⁵ In virtually any case involving less pressure to come up with something to show for the agency's strenuous investigative efforts, the absence of such evidence would lead the Commission to reject a hypothesized product market that included both marquee services. Suppose that two producers of product A proposed to merge and sought to persuade the Commission that the relevant market also included product B, but they could not provide any examples of actual substitution of B for A, or any evidence that threats of substitution of B for A actually elicited price reductions from sellers of A. In the usual run of cases, this lack of substitutability would almost surely lead the Commission to reject the expanded market definition. But not so here.

in what appears to be a very different theory of postmerger competitive behavior. This theory posits an increased likelihood of program "bundling" as a consequence of the transaction.⁶ But there are two major problems with this theory as a basis for an enforcement action. First, there is no strong theoretical or empirical basis for believing that an increase in bundling of TW and TBS programming would occur postmerger. Second, even if such bundling did occur, there is no particular reason to think that it would be competitively harmful.

Given the lack of documentary evidence to show that TW intends to bundle its programming with that of TBS, I do not understand why the majority considers an increase in program bundling to be a likely feature of the postmerger equilibrium, nor does economic theory supply a compelling basis for this prediction. Indeed, the rationale for this element of the case (as set forth in the *Analysis to Aid Public Comment*) can be described charitably as "incomplete." According to the *Analysis*, unless the FTC prevents it, TW would undertake a bundling strategy in part to foist "unwanted programming" upon cable operators.⁷ Missing from the *Analysis*,

⁶ As I noted earlier, a remedy that does nothing more than prevent "bundling" of different programs would fail completely to prevent the manifestations of market power -- such as across-the-board price increases -- most consistent with conventional horizontal theories of competitive harm.

⁷ As I have noted, *supra* n.2, the *Analysis* also claims that TW could obtain "substantially greater negotiating leverage over cable operators . . . by combining all or some of [the merged firm's] 'marquee' services and offering them as a package . . ." If the *Analysis* uses the term "negotiating leverage" to mean "market power" as the latter is conventionally defined, then it confronts three

however, is any sensible explanation of *why* TW should wish to pursue this strategy, because the incentives to do so are not obvious.⁸

A possible anticompetitive rationale for "bundling" might run as follows: by requiring cable operators to purchase a bundle of TW and TBS programs that contains substantial amounts of "unwanted" programming, TW can tie up scarce channel capacity and make entry by new programmers more difficult. But even if that strategy were assumed *arguendo* to be profitable,⁹ the order would have only

difficulties: (1) the record fails to support the proposition that the TW and TBS "marquee" channels are close substitutes for each other; (2) even assuming that those channels are close substitutes, there are more straightforward ways for TW to exercise postmerger market power; and (3) the remedy does nothing to prevent these more straightforward exercises of market power. See discussion *supra*.

⁸ In "A Note on Block Booking" in *THE ORGANIZATION OF INDUSTRY* (1968), George Stigler analyzed the practice of "block booking" -- or, in current parlance, "bundling" -- "marquee" motion pictures with considerably less popular films. Some years earlier, the United States Supreme Court had struck this practice down as an anticompetitive "leveraging" of market power from desirable to undesirable films. *United States v. Loew's Inc.*, 371 U.S. 38 (1962). As Stigler explained (at 165), it is not obvious why distributors should wish to force exhibitors to take the inferior film:

Consider the following simple example. One film, Justice Goldberg cited *Gone with the Wind*, is worth \$10,000 to the buyer, while a second film, the Justice cited *Getting Gertie's Garter*, is worthless to him. The seller could sell the one for \$10,000, and throw away the second, for no matter what its cost, bygones are forever bygones. Instead the seller compels the buyer to take both. But surely he can obtain no more than \$10,000, since by hypothesis this is the value of both films to the buyer. Why not, in short, use his monopoly power directly on the desirable film? It seems no more sensible, on this logic, to block book the two films than it would be to compel the exhibitor to buy *Gone with the Wind* and seven Ouija boards, again for \$10,000.

⁹ The argument here basically is a variant of the argument often used to condemn exclusive dealing as a tool for monopolizing a market. Under this argument, an upstream monopolist uses its market power to obtain exclusive

a trivial impact on TW's ability to pursue it. The order prohibits only the bundling of TW programming with TBS programming; TW remains free under the order to create new "bundles" comprising exclusively TW, or exclusively TBS, programs. Given that many TW and TBS programs are now sold on an unbundled basis -- a fact that calls into question the likelihood of increased postmerger bundling¹⁰ -- and given that, under the majority's bundling theory, *any* TW or TBS programming

distribution rights from its distributors, thereby foreclosing potential manufacturing entrants and obtaining additional market power. But there is problem with this argument, as Bork explains in THE ANTITRUST PARADOX (1978):

[The monopolist] can extract in the prices it charges retailers all that the uniqueness of its line is worth. It cannot charge the retailer that full worth in money and then charge it again in exclusivity the retailer does not wish to grant. To suppose that it can is to commit the error of double counting. If [the firm] must forgo the higher prices it could have demanded in order to get exclusivity, then exclusivity is not an imposition, it is a purchase.

Id. at 306; *see also id.* at 140-43.

Although modern economic theory has established the theoretical possibility that a monopolist might, under very specific circumstances, outbid an entrant for the resources that would allow entry to occur (thus preserving the monopoly), modern theory also has shown that this is not a generally applicable result. It breaks down, for example, when (as is likely in MVPD markets) many units of new capacity are likely to become available sequentially. *See, e.g.,* Krishna, "Auctions with Endogenous Valuations: The Persistence of Monopoly Revisited," 83 *Am. Econ. Rev.* 147 (1993); Malueg and Schwartz, "Preemptive investment, toehold entry, and the mimicking principle," 22 *RAND J. Econ.* 1 (1991).

¹⁰ If bundling is profitable for anticompetitive reasons, why do we not observe TW and TBS now exploiting all available opportunities to reap these profits?

can tie up a cable channel and thereby displace a potential entrant's programming, the order hardly would constrain TW's opportunities to carry out this "foreclosure" strategy.

Finally, all of the above analysis implicitly assumes that the bundling of TW and TBS programming, if undertaken, would more likely than not be anticompetitive. The *Analysis to Aid Public Comment*, however, emphasizes that bundling programming in many other instances can be *pro*competitive. There seems to be no explanation of why the particular bundles at issue here would be anticompetitive, and no articulation of the principles that might be used to differentiate welfare-enhancing from welfare-reducing bundling.¹¹

Thus, I am neither convinced that increased program bundling is a likely consequence of this transaction nor persuaded that any such bundling would be anticompetitive. Were I convinced that anticompetitive bundling is a likely

¹¹ Perhaps this reflects the fact that the economics literature does not provide clear guidance on this issue. See, e.g., Adams and Yellen, "Commodity Bundling and the Burden of Monopoly," 90 *Q.J. Econ.* 475 (1976). Adams and Yellen explain how a monopolist might use bundling as a method of price discrimination. (This also was Stigler's explanation, *supra* n.8.) As Adams and Yellen note, "public policy must take account of the fact that prohibition of commodity bundling without more may increase the burden of monopoly . . . [M]onopoly itself must be eliminated to achieve high levels of social welfare." 90 *Q.J. Econ.* at 498. Adams and Yellen's conclusion is apposite here: if the combination of TW and TBS creates (or enhances) market power, then the solution is to enjoin the transaction rather than to proscribe certain types of bundling, since the latter "remedy" may actually make things worse. And if the acquisition does not create or enhance market power, the basis for the bundling proscription is even harder to discern.

consequence of this transaction, I would find the proposed remedy inadequate.

Vertical Theories of Competitive Harm

The proposed consent order also contains a number of provisions designed to alleviate competitive harm purportedly arising from the increased degree of vertical integration between program suppliers and program distributors brought about by this transaction.¹² I have previously expressed my skepticism about enforcement actions predicated on theories of harm from vertical relationships.¹³ The current complaint and proposed order only serve to reinforce my doubts about such enforcement actions and about remedies ostensibly designed to address the alleged competitive harms.

The vertical theories of competitive harm posited in this matter, and the associated remedies, are strikingly similar to those to which I objected in *Silicon Graphics, Inc.* ("SGI"), and the same essential criticisms apply. In *SGI*, the Commission's complaint alleged anticompetitive effects arising from the vertical integration of SGI -- the leading manufacturer of entertainment graphics workstations -- with Alias Research, Inc., and Wavefront Technologies, Inc. -- two leading suppliers of entertainment graphics software. Although the acquisition seemingly raised straightforward horizontal competitive problems arising from the combination of Alias and Wavefront, the Commission inexplicably found that the

¹² Among other things, the order (1) constrains the ability of TW and TCI to enter into long-term carriage agreements (¶ IV); (2) compels TW to sell Turner programming to downstream MVPD entrants at regulated prices (¶ VI); (3) prohibits TW from unreasonably discriminating against non-TW programmers seeking carriage on TW cable systems (¶ VII(C)); and (4) compels TW to carry a second 24-hour news service (*i.e.*, in addition to CNN) (¶ IX).

¹³ Dissenting Statement of Commissioner Roscoe B. Starek, III, in *Waterous Company, Inc./Hale Products, Inc.*, File No. 901 0061, 5 Trade Reg. Rep. (CCH) ¶ 24,076 at 23,888-90; Dissenting Statement of Commissioner Roscoe B. Starek, III, in *Silicon Graphics, Inc. (Alias Research, Inc., and Wavefront Technologies, Inc.)*, Docket No. C-3626 (Nov. 14, 1995), 61 Fed. Reg. 16797 (Apr. 17, 1996); Remarks of Commissioner Roscoe B. Starek, III, "Reinventing Antitrust Enforcement? Antitrust at the FTC in 1995 and Beyond," remarks before a conference on "A New Age of Antitrust Enforcement: Antitrust in 1995" (Marina Del Rey, California, Feb. 24, 1995) [available on the Commission's World Wide Web site at <http://www.ftc.gov>].

horizontal consolidation was not anticompetitive on net.¹⁴ Instead, the order addressed only the alleged vertical problems arising from the transaction. The Commission alleged, *inter alia*, that the acquisitions in *SGI* would reduce competition through two types of foreclosure: (1) nonintegrated software vendors would be excluded from the SGI platform, thereby inducing their exit (or deterring their entry); and (2) rival hardware manufacturers would be denied access to Alias and Wavefront software, without which they could not effectively compete against SGI. Similarly, in this case the Commission alleges (1) that nonintegrated program vendors will be excluded from TW and TCI cable systems and (2) that potential MVPD entrants into TW's cable markets will be denied access to (or face

¹⁴ I say "inexplicably" not because I necessarily believed this horizontal combination should have been enjoined, but because the horizontal aspect of the transaction would have exacerbated the upstream market power that would have had to exist for the vertical theories to have had any possible relevance.

supracompetitive prices for) TW and TBS programming -- thus lessening their ability to effectively compete against TW's cable operations. The complaint further charges that the exclusion of nonintegrated program vendors from TW's and TCI's cable systems will deprive those vendors of scale economies, render them ineffective competitors *vis-à-vis* the TW/Turner programming services, and thus confer market power on TW as a seller of programs to MVPDs in non-TW/non-TCI markets.

My dissenting statement in *SGI* identified the problems with this kind of analysis. For one thing, these two types of foreclosure -- foreclosure of independent program vendors from the TW and TCI cable systems, and foreclosure of independent MVPD firms from TW and TBS programming -- tend to be mutually exclusive. The very possibility of excluding independent program vendors from TW and TCI cable systems suggests the means by which MVPDs other than TW and TCI can avoid foreclosure. The nonintegrated program vendors surely have incentives to supply the "foreclosed" MVPDs, and each MVPD has incentives to induce nonintegrated program suppliers to produce programming for it.¹⁵

¹⁵ Moreover, as was also true in *SGI*, the proposed complaint in the present case characterizes premerger entry conditions in a way that appears to rule out significant anticompetitive foreclosure of nonintegrated upstream producers as a consequence of the transaction. Paragraphs 33, 34, and 36 of the complaint allege in essence that there are few producers of "marquee" programming before the merger (other than TW and TBS), in large part because entry into "marquee" programming is so very difficult (stemming from, *e.g.*, the substantial irreversible investments that are required). If that is true -- *i.e.*, if the posited programming

In response to this criticism, one might argue -- and the complaint alleges¹⁶ -- that pervasive scale economies in programming, combined with a failure to obtain carriage on the TW and TCI systems, would doom potential programming entrants (and "foreclosed" incumbent programmers) because, without TW and/or TCI carriage, they would be deprived of the scale economies essential to their survival. In other words, the argument goes, the competitive responses of "foreclosed" programmers and "foreclosed" distributors identified in the preceding paragraph never will materialize. There are, however, substantial conceptual and empirical problems with this argument, and its implications for competition policy have not been fully explored.

First, if one believes that programming is characterized by such substantial scale economies that the loss of one large customer results in the affected programmer's severely diminished competitive effectiveness (in the limit, that programmer's exit), then this essentially is an argument that the number of program producers that can survive in equilibrium (or, perhaps more accurately, the number of program producers in a particular program "niche") will be small -- with perhaps only one survivor. Under the theory of the current case, this will result in

market already was effectively foreclosed before the merger -- then, as in *SGI*, TW's acquisition of TBS could not cause substantial postmerger foreclosure of competitively significant alternatives to TW/TBS programming.

¹⁶ See Paragraph 38.b of the proposed complaint.

a supracompetitive price for that program. Further, this will occur *irrespective of the degree of vertical integration between programmers and distributors*. Indeed, under these circumstances, there is a straightforward reason why vertical integration between a program distributor and a program producer would be both profitable *and* procompetitive (*i.e.*, likely to result in *lower* prices to consumers): instead of monopoly markups by both the program producer and the MVPD, there would be only one markup by the vertically integrated firm.¹⁷

Second, and perhaps more important, if the reasoning of the complaint is carried to its logical conclusion, it constitutes a basis for challenging *any* vertical integration by large cable operators or large programmers -- even if that vertical integration were to occur via *de novo* entry by an operator into the programming market, or by *de novo* entry by a programmer into distribution. Consider the following hypothetical: A large MVPD announces both that it intends to enter a particular program niche and that it plans to drop the incumbent supplier of that type of programming. According to the theory underlying the proposed complaint,

¹⁷ See, *e.g.*, Tirole, THE THEORY OF INDUSTRIAL ORGANIZATION 174-76 (1988). The program price reductions would be observed only in those geographic markets where TW owned cable systems. Thus, the greater the number of cable subscribers served by TW, the more widespread would be the efficiencies. According to the proposed complaint (¶ 32), TW cable systems serve only 17 percent of cable subscribers nationwide, so one might argue that the efficiencies are accordingly limited. But this, of course, leaves the Commission in the uncomfortable position of arguing that TW's share of total cable subscribership is too small to yield significant efficiencies, yet easily large enough to generate substantial "foreclosure" effects.

the dropped program would suffer substantially from lost scale economies, severely diminishing its competitive effectiveness, which in turn would confer market power on the vertically integrated entrant in its program sales to other MVPDs. Were the Commission to apply its current theory of competitive harm consistently, it evidently would have to find this *de novo* entry into programming by this large MVPD competitively objectionable.

I suspect, of course, that virtually no one would be comfortable challenging such integration, since there is a general predisposition to regard expansions of capacity as procompetitive.¹⁸ Consequently, one might attempt to reconcile the differential treatment of the two forms of vertical integration by somehow distinguishing them from each other.¹⁹ But in truth, the situations actually merit

¹⁸ This would appear true especially when, as posited here, there is substantial premerger market power upstream because, under such circumstances, vertical integration is a means by which a downstream firm can obtain lower input prices. As noted earlier (*supra* n.17 and accompanying text), this integration can be procompetitive whether it occurs via merger or internal expansion.

¹⁹ One might attempt to differentiate my hypothetical from a situation involving an MVPD's acquisition of a program supplier by arguing that the former would yield two suppliers of the relevant type of programming, but the latter only one. But this conclusion would be incorrect. If we assume that the number of suppliers that can survive in equilibrium is determined by the magnitude of scale economies relative to the size of the market, and that the pre-entry market structure represented an equilibrium, then the existence of two program suppliers will be only a transitory phenomenon, and the market will revert to the equilibrium structure dictated by these technological considerations -- that is, one supplier. Upstream integration by the MVPD merely replaces one program monopolist with another; but as noted above, under these circumstances vertical integration can yield substantial efficiencies.

similar treatment -- albeit not the treatment prescribed by the proposed order. In neither case should an enforcement action be brought, because any welfare loss flowing from either scenario derives from the structure of the upstream market, which in turn is determined primarily by the size of the market and by technology, not by the degree of vertical integration between different stages of production.

Third, it is far from clear that TCI's incentives to preclude entry into programming are the same as TW's.²⁰ As an MVPD, TCI is harmed by the creation of entry barriers to new programming. Even if TW supplies it with TW programming at a competitive price, TCI is still harmed if program variety or innovation is diminished. On the other hand, as a part owner of TW, TCI benefits if TW's programming earns supracompetitive returns on sales to other MVPDs. TCI's *net* incentive to sponsor new programming depends on which factor dominates -- its interest in program quality and innovation, or its interest in supracompetitive returns on TW programming. All of the analyses of which I am aware concerning this tradeoff show that TCI's ownership interest in TW would have to increase substantially -- far beyond what the current transaction contemplates, or what would be possible without a significant modification of

²⁰ Even TW has mixed incentives to preclude programming entry. As a programmer allegedly in possession of market power, TW would wish to deter programming entry to protect this market power. But as a MVPD, TW -- like any other MVPD -- benefits from the creation of valuable new programming services that it can sell to its subscribers. On net, however, it appears true that TW's incentives balance in favor of wishing to prevent entry.

TW's internal governance structure²¹ -- for TCI to have an incentive to deter entry by independent programmers. TCI's incentive to encourage programming entry is intensified, moreover, by the fact that it has undertaken an ambitious expansion program to digitize its system and increase capacity to 200 channels. Because this appears to be a costly process, and because not all cable customers can be expected to purchase digital service, the cost per buyer -- and thus the price -- of digital services will be fairly high. How can TCI expect to induce subscribers to buy this expensive service if, through programming foreclosure, it has restricted the quantity and quality of programming that would be available on this service tier?²²

The foregoing illustrates why foreclosure theories fell into intellectual

²¹ TW has a "poison pill" provision that would make it costly for TCI to increase its ownership of TW above 18 percent.

²² Note too that there is an inverse relationship between TCI's *ability* to prevent programming entry and its *incentives* to do so. Much of the analysis in this case has emphasized that TCI's size (27 percent of cable households) gives it considerable ability to determine which programs succeed and which fail, and the logic of the proposed complaint is that TCI will exercise this ability so as to protect TW's market power in program sales to non-TW/non-TCI MVPDs. But although increases in TCI's size may increase its ability to preclude entry into programming, at the same time such increases reduce TCI's *incentives* to do so. The reasoning is simple: as the size of the non-TW/non-TCI cable market shrinks, the supracompetitive profits obtained from sales of programming to this sector also shrink. Simultaneously, the harm from TCI (as a MVPD) from precluding the entry of new programmers increases with TCI's subscriber share. (In the limit -- *i.e.*, if TCI and TW controlled *all* cable households -- there would be no non-TW/non-TCI MVPDs, no sales of programming to such MVPDs, and thus no profits to be obtained from such sales.) Any future increases in TCI's subscriber share would, other things held constant, reduce its incentives to "foreclose" entry by independent programmers.

disrepute: because of their inability to articulate how vertical integration harms competition and not merely competitors. The majority's analysis of the Program Service Agreement ("PSA") illustrates this perfectly. The PSA must be condemned, we are told, because a TCI channel slot occupied by a TW program is a channel slot that cannot be occupied by a rival programmer. As Bork noted, this is a tautology, not a theory of competitive harm.²³ It *is* a theory of harm to competitors -- competitors that cannot offer TCI inducements (such as low prices) sufficient to cause TCI to patronize them rather than TW.

All of the majority's vertical theories in this case ultimately can be shown to be theories of harm to competitors, not to competition. Thus, I have not been persuaded that the vertical aspects of this transaction are likely to diminish competition substantially. Even were I to conclude otherwise, however, I could not support the extraordinarily regulatory remedy contained in the proposed order, two of whose provisions merit special attention: (1) the requirement that TW sell programming to MVPDs seeking to compete with TW cable systems at a price determined by a formula contained in the order; and (2) the requirement that TW carry at least one "Independent Advertising-Supported News and Information National Video Programming Service."

Under Paragraph VI of the proposed order, TW must sell Turner programming

²³ Bork, *THE ANTITRUST PARADOX*, *supra* n.9, at 304.

to potential entrants into TW cable markets at prices determined by a "most favored nation" clause that gives the entrant the same price -- or, more precisely, the same "carriage terms" -- that TW charges the three largest MVPDs currently carrying this programming. As is well known, most favored nation clauses have the capacity to cause all prices to rise rather than to fall.²⁴ But even putting this possibility aside, this provision of the order converts the Commission into a *de facto* price regulator -- a task, as I have noted on several previous occasions, to which we are ill-suited.²⁵ During the investigation third parties repeatedly informed me of the difficulty that the Federal Communications Commission has encountered in attempting to enforce its nondiscrimination regulations. The FTC's regulatory burden would be lighter only because, perversely, our pricing formula would disallow any of the efficiency-based rationales for differential pricing recognized by the Congress and the FCC.²⁶

²⁴ See, e.g., *RxCare of Tennessee, Inc., et al.*, Docket No. C-3664, 5 Trade Reg. Rep. (CCH) ¶ 23,957 (June 10, 1996); see also Cooper and Fries, "The most-favored-nation pricing policy and negotiated prices," 9 *Int'l J. Ind. Org.* 209 (1991). The logic is straightforward: if by cutting price to another (noncompeting) MVPD TW is compelled also to cut price to downstream competitors, the incentive to make this price cut is diminished. Although this effect might be small in the early years of the order (when the gains to TW from cutting price to a large, independent MVPD might swamp the losses from cutting price to its downstream competitors), its magnitude will grow over the order's 10-year duration, as TW cable systems confront greater competition.

²⁵ See my dissenting statements in *Silicon Graphics and Waterous/Hale*, *supra* n.13.

²⁶ Mirroring the applicable statute, the FCC rules governing the sale of cable programming by vertically integrated programmers to nonaffiliated MVPDs allow for price differentials reflecting, *inter alia*, "economies of scale, cost savings, or other

Most objectionable is Paragraph IX of the order, the "must carry" provision that compels TW to carry an additional 24-hour news service. I am baffled how the Commission has divined that consumers would prefer that a channel of supposedly scarce cable capacity be used for a second news service, instead of for something else. More generally, although remedies in horizontal merger cases sometimes involve the creation of a new competitor to replace the competition eliminated by the transaction, no competitor has been lost in the present case. Indeed, there is substantial entry *already occurring* in this segment of the programming market, notwithstanding the severe "difficulty" of entering the markets alleged in the complaint.²⁷ Obviously, the incentives to buy programming from an independent vendor are diminished (all else held constant) when a distributor integrates vertically into programming. This is true whether the integration is procompetitive or anticompetitive on net, and whether the integration occurs via merger or via *de novo* entry.²⁸ I could no more support a must-carry provision for TW as a result of its acquisition of CNN than I could endorse a similar requirement to remedy the "anticompetitive consequences" of *de novo* integration by TW into the news business.

direct and legitimate economic benefits reasonably attributable to the number of subscribers served by the distributor." 47 U.S.C. § 548(c)(2)(B)(iii); 47 C.F.R. § 76.1002(b)(3).

²⁷ The Microsoft/NBC joint venture, MSNBC, already is in service; the Fox entry apparently will also be operational shortly.

²⁸ The premise inherent in this provision of the order is that TW can "foreclose" independent programming entry independently (*i.e.*, without the cooperation of TCI, whose incentives to sponsor independent programming are ostensibly preserved by the stock ownership cap contained in Paragraphs II and III of the order). Given that TW has only 17 percent of total cable subscribership, I find this proposition fanciful.