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Conception to Distribution: Vertical Integration in the Television Production and ISP Industry

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CONCEPTION TO DISTRIBUTION: VERTICAL INTEGRATION IN THE TELEVISION PRODUCTION AND ISP INDUSTRY

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ABSTRACT

The intersecting regulations of agencies, stemming from the duties of the FCC, the FTC, and the DOJ to protect competition and television consumers, have been innovative in permitting two goals, first, allowing companies to pursue these integrations and, second, placing conditions on integrations to prevent potential harms that could come from developing media giants. As the market continues to consolidate, with companies having more access to the ability to distribute through alternative middlemen, and as they have the opportunity to gain popularity through social media networks and word of mouth, the healthy competition seen in the former entertainment industry is likely to be sustained. While the structural elements of the industry will likely remain the same, merely the faces will change. Instead of viewing a DVD or VHS, consumers will log onto online streaming websites. And, instead of successful products coming from independent production studios, even the garage director will have the opportunity to produce popular content. Summarily, vertical integration is merely a method for the traces of former companies to survive and a method for them to change with the times. Because they have the resources to develop the Internet networks, they are able to fit into the market, and, because they can purchase content from others using those revenues, it is likely that the companies will either change their business models or they will lose their production sides, as has been seen with the AOL/Timer Warner merger and the Hughes Electronics Corporation/News Corporation transaction. Where a few of the benefits and harms of these integrations have been elaborated here, the majority of the effects have yet to be seen.

I. INTRODUCTION

Mergers between Internet Service Providers ("ISPs") and television production companies potentially harm competition in the television market by excluding multichannel video programming distributor ("MVPD") rivals from access to video programming, and increasing the price thereof. This could then raise rivals' costs and increase consumers' prices.[1] And merged companies' new ability to limit competition in distribution is likely to inhibit "diversity and localism in broadcast television and video programming distribution."[2]

The Federal Communications Commission ("FCC") and the Department of Justice ("DOJ") attempted to limit the ability of vertical integrations to compromise competition by constraining the recent NBCUniversal/Comcast joint venture.[3] However, "a joint venture is an integration of operations likely to lead to the expansion of output, and it thereby deserves permissive antitrust treatment."[4] The relaxed scrutiny permitted the DOJ and the FCC to place constraints sufficient

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[1] Jonathan B. Baker, *Comcast/NBCU: The FCC Provides A Roadmap for Vertical Merger Analysis*, 25 ANTITRUST, Spring 2011, at 36.

[2] Applications of Comcast Corporation, General Electric Company and NBC Universal, Inc. for Consent to Assign Licenses and Transfer Control of Licensees, 26 FCC Rcd. 4238, 4240 (2011) [hereinafter Comcast].

[3] *Id.* at 4238.

[4] Joseph F. Brodley, *Joint Ventures and Antitrust Policy*, 95 HARV. L. REV. 1521, 1525 (1982) (footnotes omitted).

to protect competition and diversity; however, the analysis was less based on the standard mechanical analysis of the markets into which the merged companies entered, and more based on the comparison of the harms and benefits of the merger.[5] The final constraints the departments chose to apply included: (1) assurance of reasonable access to programming, (2) maintenance of access to NBCUniversal/Comcast's distribution channels, and (3) protection of online video distribution competition.[6] These limitations—imposed on only the most recent vertical integration—identify the potential anticompetitive effects of permitting cooperation between ISPs and television production companies.[7] Whether these constraints are sufficient to guard against the potential harms of permitting vertical integration is an issue in light of the slighter scrutiny applied to joint ventures.[8] Based on previous interactions between Hollywood and the United States government, the fear of permissive screenings is minimized.[9]

Past interactions between the entertainment industry and the United States government, specifically the interactions surrounding the Paramount decrees, have shown that in this realm, there is uncharted territory, especially because of the involvement of intellectual property rights and new technologies. The question at hand is whether the NBCUniversal/Comcast merger should be an example for the DOJ to follow for all future mergers, or whether meddling in the affairs of the entertainment industry will lead to disparities in market shares and potential damage to public welfare. This question is complicated by the FCC's duty to "[support] the nation's economy by ensuring an appropriate competitive framework for the unfolding of the communications revolution," and to promote diversity and localism, and encourage innovation.[10] The involvement of the FCC heightens the scrutiny of the television industry, and increases the number of regulators watching over the television industry.[11] Thus, the question not only addresses the health of competition in the entertainment industry, but also the ability of the television companies to provide a diverse and innovative experience for consumers. This paper seeks to address these questions by looking at the recent limitations placed on NBCUniversal, and at the anniversary mark of the approval of the joint venture, to determine whether the industry and the public welfare will be helped or hindered by this merger.

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[5] *Id.*

[6] *Id.* at 3.

[7] *See* Comcast, *supra* note 2, at 4250.

[8] *See* Thomas A. Piraino, Jr., *The Antitrust Analysis of Joint Ventures After the Supreme Court's Dagher Decision*, 57 EMORY L.J. 735, 738–39 (2008).

[9] *See* Charles W. McCoy, Jr., *The Paramount Cases: Golden Anniversary in a Rapidly Changing Market*, 2 ANTITRUST, Summer 1988, at 32. "The motion picture industry, perhaps more than any other, has been continuously monitored by antitrust regulators." *Id.*

[10] *What We Do*, FCC, http://www.fcc.gov/what-we-do (last visited Feb. 22, 2012).

[11] Gene I. Kimmelman, Chief Counsel for Competition Policy & Intergovernmental Relations, Antitrust Enforcement and Media Industries: Competition And Beyond for the American Antitrust Institute's Civil Liberties and Competition Policy Conference (June 21, 2012), *in* 2012 WL 2491339 (F.T.C.), at *4.

II. CHANGES IN THE MARKET

The entertainment industry is changing.[12] The Internet rang the death knell for the music CD, and the bell will likely toll for the DVD and Blu-ray in the near future. As consumers increased their consumption of online home entertainment, the need for television and movie theatres declined, thus, changing the market dynamics in the distribution and production industries.[13] Accordingly, major entertainment companies were forced to keep up with the times by altering their corporate structures.[14] Within the past ten years, content producers and providers merged to assure the future success of their companies, including: CBS and Viacom; AT&T, TCI, MediaOne, Comcast and Universal; Time Warner and AOL; and News Corporation-Hughes.[15]

In the network provision and television production industries, capital is king. When markets shifted from physical to electronic distribution, companies with large capital stores and huge shares of market power were favored. Their savior came in the form of revenue gained from the market in which they already operated in natural monopoly—the ISP market.[16] The following sections describe how companies and the government responded to the changes in the market, including how companies generate revenue in the current distribution environment, how the government has sought to regulate these media mergers in the past, and the most recent government action regulating the NBCUniversal/Comcast merger.

A. Modern Business Models

Modernly, MVPDs profit by bundling cable packages.[17] For example, those seeking a channel that offers child programming may be offered a package including a child programming station, but they will also be required to purchase a sports network and a news network. Regardless of the means of distribution—by satellite or terrestrially—cable companies typically offer (1) a basic tier consisting

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[12] Electronic delivery is expected to have 13.8% compound growth between 2011 and 2015. Paul Bond, *Film Industry, Led By Electronic Delivery, Will Grow in Every Category Through 2015: Report (Exclusive)*, HOLLYWOOD REP. (June 14, 2001, 12:01 AM), http://www.hollywoodreporter.com/news/film-industry-led-by-electronic-200881. This is followed by growth in "cinema advertising (6.7%), the box office (6.1%), physical sell-through (3.9%) and in-store rentals (1.4%). Globally, the order in growth nearly identical, the exception being that the box office will slightly outpace cinema advertising." *Id.*

[13] *See generally* Susan P. Crawford, *The Communications Crisis in America*, 5 HARV. L. & POL'Y REV. 245, 249–254 (2011).

[14] *Id.* at 256–63. For more information on future regulations that will affect how internet is consumed, see Edward Wyatt & Jennifer Steinhauer, *Congress to Sell Public Airwaves to Pay Benefits*, N.Y. TIMES (Feb. 17, 2012) at A1, *available at* http://www.nytimes.com/2012/02/17/business/media/congress-to-sell-public-airwaves-to-pay-benefits.html?_r=1&nl=todaysheadlines&emc=tha2. To better accommodate the growing need for Internet connections, the United States government has developed a plan to auction television broadcast spectrum to expand wireless broadband, where the proceeds for the auction will go towards fostering unemployment and medical benefits, and television companies that voluntarily relinquish their spectrum will be offered compensation for doing so. *Id.*

[15] DANIEL L. BRENNER, MONROE E. PRICE, MICHAEL I. MEYERSON, CABLE TELEVISION AND OTHER NONBROADCAST VIDEO § 4:21 (2011).

[16] *See infra* Part III.A.i.

[17] T. Randolph Beard et. al., *A La Carte and "Family Tiers" As A Response to A Market Defect in the Multichannel Video Programming Market,* 15 COMMLAW CONSPECTUS 31, 37–44 (2006).

of local, governmental and public access channels; (2) an extended tier including basic bundle plus an additional thirty-six cable networks; (3) a premium tier with the option of several bundles, which include sets of packaged networks; (4) a pay-per-view tier; and (5) a family tier.[18] These bundled packages give MVPDs the opportunity to force access to channels that range in popularity in the hope that consumption of the bundles generate future demand for the programs featured on less popular channels.[19]

With over 166 million premium program services sold to subscribers, as compared to the 60 million basic subscribers, the cable industry derives most of its $93 billion in revenue from its premium subscribers and only $35 billion from its basic subscribers.[20] Subscription fees and advertisements derived from cable companies generate the revenue used to purchase programs and to pay television production companies for their content.[21] However, if consumers are given the option to purchase individual episodes of television programs, more consumers will "cut the cord" and cancel cable subscriptions, in preference of viewing content online for a lower price.[22] The "cord cutting" trend has been mounting for several years, and it saw a jump in 2010 when the number of consumers—for the first time—declined in overall subscribership.[23]

Television is still a popular form of entertainment consumption; however, consumers modernly prefer their computer and Internet over television for entertainment and enjoy consuming their television content on the Internet as well.[24] Because of shifts in distribution from cable to Internet, the revenue strategies of entertainment companies have shifted accordingly.[25] The lack of bundling revenue has shifted the burden to advertisement and subscriptions.[26]

Three potential business models for the Internet distribution of films include: (1) ad-supported content, (2) unlimited streaming subscriptions, and (3) electronic-

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[18] Holly Phillips, *I Want My MTV, but Not Your VH1: A La Carte Cable, Bundling, and the Potential Great Cable Compromise*, 28 J. NAT'L ASS'N ADMIN. L. JUDICIARY 321, 368 (2008).

[19] *Id.*

[20] U.S. Census Bureau, *1142—Cable and Premium TV—Summary*, THE 2012 STATISTICAL ABSTRACT (Sept. 28, 2011), *available at* http://www.census.gov/compendia/statab/2012/tables/12s1142.xls.

[21] Adam B. Vanwagner, *Seeking A Clearer Picture: Assessing the Appropriate Regulatory Framework for Broadband Video Distribution*, 79 FORDHAM L. REV. 2909, 2918 (2011) (footnotes omitted).

[22] *Id.*

[23] *Id.*

[24] DELOITTE GLOBAL SERVS. LTD., DELOITTE'S STATE OF THE MEDIA DEMOCRACY SURVEY 3 (2010), *available at* http://www.deloitte.com/assets/Dcom-Global/Local%20Assets/Documents/State%20of%20Media%20Democracy%20Survey_4th_Edition.pdf.

[25] Hulu's CEO Jason Kilar points to three ways online distribution will change consumption of television. First, "consumers are increasingly moving to on-demand viewing, in part because of the lighter ad load." Jason Kilar, *Stewart, Colbert, and Hulu's Thoughts About the Future of TV*, HULU BLOG (Feb. 2, 2011), http://blog.hulu.com/2011/02/02/stewart-colbert-and-hulus-thoughts-about-the-future-of-tv/. Second, "[c]onsumers want TV to be more convenient for them." *Id.* Third, consumers control content because social media tools allow consumers "to immediately tank a bad series." *Id.* Thus, with the ability to control the advertisements, convenience, and content of their television, consumers will increasingly trend towards digital distribution. *Id.*

[26] Marguerite Rigoglioso, *What's Up, Doc? Terry Semel on the Future of Media*, STAN. GRADUATE SCH. BUSINESS (Feb. 12, 2010), http://www.gsb.stanford.edu/news/headlines/semel_media_conf.html.

sell-through ("EST").[27] Ad-supported content, such as the service provided by Hulu, offers customers free viewing of content in exchange for a mere minute or two of advertisements throughout the program.[28] Unlimited streaming subscriptions, such as the service provided by Netflix, offer consumers unlimited, commercial-free viewing of a range of shows for a monthly fee.[29] Finally, EST offers a pay-per-view type service where consumers can purchase or rent television programs and movies for a fee paid for the content on a "show-by-show" basis.

These methods of revenue generation altered the dynamics of the television industry and have made it more difficult for production and distribution companies to survive unilaterally. Where former bundling options offered opportunities for new content to be consumed and new habits based around this consumption to develop, modern forms of distribution favor viewing the "tried-and-true" programming or programming that is heavily advertised.[30] Because of this change, television production companies are less incentivized to generate risky content because the likelihood of the content being viewed diminishes when consumers are not exposed to the content through bundled packages. Thus, television production companies have been forced to find new ways to generate revenue to create risky products, or have been forced to generate cliché television programs, the success of which—in terms of revenue and viewership—is dubious.[31] Without a stable source of revenue, television production companies must turn to their single steady source of revenue: their distributors. On the other side of the coin, cable distribution companies are no longer able to rely on new programming to encourage consumers to continue purchasing premium packages, unless they invest heavily in advertising for new shows.[32] Moreover, cable companies have seen reductions in their subscriber base, resulting in less revenue and diminished ability to invest in the infrastructure required to provide cable services.[33] Thus, companies on both ends have been forced to alter their business structure to accommodate these reductions in revenue to ensure their future viability.[34] A form of restructuring, used by large cable service providers, is through the integration of cable service providers with television production studios. Past examples of this will be discussed in the following paragraphs, along with the regulatory actions the government has taken to avoid diminution of consumer welfare.[35]

B. Past Regulatory Actions

Before examining the instances of regulatory actions in the recent history of ISP and television production integration, it is important to note that the goal of

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[27] Annual Assessment of the Status of Competition in the Mkt. for the Delivery of Video Programming, 27 FCC Rcd. 8610, 8739 (2012) [hereinafer Annual Assessment 2012].

[28] *See* HULU, http://www.hulu.com (last visited Sept. 25, 2012).

[29] *See* NETFLIX, http://www.netflix.com (last visited Sept. 25, 2012).

[30] Annual Assessment 2012, at 8695.

[31] *Id.* at 8765–66.

[32] *See generally id.* at 8769.

[33] *Id.* at 8756. "According to one estimate, 13 percent of consumers with a broadband connection 'cord-shaved' in the past year." *Id.* at 8670.

[34] *See generally id* at 8723.

[35] *See infra* Part II.B.

competition policy is to promote economic welfare, and at times, competition restrictions may not be detrimental to that goal.[36] However, the scope of this goal is limited, and competition regulation only "applies to special sectors, whose structure is such that one would not expect competitive forces to operate without problems."[37] For example, where natural monopoly exists due to high fixed costs or where markets are transitioning from legally operated monopolies to liberalized markets.[38] Because of the nature of the television distribution market, the government is highly involved in the regulation of competition.[39] Government regulation pervades the television distribution market because these markets cannot function properly due to their high fixed costs[40] and because of the unique nature of the industry.

The following sections look at recent regulation of these markets because the nature of the market implies that it will always be heavily regulated and monitored by the government, and it is essential to those who study these markets to understand the interplay between regulation and market function. Additionally, in examining the historical examples of this regulation, the question which has arisen is whether or not regulatory action was essential to maintaining consumer welfare, given the disbandment of two approved mergers.

Beginning in 2000, with the merger of America Online ("AOL") and Time Warner, Inc. ("Time Warner"), the FCC and Federal Trade Commission ("FTC") have shown great interest in regulating mergers between ISPs and television content providers.[41] The AOL/Time Warner merger was granted with conditions, as was the Hughes Electronics Corporation/News Corporation transaction.[42] The most recent joint venture between NBCUniversal/Comcast was also granted with conditions.[43] Since the approvals of the AOL/Time Warner and the Hughes Electronics Corporation /News Corporation mergers, transactions have essentially become undone.[44] Similarly, AOL and Time Warner have split, and News Corporation sold off its holding in DirecTV, PanAmSat, and Hughes Network System.[45]

i. Time Warner and America Online

On December 14, 2000, the FTC accepted a proposed consent order for the merger of AOL and Time Warner.[46] This constituted a merger of the largest ISP and a large national cable provider.[47] Time Warner also brought a variety of

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[36] MASSIMO MOTTA, COMPETITION POLICY: THEORY AND PRACTICE xvii (2004).

[37] *Id.* at xviii.

[38] *Id.*

[39] *See* McCoy, *supra* note 9, at 32.

[40] *See* Annual Assessment 2012, *supra* note 27, at 8644.

[41] *See infra* Part II.B.i

[42] *See infra* Part II.B.ii.

[43] *See infra* Part II.B.iii.

[44] *See infra* Part II.B.

[45] *See infra* Part II.B.

[46] *FTC Approves AOL/Time Warner Merger with Conditions*, FTC (Dec. 14, 2000), http://www.ftc.gov/opa/2000/12/aol.shtm.

[47] *Id.*

Internet content, music, publishing, video programming, and films to the table.[48] Regulators were concerned that permitting the AOL/Time Warner merger would allow the two companies to bar access to broadband technology and foreclose diversity, freedom, and openness in the Internet market.[49] The proposed order prohibited AOL and Time Warner from interfering with other ISPs, discriminating based on content, exclusive dealing with ISPs, variable pricing for DSL in areas with and without broadband, and creating deals that would limit the ability of other cable systems to enter into alternative ISP arrangements.[50]

Separately, the FCC unanimously approved the AOL/Time Warner merger on January 11, 2001.[51] The conditions imposed upon the companies mandated that Time Warner must: (1) provide nondiscriminatory access to all ISPs using AOL's high speed cable infrastructure in order to provide residential high speed Internet, regardless of the provider's affiliation with AOL; (2) not offer video streaming applications as part of its Instant Messaging services until it could provide server-to-server interoperability, or until that interoperability was not necessary; (3) not enter into an agreement that would grant AOL affiliates exclusive access or preferential access to AT&T cable systems; and (4) notify the FCC's Cable Services Bureau and International Bureau if AOL increased its ownership in Hughes Electronics Corporation and/or General Motors Corporation.[52]

Despite the effort undertaken to secure the AOL/Time Warner merger, on May 28, 2009, AOL/Time Warner announced that AOL would be separated from Time Warner.[53] Time Warner stated that the separation would occur because Time Warner sought to focus on branding, bundling, and distributing its content; and separating would give the companies greater strategic and operational flexibility to accomplish this.[54] Thus, despite the agencies' regulation of the industry, the potential that consumers would be harmed by the companies' vertical integration was seemingly minimal, given the nature of the market and how quickly any approved mergers seem to fall apart. The over diversification of the companies seemed to cast a riff between AOL and Time Warner, and did not allow them to capture an unfair advantage in the market. This raises the question of whether the regulation truly was necessary, given the fact that the integrated companies reversed their own merger when the venture did not seem to meet their company's needs. However, it seems that this question was not raised by AOL, Time Warner, or regulatory agencies given that the merger, approval, and disbandment of AOL/Time Warner was followed by a similar integration of Hughes Electronics Corporation and News Corporation.

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48 *Id.*

49 *Id.*

50 Ilene K. Gotts & Joseph G. Krauss, *Divestiture Policy for New Economy Transactions*, 15 ANTITRUST, Spring 2001, at 64, 64 (2001).

51 *Id.* at 65.

52 *Id.*

53 *Time Warner Inc.-AOL Separation Information*, TIME WARNER, http://ir.timewarner.com/phoenix.zhtml?c=70972&p=irol-aolseparation (last visited Feb. 22, 2012).

54 *Time Warner Inc. Announces Plan to Separate AOL*, TIME WARNER, http://ir.timewarner.com/phoenix.zhtml?c=70972&p=irol-aolseparation (last visited Feb. 22, 2012).

ii. Hughes Electronics Corporation and News Corporation

The FTC approved News Corporation's acquisition of thirty-four percent of Hughes Electronics Corporation on January 14, 2004.[55] The acquisition included the transfer of control over various authorizations and licenses granted by the Commission "including direct broadcast satellite and fixed satellite space station, earth station, and terrestrial wireless authorizations."[56] This merger was of interest to the FCC because Hughes Electronics Corporation held a cable provider (DirecTV), a satellite operator (PanAmSat), and a broadband satellite network provider (Hughes Network Systems); and, once the acquisition was made, News Corporation would have a de facto controlling interest over Hughes Electronics Corporation.[57] News Corporation's larger share in Fox Entertainment Group allowed the company to enter the cable market.[58]

The FCC conditioned its approval of the acquisition on: (1) News Corporation's commitment to make its programming available to all distributors without exclusivity or discrimination; (2) approval of the transaction by a majority of General Motors' shareholders; and (3) clearance by the FCC and the Internal Revenue Service.[59] News Corporation transferred its interest in DirecTV to Liberty Media Corporation in 2008.[60] Followed by a sale of PanAmSat and Hughes Network in 2004—with the exception of two satellites, which had been used by DirecTV—News Corporation divested most of its holdings in the cable service provider.[61] Despite the claimed benefits, including, "increasing the availability of local-into-local broadcast television service into as many markets as possible" and "enhancing Hughes' ability to undertake significant risks and costs of developing and deploying new products and services," the expected market gains due to the merger were not realized, and the acquisition eventually unraveled.[62] This again raised the question of whether regulation was unnecessary because the heavily regulated market did not permit additional gains, despite the anticipated market dominance due to the merger of producers and distributors.

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[55] Gen. Motors Corp., 19 FCC Rcd. 473, 476 (2004).

[56] *Id.*

[57] *News Corporation Agrees To Acquire 34% Of Hughes Electronics For $6.6 Billion In Cash And Stock*, NEWS CORP. (Apr. 9, 2003), http://www.newscorp.com/news/news_188.html. Of additional concern, News Corp. would transfer its ownership to Fox Entertainment Group, Inc. ("FEG") in exchange for 74.2 million shares in FEG. *Id.* Since News Corp. held 80.6% of FEG at the time, the acquisition would increase News Corp.'s holdings in FEG to 82%. *Id.* Where FEG is the holding location of News Corp's programming interests, not only would this merger increase the ability of the company to enter into the distribution market, but it would also give the company the opportunity to expand its holdings in television production. *Id.*

[58] *Id.*

[59] *Id.*

[60] Gen. Motors Corp., 24 FCC Rcd. 8674, 8674 (2009).

[61] *DirecTV Agrees to Sale of PanAmSat Unit*, L.A. TIMES (Apr. 21, 2004), http://articles.latimes.com/2004/apr/21/business/fi-panamsat21; Steven Pearlstein, *...And Another Thing*, WASH. POST, Dec. 8, 2004, at E01, *available at* http://www.washingtonpost.com/wp-dyn/articles/A45648-2004Dec7.html.

[62] FCC, GENERAL MOTORS CORPORATION, HUGHES ELECTRONICS CORPORATION, AND THE NEWS CORPORATION LIMITED SEEK APPROVAL TO TRANSFER CONTROL OF FCC AUTHORIZATIONS AND LICENSES HELD BY HUGHES ELECTRONICS CORPORATION TO THE NEWS CORPORATION LIMITED, 3 (May 16, 2003), *available at* http://hraunfoss.fcc.gov/edocs_public/attachmatch/DA-03-1725A1.pdf.

Whether the agencies' actions are necessary has again arisen, this time in the context of the joint venture between NBCUniversal and Comcast.

iii. NBCUniversal and Comcast

The third transaction to catch the attention of regulatory agencies was the NBCUniversal/Comcast joint venture, which was approved on February 20, 2011.[63] NBCUniversal/Comcast agreed to several conditions upon which the commissions permitted Comcast to control NBC Television Network and NBC Universal's video programming and cable networks.[64] The imposed conditions included: (1) ensuring that Multichannel Distributors had reasonable access to NBCUniversal/Comcast programming; (2) protecting online competition development; (3) granting access to Comcast's systems for distribution; and (4) guarding localism, diversity, and other public interest concerns.[65] As described by the FCC, "[t]his transaction would effectuate an unprecedented aggregation of video programming content with control over the means by which video programming is distributed to American viewers offline and, increasingly, online as well."[66] The joint venture consisted of a restructure of the two entities. This included acquisition of the twenty percent of NBCUniversal held by Vivendi S.A., contribution by NBCUniversal and Comcast of RSNs, programming networks, and Internet businesses, but not Comcast's cable systems. By the end of the transaction, Comcast would own fifty-one percent of the joint venture, with the option for General Electric to require the joint venture or Comcast to acquire General Electric's entire interest.[67] The arrangement does not permit transfers of ownership for another three and a half years, so any movements to divest the joint venture will not be seen for several years to come.[68]

By ensuring that "Comcast shall not prioritize Defendants' Video Programming or other content over other Persons Video Programming," in its management and operation of Comcast's Internet facilities, the FCC imposed

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[63] *See generally* United States v. Comcast Corp., U.S. DEP'T OF JUSTICE, http://www.justice.gov/atr/cases/comcast.html (last visited Sept. 28, 2012). Of the five-member review panel, four approved the merger; one of those members was Meredith Attwell Baker, who announced that she would leave the FCC when her term expired to join Comcast's Washington lobbying office. Edward Wyatt, *F.C.C. Commissioner Leaving to Join Comcast*, N.Y. TIMES (May 11, 2011, 4:00 PM), http://mediadecoder.blogs.nytimes.com/2011/05/11/f-c-c-commissioner-to-join-comcast/.
Commentary on the impropriety of this move a mere four months following the merger cast doubt on the decision made by the commission. *Id.*

> There's something particularly unsettling about a regulatory official who voted only four months ago to approve the $13.75 billion merger of Comcast and NBCUniversal turning around to take a high-profile job with that firm . . . . [T]he move threatens to further undermine public confidence in the government's ability to make objective decisions that put ordinary citizens' interests first.

Inquirer Editorial: Switching Sides, PHILLY.COM (May 14, 2011), http://www.philly.com/philly/opinion/121823389.html.

[64] U.S. DEP'T OF JUSTICE, *supra* note 63.

[65] Press Release, FCC, FCC Grants Approval of Comcast-NBCU Transaction, (Jan. 18, 2011), *available at* http://www.comcast.com/nbcutransaction/pdfs/FCC%20Press%20Release%201.18.11.pdf.

[66] Comcast, *supra* note 2, at 4240.

[67] *Id.* at 4245.

[68] *Id.*

restrictions that would guard against the potential vertical integration antitrust issues that could have caused the most damage to the industry.[69] Addressing in its analysis the likely direction of the market following the authorization of the joint venture, the DOJ and the FCC included essential safeguards against the harms most likely to affect the market.[70] However, the remainder of this paper will focus on whether those limitations were sufficient to guard against future anticompetitive actions or if regulation of vertical mergers of ISPs and television production companies should be stricter or more lenient. The following section will focus on the concept of vertical integration and its treatment in law and economics.

C. Regulation of Vertical Integration

The three different types of transactions can be used to accomplish horizontal or vertical integration: mergers, acquisitions, and joint ventures.[71] However, as mentioned previously, not all transactions are anticompetitive, and mergers and acquisitions are only barred when they lessen competition in a particular market under Section 7 of the Clayton Act; joint ventures are typically scrutinized under Section 7 as well.[72] Despite past schools of thought, vertical integration cannot be considered per se illegal, nor can it be considered per se legal.[73] While vertical integration has the potential to lead to efficiencies that enhance consumer welfare, they also have the potential to cause anti-competitive effects; whether a particular integration enhances or lessens consumer welfare depends on which effect dominates.[74] Currently, regulatory agencies look to the "rule of reason" analysis, which examines the complete effects of integration on competition and examines whether the integration will compromise unilateral decision making, aggregate power or financial interests, or impede competition by easing the ability of companies to collude.[75]

The remainder of the paper—following a brief introduction to vertical integration—will focus on describing these harms and benefits, and the prudence of permitting or barring vertical integration within the digital distribution market. However, an important factor to note, before examining vertical integration, is how past regulatory actions have affected similar industries, including the motion picture industry. Important precedents in vertical integration have provided the foundation for why regulatory agencies vigorously pursue such actions. And, in understanding past actions, there is the potential to understand that regulation is not merely a function of economic understanding, but a historical fear of monopolization and a resulting interference with markets that may not prove particularly beneficial. This historical perspective is important to keep in mind

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[69] United States v. Comcast Corp., No. 1:11–CV–00106, 2011 WL 5402137, at *12 (D.D.C. Sept. 1, 2011).

[70] Comcast, *supra* note 2, at 4239–43.

[71] *See generally* Piraino, *supra* note 8, at 30.

[72] Katherine L. Race, *The Future of Digital Movie Distribution on the Internet Antitrust Concerns with the Movielink and Movies.com Proposals*, 29 RUTGERS COMPUTER & TECH. L.J. 89, 104 (2003).

[73] *See generally* Piraino, *supra* note 8, at 31.

[74] *Id.* at 204.

[75] *Id.*

when agencies regulate modern vertical transactions and may provide a mitigating bite to regulation of these potentially beneficial ventures in the future.

D. Historical Precedent of Vertical Integration in Motion Pictures

Vertical integration in the television industry means that a company creates programs in-house, it airs them on their own networks, and the company has the right to resell licenses and rights to the content on their own networks.[76] Antitrust regulation typically focuses on horizontal mergers because of their resulting concentration of markets; however, vertical integration can constitute a monopoly when certain preconditions are satisfied.[77]

The fear of permitting a company to control all three aspects of an industry is that the company will either foreclose other businesses, thus limiting the diversity and competition in the market, or the company will use its leverage in one aspect of the market to reduce competition further downstream.[78] Despite the potential for reductions of diversity, several efficiency gains can be achieved from permitting vertical integration, including the elimination of double marginalization,[79] transaction costs, and strategic behavior that negatively impacts consumers.[80] Since research into vertical integration has increased, the examination of vertical integration has turned more towards a cost-benefit analysis because "[a]s our understanding of vertical control improved, it became clear that much of the policy toward it, including vertical mergers, was based simply on an assumption that, like witchcraft, what we did not understand must be bad."[81] The unique characteristics of the entertainment industry have enticed many companies to vertically integrate in order to maximize revenues and profits by reducing the negative costs associated with double marginalization, transaction costs, and strategic behaviors.[82]

The most prominent example of this was the attempted ownership of movie theatres by motion picture production companies.[83] These vertical integrations were immediately struck down by the DOJ.[84] As part of the Paramount Cases, the United States Supreme Court ruled that "vertical integrations were 'a definite

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76 Marc Simon, *Vertical Integration and Self-Dealing in the Television Industry: Should Profit Participants Be Owed A Fiduciary Duty?*, 19 CARDOZO ARTS & ENT. L.J. 433, 434 (2001).

77 Richard M. Steuer, *The Simplicity of Antitrust Law*, 14 U. PA. J. BUS. L. 543, 547 (2012). Vertical restraints are unlikely to offend the antitrust laws when there is no market power being exerted and the restraint was initiated unilaterally by the seller. *Id.*

78 *Id.* at 435.

79 Double marginalization is "the markup on the markup." Steven C. Sunshine, Deputy Assistant Attorney General, Antitrust Div. U.S. Dep't of Justice, Address before the American Bar Association Section of Antitrust Law Spring Meeting: Vertical Merger Enforcement Policy (Apr. 5, 1995), *available at* http://www.justice.gov/atr/public/speeches/2215.pdf; *see infra* text accompanying note 119.

80 *Id.*

81 Frederick R. Warren-Boulton, *The Contribution of the Merger Guidelines to the Analysis of Non-Horizontal Mergers*, U.S. DEP'T OF JUSTICE, http://www.justice.gov/atr/hmerger/11709.htm (last visited Oct. 1, 2012).

82 *Id.*

83 United States v. Paramount Pictures, Inc., 334 U.S. 131 (1948).

84 Kraig G. Fox, *Paramount Revisited: The Resurgence of Vertical Integration in the Motion Picture Industry*, 21 HOFSTRA L. REV. 505, 515 (1992).

means of carrying out the restraints and conspiracies' that were found to be illegal and in restraint of trade."[85] The court also forced all theatres that did not join in the consent decrees to divorce their holdings in movie theatres.[86]

The decrees have gradually been eliminated, and between 1985 and 1988, over one billion dollars were spent purchasing independent movie theatres.[87] However, residuals remain in the entertainment industry because the companies that participated in consent decrees were able to maintain their holdings in movie theatres and were able to capture a majority share of the market.[88]

Because of these past examples of the effect of regulation on markets, as compared to the recent allowance of mergers between ISPs and television production companies,[89] the question presented here is whether the DOJ should keep the industry at an arms distance, to allow companies to merge as they please and keep time with changing technologies, or if television production companies should be limited to the extent motion picture production companies were in the 1940s. The drawback is the potential of the creation of state endorsed monopolies because of the restriction of particular companies from integration.[90] While the potential benefits include leveling the playing field so that other companies can compete in the market without an unfair advantage to established distributors.

As previously mentioned, regulatory agencies use a cost-benefit analysis to determine whether to permit vertical integration and consider varying factors, depending on the industry. This is because not all vertical integration is necessarily bad. The following paragraphs will look to the reasons why regulatory agencies will scrutinize vertical integration, and based on these factors, will analyze the market effect of permitting NBCUniversal/Comcast's joint venture. Furthermore, they will examine whether the agencies should be able to dictate the future of markets, and potentially dictate market leaders simply through regulation of potential competition suppressors—as was the case following the Paramount Decrees.

III. COSTS AND BENEFITS OF VERTICAL INTEGRATION

When companies merge, regardless of whether it is a horizontal or vertical merger, there will inevitably be benefits and costs to the industries and consumers affected by the mergers. Vertical integration can give organizations greater control over, and access to, inputs when they come into ownership of upstream producers, yet these acquisitions are also costly and result in companies that are less

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[85] *Id.*

[86] *Id.*

[87] *Id.* at 529.

[88] *Id.* at 530.

[89] *See supra* Part II.B.

[90] *See* Barry J. Brett, *A Fresh Look at the Paramount Decrees*, ENT. & SPORTS LAW, Fall 1991, at 1, 4. These drawbacks are similar to those that resulted from the Paramount Decrees, including the diminution of the Paramount defendants from their positions as market leaders into smaller market powers where "the Paramount defendants account for only 25-to-30 percent of the features released in 1990," following "the breakdown of the studio system and increases in independently produced films and foreign releases." *Id.*

specialized.[91] Five advantages that have been either generally accepted, or were set forth in the NBCUniversal/Comcast merger, include: (1) more investment in risky endeavors and product diversification, (2) price deflation, (3) reductions in transaction costs, (4) benefits from content aggregation, and (5) economies of scale and scope. Yet, the television industry could be harmed because of decreases in competition as a result of heightened barriers to entry and exclusion, which could harm the diversity, quality, and price of content.

A. Benefits of Vertical Integration in the Television Industry

i. Ability to Pursue Risky Ventures

Television production companies and ISPs have large upfront costs.[92] Unless those costs can be recovered, investments in new products cannot be made without seeking external sources of funding.[93] Permitting these two types of companies to merge allows for investment in more risky endeavors.[94] For example, the NBC/Comcast merger would provide an additional 1,500 on-demand offerings to children.[95] In addition, the merger would provide six additional rural communities with broadband Internet access and 600 new institutions—including low-income areas, schools, and libraries—with free high-speed Internet service.[96] Despite the large initial costs in both industries, the structure of the costs in each industry is different.[97] Television production studios have large initial variable costs while ISPs have large initial fixed costs.[98] Thus, investments are not

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[91] *Vertical Integration*, ECONOMIST (Mar. 30, 2009), http://www.economist.com/node/13396061.

[92] Christopher S. Yoo, *Vertical Integration and Media Regulation in the New Economy*, 19 YALE J. ON REG. 171, 262 (2002).

[93] *Id.*

[94] *Id.*

[95] Comcast, *supra* note 2, at 4243.

[96] *Id.* at 4242.

[97] Daniel L. Rubinfeld & Hal J. Singer, *Open Access to Broadband Networks: A Case Study of the AOL/Time Warner Merger*, 16 BERKELEY TECH. L.J. 631, 643–44 (2001). "For example, most of the production costs of broadband Internet content, like cable television content, are upfront costs, while the marginal costs (for example, the costs of distribution) are negligible." *Id.* at 643.

[98] Jonathan A. Knee, *Why Content Isn't King*, THE ATLANTIC (July 2011), http://www.theatlantic.com/magazine/archive/2011/07/why-content-isnt-king/308551/. The infrastructure of the Internet, including the materials used to build the lines, the laborers involved in the construction, is a fixed cost requiring minimal additional costs to provide a home with Internet access. Nate Anderson, *Should Broadband Data Hogs Pay More? ISP Economics Say "No"*, ARS TECHNICA, http://arstechnica.com/tech-policy/news/2010/07/should-broadband-data-hogs-pay-more-isp-economics-say-no.ars (last visited Feb. 23, 2012). In an article discussing the marginal costs and whether there is an additional cost of providing one more unit of output associated with high data downloads through broadband, one reporter found virtually inconclusive results:

> I tried to explore the marginal costs with Mr. Hobbs. When someone decides to spend a day doing nothing but downloading every Jerry Lewis movie from BitTorrent, Time Warner doesn't have to write a bigger check to anyone. Rather, as best as I can figure it, the costs are all about building the network equipment and buying long-haul bandwidth for peak capacity.
>
> If that is true, the question of what is "fair" is somewhat more abstract than just saying someone who uses more should pay more. After all, people who watch more hours of cable television don't pay more than those who don't.
>
> Mr. Hobbs declined to react to my hypothesis about how costs are almost all

typically made in creating risky television content because, regardless of the size of the production studio, creating new content relies on variable costs, which cannot be recovered without generating revenue beyond what is required to cover fixed costs.[99]

When variable costs fluctuate, total costs—the combination of variable and fixed costs—fluctuate.[100] Profit is the total revenue minus total costs; thus, the companies with the highest profit will maximize the difference between total revenue and total costs.[101] The difference between the revenue generated by studios is in the number or popularity of films.[102] Thus, to increase their profits, studios must increase their revenues by producing content of a higher quantity and quality; or, they must decrease their costs. Studios' variable costs are based on the quality or the quantity of the content.[103] And, despite the monetary value of the film, the consumer judges the quality of content.[104] Because consumers' enjoyment of content is unpredictable, studios must produce large libraries of films in hopes of attracting new viewers and higher revenues.[105] This expensive process

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> fixed costs. He did invite me to meet with an engineer to go over the details, an offer I want to take him up on.

Saul Hansell, *Time Warner Cable Profits Will Grow With Broadband Caps*, N.Y. TIMES, (Apr. 8, 2009, 5:52 PM), http://bits.blogs.nytimes.com/2009/04/08/time-warner-cable-profits-on-broadband-are-great-and-will-grow-because-of-caps/. Meanwhile, in the motion picture industry, although producing one additional copy of a movie has virtually no cost, viewing the product of the motion picture industry as an individual film, instead of an individual copy of a film, reveals that the variable cost per product produced consists of the Development Cost, the Pre-Production Cost, the Production Cost, and the Post-Production Cost. *Econ 150 Economic principles and Problems – Micro*, BYU IDAHO, http://courses.byui.edu/ECON_150/ECON_150_Presentations/Lesson_06.htm; Castor (last visited Feb. 23, 2012); *The Cost of Making a Hollywood Movie*, ANOMALOUS MATERIAL (Mar. 26, 2010 5:30 PM) http://www.anomalousmaterial.com/movies/2010/03/the-cost-of-making-a-hollywood-movie/. The production costs for these expenses can range from a few thousand dollars to $20 million, for movies like Spider Man 2; and can even reach $240 million, for movies like Avatar. *Id.* While the average cost of producing and marketing a movie was $106.6 million in 2007, the MPAA stopped releasing these figures in 2009, so more recent and accurate data could reveal that costs are even higher now. Richard Verrier, *MPAA stops disclosing average costs of making and marketing movies*, L.A. TIMES (Apr. 1, 2009), http://articles.latimes.com/2009/apr/01/business/fi-cotown-mpaa1.

[99] *See*, *e.g.*, Knee, *supra* note 98. Fixed costs do not change with the level of a company's production, which must be paid regardless of whether any products are being sold. *Fixed Cost*, INVESTOPEDIA, http://www.investopedia.com/terms/f/fixedcost.asp#axzz1mYUMdYSF (last visited Oct. 2, 2012). However, variable costs do vary with output and can include production inputs, where costs will increase with increased production or decrease with decreased production. *Variable Cost*, INVESTOPEDIA, http://www.investopedia.com/terms/v/variablecost.asp#axzz1mYUMdYSF (last visited Oct. 2, 2012). In the apple pie example, fixed costs are the cost of the machines, the rent for the factory, the electricity for the grocery store, etc. Alternatively, the variable costs are the cost of apples since producing more pies requires more apples, the cost of apple pie tins, for the same reason, and wages for the laborers.

[100] Valentino Piana, *Firm-Specific Fixed and Variable Costs: A Model of Market Dynamics*, ECON. WEB INST. (2006), http://www.economicswebinstitute.org/essays/fixedvar.htm.

[101] Valentino Piana, *Costs*, ECON. WEB INST. (2003), http://www.economicswebinstitute.org/glossary/costs.htm#tota.

[102] *See HBO and the Future of Pay-TV*, ECONOMIST (Aug. 20, 2011), http://www.economist.com/node/21526314.

[103] *See generally id.*

[104] *See*, *e.g.*, Knee, *supra* note 98.

[105] *See Time Warner Earnings Rise 22%, Helped by HBO*, L.A. TIMES (Feb. 2, 2011), http://articles.latimes.com/2011/feb/02/business/la-fi-0203-time-warner-earns-20110202. However, it has been noted that in the motion picture industry, production costs have a high correlation to gross box office revenues. Liran Einav & Barak Y. Orbach, *Uniform Prices for Differentiated Goods: The Case*

of creating voluminous libraries of risky content causes large variable costs, which can be covered by revenue in the form of increasing advertising, increasing the number of viewers, or increasing the prices paid by viewers.[106] In an industry where the prices that consumers pay are fairly uniform, it is likely that there will not be any reductions in the prices consumers pay.[107] But the industry can produce more content to attempt to increase their revenues. "In general, satellite entry induces improvements to cable quality to a greater extent, proportionally, than it promotes lower cable prices."[108] Thus, to bolster profitability, television production studios can either produce larger libraries with more diverse content to attract viewers, or they can increase advertisements.[109] The remaining issue is how to fund the production of larger libraries. This issue results because "there is little additional cost [for digital distribution], . . . this situation is not about profit

of the Movie-Theatre Industry, 27 INT'L REV. L. & ECON. 129 (2007). Additionally, sequels perform similarly to their originals, and a movie's success can typically be revealed after its first weekend. *Id.* at 135. And although it is difficult to estimate demand for films because of the persistence of uniform prices in the industry, it has been argued that variations in total demand can reflect the elasticity of prices. *Id.* at 134. The number of weekend moviegoers exceeds the number of weekday moviegoers 3.5 to 1. *Id.* at 135. Which indicates that moviegoers on the weekend could have a higher elasticity in their demand for films. *Id.* The same can be said for moviegoers during the summer and during holidays. *Id.* While distribution in motion theatres is a unique product relative to viewing films on a television screen at home, "if viable substitutes exist for a good or service, and they exist at a cheaper price than the original, then consumers will demand more of the new good or service and less of the original." Kevin J. Corbett, *The Big Picture: Theatrical Moviegoing, Digital Television, and beyond the Substitution Effect*, 40 CINEMA JOURNAL 17, 29 (Winter 2001) *available at* http://www.jstor.org/stable/1225841 (quoting DOUGLAS GOMERY, SHARED PLEASURES: A HISTORY OF MOVIE PRESENTATION IN THE UNITED STATES 84 (1992)). Modernly, a consumer can purchase twenty-four hour access to HBO films for an entire month for $16.00, but he could only purchase access to one film for an average ticket price of $7.93 in 2011. Richard Verrier, *Average Movie-Ticket Price Edges Up to a Record $7.93 for 2011*, L.A. TIMES (Feb. 9, 2012, 1:04 PM), http://latimesblogs.latimes.com/entertainmentnewsbuzz/ 2012/02/average-movie-ticket-price-2011.html; *Premium Channels*, DISH NETWORK LLC, http://www.dish.com/entertainment/channels/ (last visited Oct. 2, 2012). In volatile markets, such as the market in 2011, where an increase in oil price forced consumers to decrease spending on discretionary items because discretionary income is not increasing, and consumers were forced to substitute more expensive necessities for reductions in discretionary spending, consumers could be forced to forego an expensive and enjoyable night out for a quieter and cheaper night in. Ben Casselman & Conor Dougherty, *Oil Rise Imperils Budding Recovery*, WALL ST. J. (Feb. 16, 2012), http://online.wsj.com/article/SB10001424052970204792404577224932060341956.html; *see* James Rankin & Kyle Brown, *Personal Income and Outlays, December 2011*, U.S. DEP'T COMM. BUREAU ECON. ANALYSIS (Jan. 30, 2012, 8:30 AM), http://www.bea.gov/newsreleases/national/ pi/2012/pi1211.htm. Thus the trends seen in consumption of movies could be seen in television, and prices could be seen as equally correlated with the price of the production of television shows. And where products are substitutes, times where consumers would be interested in consuming a particular item would likely be times that could now be filled with the substitute, for example, choosing to watch a film at home with the family over the holidays instead of watching a film in the movie theatre.

[106] *See, e.g.*, *Time Warner Earnings Rise 22%*, *supra* note 83.

[107] Chenghuan Sean Chu, *The Effect of Satellite Entry on Cable Television Prices and Product Quality*, 41 RAND J. OF ECON. 730, (2010).

[108] *Id.* at 763.

[109] *See* Stuart Elliott, *Study Measures Ad Industry's Impact on State Economies*, N.Y. TIMES, Apr. 14, 2011, at B3, *available at* http://www.nytimes.com/2011/04/14/business/media/14adco.html? emc=eta1. Since increasing advertisements is a foregone conclusion because of the immense success of using advertisements, it is assumed that regardless of the means of distribution, advertisements would remain constant across industries because for each show there is only the time frame of the movie during which advertisements can be shown, and this will reach its maximization point where the film becomes just an advertisement instead of a motion picture.

maximization, but simply revenue optimization."[110] Unlike the market as it existed prior to the emergence of OVDs, most companies have access to digital distributors through Apple, Amazon, Hulu, and other various online content aggregators.[111] The availability of digital distribution through various online content aggregators could provide a potential mechanism for wider distribution for vertically integrated companies due to the ease with which individuals can contract with these OVDs. However, these companies cannot garner additional revenue simply because they have access to digital distribution, because these new middlemen provide access to all companies, not just the integrated companies, and no competitive benefit is provided to the companies that control internet access.[112] Thus, the benefits to vertically integrated companies that provide Internet services does not come through digital distribution, but instead, additional revenue to increase their television production can come through Internet subscriptions. One form of increasing revenue that is unique to the Internet service provider industry, a benefit that cannot be tapped by television producers, is the ability to receive government grants to expand their networks, as will be discussed below.

At the time the Connect America Fund was enacted—an act providing funding to expand accessibility to high-speed Internet—eighteen million Americans lived in underserved areas with limited or no access to high-speed Internet.[113] To spur development in these areas, the government awarded more than $7 billion in grants, loans, and initiatives to private companies to improve broadband access in rural areas.[114] It was estimated that $24 billion is required to provide service to all underserved Americans.[115]

These grants have dual benefits for integrated companies. Where grants and initiatives are provided to companies that seek to expand in rural areas, the fixed costs for integrated companies can be reduced, and when companies are able to gain subscribers they did not access originally, they can expand their subscriber base and their revenues.[116] Despite the reduced prices that companies offered for

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110 Joern Meissner, *The Price of the Digital Revolution*, MEISSNER RESEARCH GROUP (Feb. 24, 2010), http://www.meiss.com/blog/tag/elasticity/.

111 Paul Bond, *Film Industry, Led by Electronic Delivery, Will Grow in Every Category Through 2015: Report (Exclusive)*, HOLLYWOOD REP. (June 14, 2011, 12:01 AM), http://www.hollywood reporter.com/news/film-industry-led-by-electronic-200881.

112 *Id.*

113 FCC, *Connecting America*, FCC ENCYCLOPEDIA, http://www.fcc.gov/encyclopedia/connecting-america (last visited Feb. 23, 2012). For a graphic depiction of the availability of wire line broadband across America, see FCC, *Broadband Availability*, MAPBOX, http://tiles.mapbox.com/fcc/map/ Unavail_20111007_2 (last visited Feb. 23, 2012).

114 *In re* Inquiry Concerning the Deployment of Advanced Telecommunications Capability to All Americans in A Reasonable and Timely Fashion, and Possible Steps to Accelerate Such Deployment Pursuant to Section 706 of the Telecommunications Act of 1996, As Amended by the Broadband Data Improvement Act, 26 FCC Rcd. 11800, 11810 (2011).

115 In re Inquiry Concerning the Deployment of Advanced Telecommunications Capability to All Americans in A Reasonable & Timely Fashion, & Possible Steps to Accelerate Such Deployment Pursuant to Section 706 of the Telecommunications Act of 1996, As Amended by the Broadband Data Improvement Act, 26 FCC Rcd. 8008, 8035 n.175 (2011).

116 *Id.* at 8014 n.47. "Because service providers in [areas with low population density] cannot earn enough revenue to cover the costs of deploying and operating broadband networks, including expected returns on capital, there is no business case to offer broadband services in these areas. As a result, it is unlikely that private investment alone will fill the broadband availability gap." *Id*.

rural service, the revenue gained from signing up consumers for an Internet service subscription—particularly where the government funds part of the fixed costs—can contribute to other services provided by the company.[117] This expansion of revenue is further bolstered when production studios choose to provide access to their content through the Internet, because consumers demand for Internet service increases as they alter their consumption from cable to the Internet channels through which producers provide their content.[118] Accordingly, studios that have alternative sources of income can delve into more risky investments because they have the potential to recover costs, especially when those companies are receiving government funding, as has been discussed previously in regards to the Connect America Fund. This advantage to permitting the vertical integration is bolstered by other advantages, including price deflation.

ii. Potential Price Deflation

In addition to providing a broader range of riskier services, there is a potential for price deflation because of the consolidation of costs.[119] The first potential consolidation is where "double marginalization" occurs.[120] Double marginalization refers to each member in a chain of distribution taking a profit above marginal cost.[121] For example, in the production of an apple pie, assuming that one company grows the apples, and takes a dollar profit on each box of apples, and then its distributor takes a dollar profit on each box of apples the distributor delivers, and then delivers the apples to an apple pie making company. Assuming that the apple pie making company continues the trend, and takes a dollar profit for each apple pie it sells to a grocery store and, finally, assuming that the grocery store takes a dollar profit on each pie it sells, then the consumer pays not only the price of the pie, but also four additional dollars for the profit to each company. However, if a bakery owns not only the grower, but also the distributor and the pie making company, then the bakery can take just one dollar of profit, and have the same profits it realized as an unintegrated company, but with lower costs.[122] Though this will not always be the case, it does become an option once the merger occurs, even in the television industry.

As was previously mentioned, the producers, networks, and broadcasters comprise the distribution chain of television programs.[123] In a model established by Dr. Anna P. Della Valle, it was found that the percentage taken by exhibitors

[117] *Id.* at 8043 n.236. For example, Comcast's Broadband Opportunity Program offered eligible customers $9.95 a month for Internet access service, with no modem or installation charges; in some cases, Comcast provided customers with $150 computers. *Id.*

[118] *See* Ben Fritz, *Summit Signs Pay-TV Deal with HBO, Dumping Showtime*, L.A. TIMES (May 27, 2011), http://articles.latimes.com/2011/may/27/business/la-fi-ct-summit-20110527.

[119] Comcast, *supra* note 2, at 4334. The fact that "[t]he Applicants estimate that eliminating the double marginalization on these subscribers would save [REDACTED] per year," includes a value that is redacted leads one to become quite excited about the potential savings in cable services because the applicants believed that the deal was too good to be released. *Id.*

[120] *Id.* at 4335.

[121] *Id.*

[122] *Id.*

[123] *See supra* Part III.A.ii.

and distributors had a substantial effect on the final profitability of a film.[124] For example, in motion theatre exhibition, a reduction of the retained percentage of box office receipts by an exhibitor from fifty percent to forty percent resulted in an increase in profit from twelve-and-a-half percent to thirty percent.[125] And a reduction in the percentage of gross receipts to distributors from thirty-five percent to thirty percent results in a total increase in profit to thirty-two percent.[126] In a merger, the percentages taken by each party would fall to zero, which would result in a one hundred percent profit going to the merged companies. Thus, the profit has the potential to increase by more than thirty-two percent, and provide the opportunity for companies to reduce their prices even further to increase demand for their product and maximize their profits. Where the companies merely worked in a joint venture or an acquisition, reductions in the percentage taken by each party can be realized for the benefit of the company and the consumer. The benefit to the consumer is having a product that is lower priced, which will likely be capitalized upon by a prudent consumer. The benefit to the producer is an increase in his market share because he has the opportunity to abscond with his competitor's consumers because he can offer a lower price, yet retain his original percent of profit. Thus, benefits can be realized because of the reduction in double marginalization.[127]

The initial opinion regarding NBCUniversal/Comcast did not predict any substantial savings from double marginalization.[128] However, as was the example from the vertical integration of the motion picture industry,[129] in the NBCUniversal/Comcast deal, any savings due to double marginalization will play out as the companies alter their pricing to accommodate the new market structure. Regulatory agencies are conducting an "examination—not yet a full-blown investigation—[which] is looking at how the actions of programmers and distribution companies affect competitors and, ultimately, consumers."[130] Although the review of the NBCUniversal/Comcast vertical integration did not predict any cost savings from double marginalization,[131] the results of these studies will show whether the pricing structure has been altered. If so, then there is the potential that, in order to gain a competitive advantage, the NBCUniversal/Comcast may find the ability to reduce prices due to the price flexibility that can be achieved through double marginalization, and due to lower transaction costs, which brings the analysis to the third potential cost

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124 Anna P. Della Valle, *Is Making Movies All That Different Than Making Plays? Analysis of Cost Structure in Film and Live Theatre*, FOKUS, 11 (July 6, 2006), http://www.fokus.or.at/fileadmin/fokus/user/downloads/acei_paper/Della%20Valle.doc.

125 *Id.*

126 *Id.*

127 Specifically in the NBCUniversal/Comcast merger, the companies mad a commitment that "the combined firm will no longer treat the marginal cost of the upstream product (e.g., programming) as the price the downstream firm previously paid but as the lower amount it actually costs to produce it." Comcast, *supra* note 2, at 4335.

128 United States v. Comcast Corp., No. 1:11–CV–00106, 2011 WL 5402137, at *29 (D.D.C. Sept. 1, 2011).

129 *See supra* Part II.D.

130 Joe Flint, *U.S. is Probing How Pay-TV Industry Affects Online Competitors*, L.A. TIMES (June, 13, 2012), http://articles.latimes.com/2012/jun/13/business/la-fi-ct-justice-cable-probe-20120614.

131 Comcast, *supra* note 2, at 4334.

consolidation. As was shown in the motion picture industry,[132] where companies can see increases in profit because of their control of a larger percentage of receipts, if television producers can take one hundred percent of the profit from the sale of their show on their own internet distribution method, then they will have the ability to lower prices. Where consumers have seen reductions in their disposable income since the 2008 recession,[133] there is a high probability consumers will increase their consumption of less costly programs. However, in summary, there are no expected benefits to consumers due to double marginalization, but if it turns out that companies are able to benefit consumers by reducing prices due to the changed structure of television distribution, there is the potential that there will be benefits derived from permitting the vertical integration.

iii. Consolidation of Transaction Costs

The third potential consolidation is in transaction costs.[134] Following the theme of the previous consolidation, where a bakery store does not have to deal with several vendors, he does not have to pay for contracts, nor does he have to deal with potential conflicts of interest.[135] In the television industry, this is particularly important because transaction costs for intellectual property, licensing, marketing, and advertisement are complex.[136] Because all of the transactions would occur within one company, the costs of creating these deals will reduce substantially.[137] Additionally, without conflicts, parties can move together towards the production of new products.[138] In television production, producers and networks have the option to extend or terminate a program at the end of the series.[139] While option contracts are the standard in the industry, at times programs—even profitable ones—get cancelled because renegotiations are not fruitful.[140] To guard their profitable products, networks may contract for programs that they do not intend to use—a form of bundling that has always existed in the motion picture industry.[141] These all have the potential to increase prices to consumer. There are additional transaction costs in the risk of losing programming because each transaction requires bringing both parties to the table, paying expensive lawyers to negotiate the deals and draft the contracts, and each involves an inherent risk that the parties' views are not in alignment, which will result in the cancellation of a program.[142] Particularly in licensing video content for multiple

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[132] *See supra* Part II.D.

[133] *See Monetary Policy Report to the Congress; Figure 1. Change in Real Gross Domestic Product, 2005-11*, BOARD GOVERNORS FED. RES. SYS. (February 29, 2012), http://www.federalreserve.gov/monetarypolicy/mpr_20120229_part2_accessible.htm#fig5.

[134] Comcast, *supra* note 2, at 4337.

[135] *Id.*

[136] *Id.*

[137] *Id.*

[138] *Id.*

[139] Richard E. Caves, *Contracts Between Art and Commerce*, 17 J. ECON. PERSP., Spring 2003, at 73, 81, *available at* http://www.jstor.org/stable/3216857.

[140] *Id.* at 82.

[141] *Id.*

[142] *Id.*

platforms—digital distribution, physical distribution, broadcast distribution—parties tend to have conflicts and may have difficulties in reaching agreements that are satisfactory to both sides, which can result in lengthy negotiations or no deal at all.[143]

Through vertical integration, when parties sit on the same side of the table and know that at the end of the day they will have to continue working together, and when they are aiming for the same goal, agreements are much easier to come by, and it is much more likely to be a speedy resolution.[144] Thus, the costs of these minimized negotiations will not be passed on to the consumer, and the consumer will likely have more options because less time was spent negotiating which territories films would be shown in, and more time acquiring or developing new content. Thus, another benefit of permitting vertical integration in television is a transaction costs reduction, which could result in reduced prices to consumers.

In the case of NBCUniversal/Comcast, no other benefits were expected to arise from the potential reduction of transaction costs.[145] Because of the maintenance of the two companies as separate entities, and the management of the joint venture by a separate Board of Directors, there is the potential that transaction costs will not actually be reduced. This can be exemplified by the $302 million in revenue from transactions between the joint venture and Comcast, for "distribution of [the joint venture's] cable network programming and, to a lesser extent, the sale of advertising and our owned programming" in 2012.[146] The revenue of $22 million from transactions between the joint venture and GE, the corporation that owns NBCUniversal, for "the sale of advertising" further solidifies the potential areas for reductions in transaction costs.[147] Unless agreements exist to mitigate transaction costs, it appears that the formal transactions of the companies still remain separate. This decreases the likelihood that transaction costs will be reduced when such a large volume of transactions occurs. Thus, it is unlikely that substantial savings will arise from transaction costs.

iv. Aggregation of Intellectual Property

The fourth potential consolidation is the aggregation of intellectual property. Copyrighted content is the basis of the television industry, because the protection of "original works of authorship fixed in any tangible medium of expression," particularly motion pictures, is the good exchanged in the market.[148] The more

[143] Comcast, *supra* note 2, at 4331 n.599.

[144] *Id.* at 94.

[145] United States v. Comcast Corp., No. 1:11–CV–00106, 2011 WL 5402137, at *30 (D.D.C. Sept. 1, 2011).

[146] NBCUNIVERSAL MEDIA, FORM 10-Q (QUARTERLY REPORT) 7 (Aug. 1, 2012), *available at* http://files.shareholder.com/downloads/CMCSA/2292725402x0xS1193125%2D12%2D328960/902739/filing.pdf.

[147] *Id.* at 7–8,

[148] 17 U.S.C. § 102 (2006).

> When the U.S. film industry succeeds, everyone benefits. It allows studios to take a chance on more risky movies, emerging screenwriters and unknown actors. It enables them to bring big budget productions to cities across the country and pour money into local economies. It also enables our industry to employ more American workers. The impact is clear. More jobs, more entertainment choices,

content a company has, the more sales and revenue the company will likely generate because it can sell those content rights to others, or it can distribute that content to consumers.[149] "Copyrights are valuable assets to studios. If this intellectual property is taken from them, studios have virtually no other means of generating revenue."[150] Thus, by aggregating content between content producers, companies have greater opportunities to sell their content, thus they have greater opportunities for profit.

By aggregating this content, not only will companies have the opportunity to provide consumers with a broad experience, but they will also have the ability to develop new content.[151] As with the modern middlemen, such as Hulu, Apple, and Amazon, revenues are gained from increasing the number of titles they offer.[152] However, there is also an incentive for producers to go to the middlemen to distribute their services because of the decreased costs of delivery required for digital distribution, instead of physical distribution or cable distribution.[153] And in a system where both the producers and distributors are drawn to middlemen, the middleman market is likely to grow. When companies, such as NBCUniversal and Time Warner seek to provide distribution services by bundling their Internet service to online access to films, producers will be more likely to go to those companies to distribute their content.[154] Since these companies already have content, they do not need to worry about whether they must purchase content first or advertise their services first. They can merely post their content online and invite consumers to view the content, making them a middleman with a built-in consumer base, which reduces marketing and advertising costs. Thus, they are attractive to producers seeking wider audiences, which make them strong content aggregators.

This benefits consumers by centralizing their options for viewing content. When companies pool their intellectual property, they can avoid licensing entanglements and limit conflicts over rights to content.[155] Where companies can

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> more opportunities for the creative professions. Protecting that creativity from theft benefits everyone.

Frequently Asked Questions, MOTION PICTURE ASSOCIATION OF AMERICA, http://www.mpaa.org/faq (last visited Feb. 23, 2012).

[149] MICHAEL MASNICK & MICHAEL HO, THE SKY IS RISING: A DETAILED LOOK AT THE ENTERTAINMENT INDUSTRY 5 (2012), *available at* http://www.ccianet.org/CCIA/files/ccLibraryFiles/Filename/000000000586/TheSkyIsRising7-130.pdf.

[150] Race, *supra* note 72, at 108.

[151] *Frequently Asked Questions*, HULU, http://www.hulu.com/about/media_faq (last visited Feb. 23, 2012).

[152] Erika Morphy, *Amazon Sweetens Prime Deal with More Instant Vid Titles*, E-COMMERCE TIMES (Feb. 8, 2012 9:25 AM), http://www.ecommercetimes.com/story/Amazon-Sweetens-Prime-Deal-With-More-Instant-Vid-Titles-74385.html.

[153] Neildittmar, *Digital Distribution vs. Physical Product—Providers Can't Have It Both Ways*, SLIGHTLY IMPAIRED (Apr. 1, 2010, 10:20 AM), http://www.slightlyimpaired.org/index.php?option=com_content&view=article&id=258:digital-distribution-vs-physical-product-providers-cant-have-it-both-ways&catid=53:technology&Itemid=72.

[154] *See, e.g.*, *HBO Go*, HBO, http://www.hbo.com/#/explore-hbo/hbo-go.html (last visited Feb. 23, 2012).

[155] Jonathan A. Mukai, *Joint Ventures and the Online Distribution of Digital Content*, 20 BERKELEY TECH. L.J. 781, 789 (2005).

own rights to thousands of titles, negotiating the rights to each title would be cumbersome, if not impossible.[156] By consolidating ownership to one company, the licensees know that they have proper permissions to use media, and they can use the content without fear of conflict.[157] The larger benefit for consumers is the opportunity for "one-stop shopping."[158] By having one storefront from which consumers can find content, they can minimize their own "search costs" by visiting one website where all content is aggregated.[159]

Additional benefits follow when a company can provide a singular universal player—such as the player used by Hulu, or YouTube, or Amazon—there is no need for consumers to purchase products to display their purchases, nor do they need to download players to run them on their computers.[160] Additionally, consumers can have a consolidated method of purchasing their content, need not provide their credit card number to various companies, and can have their payments and receipts centralized in one location.[161] Finally, as a benefit to both the consumer and the producer, when content is easy to find—and consumers need not hunt on each individual producer's website—there is less likelihood that consumers will turn to pirated copies of content.[162] Thus, not only will consumers have legitimate ways to view content without violating the law, but they also could potentially see reductions in prices. This would occur because the consumers who legally obtain content only have to compensate for the cost of consumers who would consume illegal content regardless of whether there was a legal version. Decreasing the lost income by the number of consumers who consumed illegal versions because the legal version was difficult to obtain or not available would decrease the costs for which the legal consumers would need to compensate.[163]

Because of the difficulty presented to other companies who attempt to establish universal storefronts, allowing production studios to vertically integrate with ISPs creates the opportunity for vertically integrated companies to provide the benefit of a universal storefront.[164] As mentioned previously, by attaching Internet service revenues to the production of content, distributors can afford to produce riskier content.[165] This ability also applies to purchasing the rights to content from independent studios and other major studios as well. As was also mentioned previously, by permitting an ISP to work with a production company that already has an established customer base, the provider does not have to worry about the risk of not gaining customers upon its entrance into the distribution world.[166]

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156 *Id.*

157 *Id.*

158 *Id.* at 790.

159 *Id.*

160 *Id.*

161 *Id.*

162 David A. Cook & Wenli Wang, *Neutralizing the Piracy of Motion Pictures: Reengineering the Industry's Supply Chain*, 26 TECH. IN SOC'Y, Nov. 2004, at 567.

163 *Id.*

164 *See* Mark S. Torpoco, *Mickey and the Mouse: The Motion Picture and Television Industry's Copyright Concerns on the Internet*, 5 UCLA ENT. L. REV. 1, 70 n.6 (1997) (citing David Clark, Lecture to the class Law, Internet, and Society at Harvard Law School (Feb. 5, 1996)).

165 *See supra* Part III.A.i.

166 *Id.*

Because these companies will have access to the means of distribution—as a result of their control of the speed and accessibility of streams to streaming websites—there is no danger that there would be increased costs for additional data usage or reduced Internet access because of slow streaming.[167]

For example, Comcast already has experience in creating online video on demand programs such as Fancast Xfinity TV or TV Everywhere.[168] As of May 25, 2011, XFinity's viewers had watched more than 20 billion programs with about 350 million views per month.[169] With such a large consumer base, any producer seeking to add new content would have the opportunity to be seen among common television programs in addition to having access to all four major broadcast networks on video on demand.[170] Thus, because of Comcast's access to these broadcast networks, in addition to being able to develop contracts to display content not only through television but also online, in a unified storefront, consumers would have the benefit of having a consolidated provider of television programs. These potential benefits highlight not only monetary benefits to consumers, but also an additional utility benefit in that they can maximize their viewership utility in finding programs that meet their specific needs. This pro-competitive advantage, much like the others listed above, and the fifth listed below, all weigh heavily in the favor of permitting vertical integration, based on the rule of reason analysis a test, balancing these pro-competitive benefits against the potential harms to consumers from permitting vertical integration.

v. Economies of Scale and Economies of Scope

Fifth, and finally, it was argued that in the NBCUniversal/Comcast merger, the companies would achieve greater economies of scale and economies of scope.[171] When companies can produce more of a good with a decreasing amount of average inputs, a company is said to have economy of scale.[172] Economies of scale can be produced internally—savings that accrue regardless of the

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167 *See* Edward Wyatt, *U.S. Court Curbs F.C.C. Authority on Web Traffic*, N.Y. TIMES, Apr. 7, 2010, at A1, *available at* http://www.nytimes.com/2010/04/07/technology/ 07net.html?pagewanted=all. It has also been argued that it's impossible to charge admission for access to a website, thus it is impossible to gain revenue for permitting individuals to view pay-per-view content online. Torpoco, *supra* note 164. First, because someone will provide the content for free once it has been posted online, thus no one will be willing to go to the paid site once it is available for free. *Id.* Second, when it's not worth the credit card fees that a company will pay for a $10 transaction, there is no viable method to collect admission charges. *Id.* This was argued in 1996, but some reality still exists in these claims. *Id.* This is because consumers may be unwilling to purchase content once it is available for free and because consumers may not be willing to provide their credit card to several companies to make several small transactions.

168 Comcast, *supra* note 2, at 4243.

169 Marcien Jenckes, *Xfinity On Demand Reaches 20 Billion Views*, COMCASTVOICES (May 25, 2011), http://blog.comcast.com/2011/05/xfinity-on-demand-reaches-20-billion-views.html.

170 J T. Ramsay, *A Look Back at Xfinity TV in 2011*, COMCASTVOICES, (Dec. 29, 2011), http://blog.comcast.com/2011/12/a-look-back-at-xfinity-tv-in-2011.html. On December 29, 2011, Comcast was the first to offer television series from the four major broadcast networks—ABC, FOX, CBS, and NBC. *Id.*

171 Comcast, *supra* note 2, at 4336.

172 Reem Heakal, *What Are Economies of Scale*, INVESTOPEDIA (Sept. 6, 2009), http://www.investopedia.com/articles/03/012703.asp#axzz1ml0B9zTv.

environment in which a company operates—or externally—economies that result from the organization of an industry.[173]

Telecommunications and Internet services are the perfect example of this because connecting one computer to the Internet has a high fixed cost; however, with each additional customer the average investment in the infrastructure reduces because no additional costs must be provided to continue to lay lines.[174] Additionally, in digital distribution, developing the initial library of films and the initial platform to distribute content, large fixed costs are ameliorated with each viewer, which results in a lower average cost for distribution.[175] Economies of scope occur where companies reduce the average total cost of production by increasing differentiation in their products.[176] In television production, where studios use the same sets, the same actors, and the same directors to produce content from teen musicals to thriller horror stories—yet still appeal to the same tastes of fans—production studios can achieve economies of scope.[177] In providing cable services and Internet service, companies can achieve economies of scope by laying lines for both products at the same time, yet paying the costs of one installation, instead of two.[178]

NBCUniversal/Comcast argued that they would achieve economies of scale and scope "in their provision of video programming, advertising and cross-promotions."[179] In video programming, NBCUniversal/Comcast argued that this would allow them to expand output and quality of programming, and reduce the costs thereof.[180] Additionally, they argued that these benefits would be seen not only in sports programming, but also women's-oriented networks and websites.[181] Further economies would be gained through the sharing of advertising resources, through the companies' combined market research and back office support.[182] Finally, NBCUniversal/Comcast argued that consumers would benefit from cross-promotion because the companies would advertise for one another on their

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[173] *Economies of Scale and Scope*, ECONOMIST (Oct. 20, 2008), http://www.economist.com/node/12446567.

[174] Economies of Scale, WIKINVEST, http://www.wikinvest.com/wiki/Economies_of_scale (last visited Feb. 23, 2012).

[175] *Id.*

[176] *Economies of Scope*, INVESTOPEDIA, http://www.investopedia.com/terms/e/economiesofscope.asp#axzz1ml0B9zTv (last visited Feb. 23, 2012).

[177] *See* The Hollywood Reporter Staff, *'American Horror Story': What the Critics Are Saying*, HOLLYWOOD REP. (Oct. 5, 2011, 4:00 PM), http://www.hollywoodreporter.com/news/american-horror-story-what-critics-244654; Comcast, *supra* note 2, at 4335.

[178] Christopher Brown, *Economies of Scope and the Learning Curve*, ARK. ST. U. (Jan. 23, 2012), clt.astate.edu/crbrown/6313f05no15.ppt.

[179] Comcast, *supra* note 2, at 4335.

[180] *Id.*

[181] *Id.* at 99. Arguably, these benefits were not truly seen since Comcast was ordered to pay $375,000 and was issued an injunction to stop discriminating against channels such as the Tennis Channel, and required Comcast to carry the Tennis Channel at the same pricing tier as it carried its wholly owned sports networks—the Golf Channel and Versus (which was recently renamed the NBC Sports Network). Georg Szalai, *FCC Judge Sides with Tennis Channel in Comcast Carriage Dispute*, HOLLYWOOD REP. (Dec. 20, 2011, 1:44 PM), http://www.hollywoodreporter.com/news/fcc-judge-sides-tennis-channel-275776; Matt Cronin, *FCC decision for Tennis Channel significant*, TENNIS.COM (Dec. 21, 2011) http://www.tennis.com/articles/templates/ticker.aspx?articleid=15450&zoneid=6.

[182] Comcast, *supra* note 2, at 4336.

respective channels thus "raising [consumers'] awareness of programming, leading to greater viewer enjoyment."[183] However, on all three fronts, the FCC expressed skepticism regarding the *actual* benefit to consumers.[184] Though, surprisingly, finding that NBCUniversal/Comcast's argument regarding cross-promotion would "change incentives so that former competitors may now cooperate, potentially benefitting the public with better information."[185]

As a result of economy of scope, companies can disregard diseconomies of scale that typically limit companies from providing services where they do not see efficient returns,[186] because they have an incentive to provide those inefficient services due to new product they have to offer.[187] More specifically, because NBCUniversal/Comcast would receive revenue from subscribers to television stations, or for pay-per-view audiences, NBCUniversal/Comcast has an incentive to provide Internet access to rural areas that are more difficult to reach because they will not only receive revenue from new Internet subscribers but also from new content viewers.[188] Thus, because of economies of scope, NBCUniversal/Comcast could serve the wider public benefit by providing equal access to Internet for all communities.[189]

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183 *Id.*

184 *Id.*

185 *Id.* at 4338.

186 "An economic concept referring to a situation in which economies of scale no longer function for a firm. Rather than experiencing continued decreasing costs per increase in output, firms see an increase in marginal cost when output is increased." *Diseconomies of Scale*, INVESTOPEDIA, http://www.investopedia.com/terms/d/diseconomiesofscale.asp#ixzz1myCtR6SQ (last visited Feb. 23, 2012).

187 "[T]he cost per subscriber of building wireless broadband networks is likely to be higher in rural areas because there are fewer customers over which to spread the cost of building wireless towers and deploying backhaul capacity." International Comparison Requirements Pursuant to the Broadband Data Improvement Act, International Broadband Data Report, FCC, 15 (May 20, 2011), *available at* http://hraunfoss.fcc.gov/edocs_public/attachmatch/DA-11-732A1.pdf.

188 Comcast, *supra* note 2, at 4374.

189 Since it has been noted that 30% of Americans are on the "wrong side" of the digital divide—where they cannot realize the equalizing benefits of the Internet—NBCUniversal/Comcast and the government recognized the ability to lessen this divide by providing access to underserved areas. *Conquering the Digital Divide: Closing the Broadband Opportunity Gap*, INTERNET ESSENTIALS FROM COMCAST, 3 http://blog.comcast.com/assets/InternetEssentialsfromComcast.pdf (last visited Feb. 23, 2012). The FCC has shown dedication to increasing accessibility to broadband Internet within the past several years to limit the digital divide between those who have access and those who do not because they see large potential benefits for decreasing this divide. Specifically, the FCC has noted that:

> The fact remains, however, that too many Americans remain unable to fully participate in our economy and society because they lack broadband. Although this is a nationwide concern, the situation is particularly bleak for Americans in rural and Tribal areas. In addition, Americans with low-income, or who are less educated, unemployed, disabled, seniors, Blacks, and Hispanics have a much lower broadband adoption rate than average. The costs of digital exclusion are high and growing: lack of broadband limits healthcare, educational, and employment opportunities that are essential for consumer welfare and America's economic growth and global competitiveness. In contrast, the widespread deployment and availability of broadband in many areas of the nation promotes a virtuous cycle of investment, innovation, and competition.

FCC, *Seventh Broadband Progress Report*, FCC, *available at* http://hraunfoss.fcc.gov/edocs_public/attachmatch/FCC-11-78A1.pdf.

Thus, while these benefits have the potential to exist, the question comes to the scope and magnitude of the benefits.[190] Additionally, if the magnitude of these benefits does not outweigh the costs to consumers of having a consolidated provider in the television and Internet service industries, then approving a merger may have been against the mandate of the DOJ and the FCC to provide for the benefit of consumers. The potential benefits for allowing television production studios and ISPs to merge, include: increases in diversity, a decrease of double marginalization, reductions in transaction costs, benefits through content aggregation, and potentially increased economies of scale. However, the next section will introduce the harms of permitting vertical integration in the entertainment industry.

B. The Harms of Vertical Mergers

Fears of anticompetitive behavior make even the slightest appearance of unfair competition become the subject of public inquiry, particularly where the entertainment industry and the "marketplace of ideas" could be compromised.[191] However, vertical integration typically receives only minimal scrutiny from regulatory agencies because the parties to the transaction are typically not in the same market, thus they cannot immediately gain and use market power.[192]

Customary concerns about vertical integration include fears of: (1) entry barriers to companies entering the market at only one tier, (2) foreclosures, (3) reductions in quality of the product, (4) reductions of diversity in the market, and (5) price squeezes.[193] Because "[c]ompetition is crucial to the lifeblood of any business, and the television business is no exception,"[194] where competitors seek to exclude new entrants, and block out old competitors, that competition is stifled.[195] As will be discussed below, diminution of competition can be caused by heightened entry barriers because of a requirement that companies enter the market at multiple tiers and exclusion from upstream or downstream products.[196] In the end, these behaviors harm consumers because they detract from consumer welfare by denying "the best allocation of our economic resources, the lowest prices, the highest quality and the greatest material progress, while at the same time providing an environment conductive to the preservation of our democratic political and social institutions."[197] In the case of the television industry, anticompetitive behaviors take away the quality of content, eliminate fair prices for consumers, and

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[190] Comcast, *supra* note 2, at 4330.

[191] H. Peter Nesvold, Note, *Communication Breakdown: Developing an Antitrust Model for Multimedia Mergers and Acquisitions*, 6 FORDHAM INTELL. PROP. MEDIA & ENT. L.J. 781, 785 (1996). The typical fear is that "too much power in too few hands will impair freedom of expression." *Id.* (quotation omitted).

[192] *Id.* at 796.

[193] Patrick M. Cox, Note, *What Goes Up Must Come Down: Grounding the Dizzying Height of Vertical Mergers in the Entertainment Industry*, 25 HOFSTRA L. REV. 261, 272–73 (1996).

[194] Roni Mueller & Gretchen Wettig, *The "New" Series Co-Production Deal in Network Series Television*, 31 SW. U. L. REV. 627, 668 (2002).

[195] WILLIAM C. HOLMES, ANTITRUST LAW HANDBOOK § 6:7 (2011).

[196] *See infra* Part II.B.i.

[197] N. Pac. Ry. Co. v. United States, 356 U.S. 1, 4 (1958).

weaken diversity of content—an antitrust concern unique to creative industries. After a brief discussion of how vertical integration can harm competition through exclusion and barriers to entry, the harms to consumer welfare will be examined more closely.

i. Required Two-Tiered Entry

The basis of two-tiered entry is that "once vertical mergers begin, they can become cumulative and self-reinforcing, as non-integrated firms feel compelled to protect themselves by acquiring access either to raw materials (backward vertical integration) or distribution outlets (forward vertical integration)."[198] This is particularly relevant in the television industry where distributors have increasingly come to find that they may need to enter into the distribution market in order to turn a profit.[199] More troublingly, in the broadband distribution market for films, "a very large audience [is] required to support the development of new programming, finding that, '[b]ecause of the economies of scale involved, the successful launch of any significant new channel usually requires distribution on MPVDs [sic] . . . that cover 40 to 60 percent of all subscribers.'"[200]

To earn profits, companies currently feel a greater need to produce and distribute content, and they tend to find that working with companies that already have a large consumer base will be the most successful avenue for distributing that content.[201] Accordingly, to ensure that a company is successful, it is more likely to merge with a large distributor, which causes other companies to merge with similar companies. Thus, consolidating the market and making it more difficult for production companies to enter the market. This challenge is amplified where entrants face established companies that already hold 40–60% of the market share. This self-reinforcing cycle could eventually spell the end for small distributors and small producers, which will be discussed below.[202] More to the point, the economies of scale gained by companies that are vertically integrated limit other firms' ability to compete because they are unable to gain comparable revenue.[203]

In an inquiry of the market conditions that permitted the major networks to continue dominating in the television industry, program suppliers revealed that many funded their projects through network license fees.[204] Network financing involves producing entities arranging deals with networks in which the production

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198 Walter Adams & James W. Brock, *Antitrust, Ideology, and the Arabesques of Economic Theory*, 66 U. COLO. L. REV. 257, 306 (1995).

199 Rubinfeld & Singer, *supra* note 97, at 645. "[M]any of the top [firms that create, package, and distribute broadband content] are vertically integrated into [cable providers, telephone companies, and other broadband conduit providers]. Those vertical relationships will ensure that a handful of broadband content providers will achieve sufficient scale to remain viable." *Id.*

200 Rubinfeld & Singer, *supra* note 97, at 644 (quoting Time Warner Inc., 123 F.T.C. 171, 207 (1997) (statement of Chairman Robert Pitofsky and Comm'rs Janet D. Steiger and Christine A. Varney)).

201 *Id.*

202 *See infra* Part III.B.iv.

203 *See supra* Part III.A.v.

204 Stanley M. Besen & Thomas G. Krattenmaker, *The FCC's Network Inquiry: A Thirty Year Retrospective*, 10 VA. SPORTS & ENT. L.J. 273, 300 (2011).

companies grant rights to the networks in exchange for financial support.[205] These deals are often signed far in advance to the airing of the program and often do not provide producers with increased revenue where programs are highly successful.[206]

Because the licensing fees production studios gain are often insufficient to cover their production costs, production studios are often forced to function at a loss, also called "deficit financing."[207] Accordingly, deficit financing options must be explored by producers "long before a network license fee agreement is signed, because the availability, size and terms of that financing will determine the program budget the producer can afford and the deficit he or she can realistically accept."[208] Where those funds must be taken from in-house or from outside investors or lenders, companies that already have financing secured have a financial foothold higher than production companies that do not have revenue from providing Internet service or television distribution methods. Although production studios can use the funds gained from previous productions, the ability to develop new content is not nearly as vast as the abilities for integrated companies. Thus, companies may be required to enter into both tiers of production and distribution to gain profit. Additionally, studios may also be required to enter at two levels because of the potential for foreclosure. Thus, permitting vertical mergers could cause harm to production studios that are unable to enter at both tiers of production and distribution could harm the industry. This is particularly true where new competitors are blocked because of competitors' inability to gather resources sufficient to compete, without integrating at both levels. These harms can be compounded by foreclosure within the market due to the required two-tiered entry.

ii. Foreclosure and Consumer Foreclosure

Foreclosure can be a result of input foreclosure, or customer foreclosure. "Input foreclosure results from upstream firms refusing to sell to rival downstream competitors or simply raising those competitors' costs for their inputs."[209] This goes back to the fact that content and its ownership can make or break a company in the entertainment industry.[210] Where companies have access to content that they have made, or content that others have made, they will be players in the game.[211] Where producers have access to a distributor in-house, they are unlikely to sell their content to other companies in the interest of preserving the profits of their own companies.[212] This will result in companies paying higher prices to receive content, or contributing their content to the integrated company's storefront.[213] In

[205] *Id.*

[206] *Id.* The ability to renegotiate terms remained, regardless of option provisions. *Id.* at 301.

[207] *Id.* at 300.

[208] Evaluation of the Syndication and Financial Interest Rules, Second Report and Order, 8 FCC Rcd. 3282, 3298 (1993).

[209] Cox, *supra* note 193, at 278 (footnotes omitted).

[210] *See supra* Part III.A.iv.

[211] *Id.*

[212] MARK COOPER & CORIE WRIGHT, WHY THE COMCAST/NBC MERGER POSES A MAJOR THREAT TO VIDEO COMPETITION THAT ANTITRUST AUTHORITIES CANNOT IGNORE, 2 (2009), *available at* http://www.freepress.net/files/FP_CFA-Comcast-NBC-WhitePaper.pdf.

[213] *Id.*

either situation, the consumer is harmed because he will pay more to receive content through another provider, or he will be forced to do business with the integrated company, regardless of whether he wants to do such business or not.[214]

"Customer foreclosure occurs when the downstream merged customer refuses to buy from the upstream rival firm."[215] Customer foreclosure is the inverse of the aforementioned anticompetitive behavior, where distributors are unwilling to accept content from producers. Though the seeming unlikely type of foreclosure—particularly where there are not rampant examples of producers refusing to do business with various distributors[216]—there is the potential for customer foreclosure where companies do not have the funds to add additional content, or where content does not seem to have sufficient economies of scale, or where distributors simply deny access to producer's material.[217] Thus, by controlling the upstream and downstream ends of the production chain, there is the potential that integrated companies can block out producers or distributors of content, thus, causing the market to become less diversified, more costly, and less convenient for consumers. Because of the resulting reduction of companies in the television market, exclusion and entry barriers cause less free competition in the market, which in turn, harms consumers because it increases prices, reduces the diversity of content, and reduces the quality of content. These examples of how vertical integration can be harmful, when weighed against the five merely marginal benefits for permitting vertical integration, can seem to exaggerate the need for regulatory action. This is especially true when coupled with the potential harms to the quality and diversity of television that could result from vertical integration.

iii. Reductions in Quality

Quality concerns arise when competition is reduced because of the exclusion of others from the market.[218] For example, where distributors do not have to display content from other exhibitors, they have no obligation to produce content that consumers would prefer, particularly where products are highly interchangeable.[219] The challenge is that no two viewers are the same in their taste

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[214] Race, *supra* note 72, at 102. "Antitrust Division lawyers are questioning whether the studios will use digital movie distribution agreements to inhibit competition by refusing to license films to other companies looking to provide digital movies, or by using their leverage in the online movie industry to drive up fees charged to consumers." *Id.*

[215] Cox, *supra* note 193, at 278.

[216] *See* Ben Fritz, Joe Flint & Dawn C. Chmielewski, *Starz to End Streaming Deal with Netflix*, L.A. TIMES (Sept. 2, 2011), http://articles.latimes.com/2011/sep/02/business/la-fi-ct-netflix-starz-20110902; Jason Gilbert, *HBO Ends Netflix DVD Discount: Report*, HUFFINGTON POST (Jan. 5, 2012, 03:06 PM), http://www.huffingtonpost.com/2012/01/05/hbo-netflix-dvd-discount_n_1186825.html.

[217] Comcast, *supra* note 2, at 4260–61. Congress has specifically feared that "vertically integrated program suppliers have the ability and incentive to favor their affiliated cable operators, allowing them to impair competition from existing competitors, new entrants, and new technologies (such as DBS)." *Id.* at 4253; *see also* Mueller & Wettig, *supra* note 194, at 669 (discussing conflicts between Steven Bochco and David Duchovny on the one hand, and Twentieth Century Fox Film Corp on the other for insufficient bargaining and preferring "sweetheart" deals with close affiliates).

[218] *See* ABA SEC. OF ANTITRUST LAW, ANTITRUST LAW DEVELOPMENTS 327 (5th ed. 2002).

[219] *See supra* Part III.A.i. This is particularly true where consumers are willing to accept "good enough" quality to take price reductions in television, even if those price reductions are only relative or are minimal. David Lieberman, *Web and Other Options are Shaking Up How We Watch TV*, USA

or approbation of content. Between critical movie sites, the number one movie listed on one site could receive an 80 out of 100,[220] a 90 out of 100 from another,[221] and a 9.2 out of 10 based on general consensus.[222] However, consumers tend to recognize that there is a quality of movie that is generally high, and a quality that is generally low, consistently rating a film at 24 out of 100,[223] 17 out of 100,[224] and 2.5 out of 10 based on general consensus.[225]

It has been argued that creative industries are typified by at least four types of properties: (1) "nobody knows" properties with uncertain demand; (2) "art for art's sake" properties that are primarily developed as a result of passion regardless of the demand; (3) "A-list/B-list" properties that are products with vertically differentiated quality; and (4) "ars longa" properties that have a quality that makes them durable in that they will gain continuing benefits in the future.[226] While the quality of the first, second, and fourth are debatable, the fact that A-list and B-list programs exist demonstrates that there is a tier of content that is seen as inferior. "A creative good's quality in the eyes of consumers can be increased by enlarging the fixed cost expended on it. These extra fixed costs might buy more elaborate special effects, crowds of extras and the like, but especially they buy more skilled (costly) creative participants."[227] Where more skilled participants are involved, there is no assurance that there will be greater quality; but, the probability is more likely than waiting for the next big hit to be produced by an "at home" director. While it is recognized that outliers can result from small scale productions,[228] small budgets, or inexperienced talent, it is difficult to determine which individuals will produce quality that consumers seek; where an individual has a tried and true track record, it is more likely that a product of high quality will result because of his skill and training in the area.

Accordingly, where companies have no incentive to produce films ranking in the top tier, because consumers will view content regardless of the quality, studios will have an incentive to place smaller investments in film when they know that

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TODAY (Jan. 6, 2011, 5:23 PM), http://www.usatoday.com/tech/news/2011-01-04-1Acable04_CV_N.htm.

220 *Critic Reviews The Shawshank Redemption*, IMDB, http://www.imdb.com/title/tt0111161/criticreviews (last visited Feb. 23, 2012).

221 *The Shawshank Redemption (1994)*, ROTTEN TOMATOES, http://www.rottentomatoes.com/m/shawshank_redemption/ (last visited Feb. 23, 2012).

222 *The Shawshank Redemption*, IMDB, http://www.imdb.com/title/tt0111161/ (last visited Feb. 23, 2012).

223 *Critic Reviews Kazaam*, IMDB, http://www.imdb.com/title/tt0116756/criticreviews (last visited Feb. 23, 2012).

224 *Kazaam (1996)*, ROTTEN TOMATOES, http://www.rottentomatoes.com/m/kazaam/ (last visited Feb. 23, 2012).

225 *Kazaam*, IMDB, http://www.imdb.com/title/tt0116756/ (last visited Feb. 23, 2012).

226 Della Valle, *supra* note 124, at 6–7.

227 Caves, *supra* note 139, at 80.

228 *See* Malcolm Gladwell, *What is Outliers About?*, GLADWELL.COM, http://www.gladwell.com/outliers/index.html (last visited Feb. 23, 2012). "'Outlier' is a scientific term to describe things or phenomena that lie outside normal experience." *Id.* For example, a cold day in the summer in Paris is an outlier because most days are expected to be warm or hot, and scientists understand why most days are hot in the summer. *Id.* Yet, for some reason, these outliers occur, and sometimes those outliers can result in unexpected success stories such as Bill Gates, or successful corporate lawyers in New York City, or stellar hockey players. *Id.*

the content will be distributed, regardless of the quality. Although the benefit of offering lower quality content is that offering lower priced bundles for lower quality content could create price tiers, companies could choose to use the quality division to maintain prices at a certain level and require consumers to purchase "premium" content bundles to turn an additional profit. Yet, on the whole, discussing quality is difficult because of the inability to peg what will be of high utility to a television consumer. Within the approval of the NBCUniversal/Comcast joint venture, the FCC pointed to its worries regarding reductions in quality at several points, highlighting the fear that as companies have less incentive to produce high quality products because of their dominant positions in the market, they will capitalize thereon, and trade quality for quantity.[229]

Another fear expressed in both the NBCUniversal/Comcast and AOL/Time Warner transactions was the reduction of the quality of others' products because of the ability of the companies to control the Internet connections through which others provide content. "For example, routers could be programmed to provide high bit rates and superior customer performance for AOL Time Warner channels, programs and services, and slower bit rates and inferior customer performance for content provided by unaffiliated sources."[230] In the NBCUniversal/Comcast joint venture, the FCC explicitly conditioned that "Comcast shall continue to meet FCC signal quality standards when offering public, educational, and governmental channels on its cable systems."[231] Thus, expressing a fear that where content was not particularly profitable, that the content would be denied valuable airtime or signal quality. This fear continues for any company not affiliated with a vertically integrated company who has not entered both markets, because producers are at the whim of companies that air their content because the quality of programs could be reduced in their distribution, even if they were high quality productions. Thus, because of the potential effects on products produced by the company, and because of the potential effects on the distribution quality of content produced by other companies, vertical integration can potentially cause a reduction in the quality of products within the television market. Another potential detriment due to permitting vertical integration could be a reduction in the diversity of content, as will be discussed below.

iv. Reduction in Diversity

Because of the difficulties in determining whether this reduction in quality will actually affect consumer utility, the more troubling anti-competitive result could be the loss of diversity in content. Industry analysts have noted that the number of prime-time programs supplied has increased, while the number of programs produced by independent producers has decreased.[232] "With vertical integration and resulting mega conglomerates, the first group to get squeezed out

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[229] Comcast, *supra* note 2, at 4342.

[230] Time Warner Inc., 16 FCC Rcd. 6547, 6594 (2001).

[231] Comcast, *supra* note 2, at 4336.

[232] Besen & Krattenmaker, *supra* note 204, at 322 (quoting STANLEY M. BESEN, THOMAS G. KRATTENMAKER, A. RICHARD METZGER, JR. & JOHN R. WOODBURY, MISREGULATING TELEVISION: NETWORK DOMINANCE AND THE FCC 113 (1984)).

was the smaller to mid-size independent production companies."[233] This results in fewer companies in the market, which harms diversity where smaller companies are absorbed into larger companies where all creative decisions must pass through one governing board, which provides only for the tastes of the board and the statistics upon which they rely to determine which content will be successful.[234] While this content may be of higher quality because of the larger companies' ability to pay for more inputs into the film, producers argue that "the best television programming springs from [their] diverse and passionate voices."[235] This provides for the outlier effect mentioned previously, which is particularly relevant in the television market.[236] Television producers have no way to know what content will satisfy consumers; and, where companies do not let new talent enter the industry, the potential for innovation in the market cannot be satisfied, and consumers cannot reach higher potential levels of utility.

In vertically integrated companies, diversity can be blocked through distribution or through production because the production decisions must go through a central body, which will inevitably limit the spectrum of content that enters the market. Or, content will be limited through distribution because vertically integrated companies could refuse to purchase content from unaffiliated producers. After these potential effects on the market, unregulated, vertically integrated companies still may cause further reductions in diversity by foreclosing companies which no longer can afford to work in the market without entering distribution and production. As a result, the fewer the competitors, the less content that can be produced because of constraints on capital, time, and resources. Thus, on the whole, the potential reductions of diversity and quality present dangers to the creative aspects of the television industry. A corollary of the reduction in diversity is the potential increase in prices that could result from vertical integration.

v. Increase in Prices

Vertical integration negatively affects prices where producers receive lower prices for their products because they have limited avenues for distributing their products and where distributors must pay higher prices to acquire content. As has been discussed, when fewer producers and distributors participate in the market, they have fewer options from which they can purchase their content. Also, where companies engage primarily in self-dealing, they reduce the number of producers and distributors in the market because they choose not to purchase content from others. Accordingly, the few players left to compete can demand higher prices because of their larger market share. Because these higher prices must be paid off, customers will be forced to absorb the cost of the monopolization in the production and distribution markets. Thus, prices can be increased as a result of reduced competition.

However, because of the self-dealing aspect of vertical integrations, it may

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[233] Mueller & Wettig, supra note 194, at 669 (footnotes omitted).

[234] *Id.*

[235] *Id.* (footnote omitted).

[236] *See supra* Part III.B.

be more costly for outsiders to buy into the distribution or production scheme held within the vertically integrated company. Thus, increased prices may occur because of the power held by companies across multiple dimensions. And, because of the symbiotic relationship between producers and distributors—where producers must have avenues to deliver their content to consumers to succeed and distributors must have access to content in order to sell that content to consumers—neither player can be excluded from the market without enduring substantial harms. Of particular interest to the expansive television content market, "programmers [cannot] support new offerings by relying on technologies or partners other than market leaders, because replicating 'the coverage of these systems by lacing together agreements with the large number of much smaller MVPDs is costly and time consuming.'"[237] Because of these factors, companies are forced to work with large companies to distribute their content; this forecloses smaller entries into the distribution market, further increasing the market power of the distributors and their ability to demand high prices from consumers. Thus, on the whole, vertical integration poses price increases because of the consolidation of the market, which would inevitably be passed on to consumers. When combined with a reduction in the quality and diversity of programming, this could result in all consumers paying exorbitant prices for B-list television programs with only limited options to choose from. In general, companies that are not barred or regulated by United States agencies would likely harm consumer's welfare.

C. Summary of the Cost Benefit Analysis

Overall, it is difficult to estimate the results of vertical integration in the television industry. This is particularly difficult where market harm can result from single-tier entry barriers, foreclosures, quality reductions, diversity reduction, and price increases; yet, benefits can result from increased investment in risky products, price deflation, decreased transaction costs, beneficial content aggregation, and economies of scale and scope. The countervailing forces on alternative ends seem to leave regulation in a zone of uncertainty that likely will not result in a decisive leaning towards finding a beneficial or harmful change in competition. In the unique television and communications markets, it is difficult to say whether competition is actually hampered by consolidation of companies because of the inherent natural monopoly that exists, as a result of the high fixed cost requirements

Regulating these integrations is detrimental to innovation in the market. Where companies seek to gain economic efficiencies through consolidation, they cannot invest in new technologies and are even forced to divest their innovations. For example, NBCUniversal/Comcast was required to completely divest the companies' holdings in Hulu; accordingly, there is a potential that regulations will push newly merged companies to separate themselves from the intermediary technology they created, and disincentivize the creation of new technology.[238]

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[237] Rubinfeld & Singer, *supra* note 97 at 644 (quoting Time Warner Inc., 123 F.T.C. 171, 207 (1997) (statement of Chairman Robert Pitofsky and Comm'rs Janet D. Steiger and Christine A. Varney)).

[238] United States v. Comcast Corp., No. 1:11–cv–0 0106., 2011 WL 5402137, at *8 (D.D.C. Sept.

And, where the trend is for companies to fall into alliance with online distribution systems—for example the participation of most studios in Netflix and Amazon programs[239]—there is an indication that there will be a new set of competitors, and the companies that are able to grab hold in those markets will have the best opportunity to act as leaders in the market.[240] Thus, there is seemingly a timing detriment to those companies who enter the market first, as was the case following the Paramount decrees. Where companies innovate and seek to bolster these ventures through increased integration with presently existing markets, they may be pushed to the background of the competitive market and forced out of their realization of benefits that they, arguably, deserve to reap. Thus, it should be questioned on the whole: where the benefits and harms of vertical integration essentially cancel one another out, should regulatory agencies step in to further curb their incentive to innovate?

IV. CONCLUSION

"The most corrosive piece of technology that I've ever seen is called television—but then, again, television, at its best, is magnificent."[241] When analyzing whether permitting vertical mergers are summarily a benefit or a harm to the television industry, the underlying currents are protecting the beauty of the content of television, guarding consumer's choice, and ensuring that the industry has the opportunity to provide for beautiful content and competition. While the benefits may include more investment in risky endeavors and product diversification, price deflation, reductions in transaction costs, benefits from content aggregation, and economies of scale and scope, there are lurking dangers in decreases in competition as a result of heightened entry barriers and exclusion, which could harm the diversity, quality, and price of content.

The intersecting regulations of agencies, stemming from the duties of of the

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[239] For an exemplification, see the joint ownership of Hulu by Fox and ABC. Ryan Nakashima, *Hulu Plus Ends Year with 1.5 Million Subscribers*, ABC ACTION NEWS (Jan. 17, 2012), http://www.abcactionnews.com/dpp/news/science_tech/hulu-plus-ends-year-with-15-million-subscribers-wcpo1326743048004. For a further example, see the alliance of Sony Pictures Home Entertainment, Twentieth Century Fox Home Entertainment, Universal Studios Home Entertainment and Warner Home Video in the UltraViolet program. Peter Svensson, *Amazon Will Sell UltraViolet Movies*, USA TODAY (January 11, 2012, 9:23 AM), http://www.usatoday.com/tech/news/story/2012-01-11/amazon-ultraviolet-movies/52495788/1.

[240] *2012 Outlook on Media & Entertainment Interview with Phil Asmundson*, ORAN, http://ornanmedia.weebly.com/1/post/2012/10/2012-outlook-on-media-entertainment.html (last visited Feb. 22, 2012).

> For content creators, from film and television to music and print, this change certainly has an impact on revenue streams . . . . Business models are changing, as consumers are looking to use new devices to view and access content on the go . . . . Think tablets; think smart phones . . . . All of the media and entertainment subsectors will have to deal with this true-life disruption . . . . One way to address this is through partnerships with newcomers to the media and entertainment ecosystem . . . . This will be the dominant issue for years looking forward . . . . It's the game that media and entertainment companies will not want to lose.

Id.

[241] Jeff Goodell, *Steve Jobs: Rolling Stone's 2003 Interview*, ROLLING STONE, Dec. 3, 2003, *available at* http://www.keystonemac.com/pdfs/Steve_Jobs_Interview.pdf.

FCC, the FTC, and the DOJ to protect competition and television consumers, have been innovative in permitting two goals, first, allowing companies to pursue these integrations and, second, placing conditions on integrations to prevent potential harms that could come from developing media giants. As the market continues to consolidate, with companies having more access to the ability to distribute through alternative middlemen, and as they have the opportunity to gain popularity through social media networks and word of mouth, the healthy competition seen in the former entertainment industry is likely to be sustained. While the structural elements of the industry will likely remain the same, merely the faces will change. Instead of viewing a DVD or VHS, consumers will log onto online streaming websites. And, instead of successful products coming from independent production studios, even the garage director will have the opportunity to produce popular content. Summarily, vertical integration is merely a method for the traces of former companies to survive and a method for them to change with the times. Because they have the resources to develop the Internet networks, they are able to fit into the market, and, because they can purchase content from others using those revenues, it is likely that the companies will either change their business models or they will lose their production sides, as has been seen with the AOL/Timer Warner merger and the Hughes Electronics Corporation /News Corporation transaction. Where a few of the benefits and harms of these integrations have been elaborated here, the majority of the effects have yet to be seen.