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Cable television has expanded enormously during the past decade by any measure - subscriber revenues, subscribers, availability ("homes passed"), channel capacity, programming, or viewing shares. In 1991, roughly sixty percent of American television households subscribe to cable television. This rapid growth, combined with recent increases in basic cable subscription rates, has led both the Federal Communications Commission and the Congress recently to re-examine the rules of the cable regulation game.

Under the Cable Communications Policy Act of 1984 ("Cable Act"), franchise authorities can regulate rates for "basic cable service" only if a cable system is not subject to effective competition. The commission has the responsibility of defining effective competition and establishing rate regulation standards. Moreover, the Cable Act directs the commission to review these regulations periodically, to amend them if necessary, and to submit a report to Congress "regarding rate regulation of cable services." In that report, the commission found that "cable operators possess varying degrees of market power in the local distribution of video programming" (FCC 1990b). Market power is the ability of a firm profitably to raise the price of a product above the cost of providing it. The commission's report also includes legislative proposals designed to promote competition between cable and other multichannel delivery systems. While effective competition rules may constrain cable market power in the distribution of basic cable service, the commission favors reliance on competition rather than additional regulation to constrain cable market power with respect to other components of cable service. Various bills have been introduced in Congress to "reregulate" cable, but none have become law. These proposals would permit, in some circumstances, regulation of more than just the basic tier of service.

The commission has recently revised the effective competition criteria and rate regulation standards. Significantly, definition of effective competition now requires that six unduplicated broadcast signals be available rather than the previous standard of three unduplicated broadcast signals. Many more cable TV franchises are potentially subject to regulation of basic rates under the new six-station standard than under the old three-station standard. Because of this change, cable TV regulation is likely to be revisited by state legislatures and local governments that grant cable franchises. This article explains both the Federal Communications Commission's recent decision, and also explores the economic issues of competition and regulation in the cable TV industry.

Characteristics of cable television

Cable television has come a long way since it started roughly forty years ago as "community antenna television" - CATV. As that earlier name suggests, cable began as a medium for retransmitting television broadcast signals to areas with poor reception or limited local availability of broadcast service. In the early 1950s, there were relatively few television stations

in the country and the first cable systems had quite limited channel capacity. Now cable systems have larger channel capacity and offer a rich menu of programming in addition to local broadcast signals. The explosion in cable programming is due in great part to the use of satellite communications for national distribution of programming to cable systems.

Today, retransmission of local broadcast signals, cable's "antenna service" function, remains important. Indeed, local broadcast signals account for a majority of all-day viewing in cable television households. However, cable provides two other broad categories of service-"basic cable" networks and "premium" service.

Basic cable networks are generally offered as part of a package or "tier" of services for a single monthly fee. Most carry advertising, so these networks have a "dual revenue stream" from advertising and per-subscriber fees paid by cable operators. Cable operators may offer more than one service tier, and at least some basic cable networks are usually packaged with retransmitted local broadcast signals.

Basic cable networks fall into two rough subcategories - general interest and specialized. The general interest services offer a variety of movies, series, and other entertainment, including some sports. Their programming resembles that of independent television stations. Examples of general interest basic cable networks are USA, TNT, and the Family Channel. This group also includes distant broadcast stations (stations not available off-air locally) and superstations (independent television broadcast stations that are widely distributed by satellite beyond their home markets). WTBS from Atlanta, WGN from Chicago, and WWOR from New York are examples of superstations.

Some basic cable networks offer specialized programming. CNN and Headline News are twenty-four-hour news channels. ESPN provides all sports, and MTV and VH-1 provide music videos and related programming aimed at different musical generations. Other cable networks target children, Blacks, and Spanish speakers, as well as groups such as those interested in travel. Local broadcast signals are, to some extent, substitutes for basic cable networks, particularly the general interest services. Thus, broadcast signal availability provides some competition to cable systems' provision of basic cable networks as well as to provision of "antenna service."

The "premium" category includes services such as Home Box Office, Showtime, or the Disney Channel, which offer high value programming, such as, recent (or classic) movies, usually without advertisements. These services are generally sold on a per-channel basis. Pay-per-view also falls within the premium category. The main pay-per-view offerings are very recent movies, some concerts, and sporting events (boxing and professional wrestling in particular). To access premium services, consumers must subscribe to basic cable service. Because most households have videocassette recorders (VCRs) and because tape rentals are so widely available, premium services are currently subject to substantial competitive pressure.

Availability of cable television

During the last decade, cable television has expanded substantially by virtually any criterion. In 1980, 45.7 percent of the nation's 76.3 million television households were "passed" by cable. The

1991 projection is ninety-five percent of 92.3 million television households. From 1980 to 1991, the number of basic cable households jumped from 19.2 million, or 25.2 percent of television households, to a projected 53.1 million, or fifty-eight percent of television house- holds (Paul Kagan Associates 1990, 1991).

The quantity of programming available also increased substantially. In 1980, only 8.6 percent of cable subscribers were served by cable systems with thirty or more channels. In 1991, the fraction is 92.2 percent (Warren Publishing 1980, 1991). As channel capacity was growing, so was the number of national cable programming networks, which leaped from twenty-seven to seventy-two between 1980 and 1991 (National Cable Television Association 1991). This programming is, of course, augmented by regional and even local cable-originated programming.

The expansion in cable programming has been accompanied by increases in cable viewing, revenues, and rates. From 1984-85 to 1989-90, the all-day viewing share of cable-originated services increased from fourteen to twenty-six percent (Setzer and Levy 1991, pp. 23 and 28). These figures are for all television households. Cable viewing shares are higher in cable households and are also rising. The situation in prime time is similar, although cable shares are smaller. From 1982-83 to 1989-90, the viewing share in all television households of cable-originated programming doubled, rising from ten to twenty percent. Cable revenues have skyrocketed over the last decade (Setzer and Levy 1991, pp. 73, 116). From 1980 to 1990, cable operator revenues increased from $2.6 billion to $17.9 billion. Virtually all of this is subscriber revenues rather than advertising. Currently, most cable advertising revenues accrue directly to the program networks. Cable network advertising revenues jumped from $45 million in 1980 to $1.4 billion in 1990.

The General Accounting Office (GAO) has conducted three comprehensive surveys of cable television rates and services. The most recent survey permits comparison of cable rates as of November 30, 1986 (just before the Cable Act's rate deregulation provisions went into effect) and April 1, 1991 (GAO 1991, pp. 5, 7). Adjusted for inflation, the average monthly basic service rate for the most popular service rose by 36.5 percent, while the average monthly basic service rate for the lowest priced service rose by thirty-two percent. However, if the monthly rates are expressed on a per channel basis, the inflation-adjusted increase for the most popular service was only 4.7 percent, while the increase for the lowest priced service was 2.2 percent. (Because market power is the ability to maintain price above cost, price data alone are insufficient for determining if cable systems are exercising market power. Cost data, which are not readily available, are also required.)

Cable television regulation before 1984

Cable television has been subject to regulation by both local franchise authorities and the Federal Communications Commission. Initially, cable television was subject to local regulation only. Local authorities generally require cable operators to have a franchise. As part of the franchise grant, local authorities were able to regulate basic cable rates and cable services. Federal Communications Commission regulation began in 1965. The U.S. Supreme Court upheld the commission's "ancillary jurisdiction" over cable in 1968. That is, the court found that, in order to achieve the goals of broadcast regulation, the commission had the authority to regulate cable.

The commission chose to regulate cable television out of concern that it might have an adverse economic impact on local broadcast stations. Between 1965 and 1972, the commission adopted detailed regulations for cable that had the effect of protecting local broadcasters from cable competition. They included "must carry" rules (requirements that cable systems carry all local television broadcast signals), "syndicated exclusivity" and "network nonduplication" rules (to protect local stations from duplication of their network or syndicated programming by imported signals), and outright limits on the number of distant signals that a cable system could import. The commission prohibited common ownership of cable television systems and television broadcast stations or telephone companies within the service area of the station or company. The commission also preempted local regulation of non-basic cable subscription rates and then chose to forbear from regulating those rates (FCC 1974). Thus, even before the Cable Act, premium service rates were not regulated.

The Cable Communications Policy Act of 1984

Even before 1984, the tide of cable television regulation had begun to ebb. The commission eliminated some of its cable television regulations, and some jurisdictions chose to deregulate cable rates on their own initiative. Still, the Cable Act sought to reduce what was then seen as an excessively stringent regulatory regime for cable TV.

The Cable Act amended the Communications Act of 1934 to add a new Title VI, which provides the framework for cable regulation that is in effect today. The Cable Act established "a national policy concerning cable communications" and is designed to "promote competition in cable communications and minimize unnecessary regulation that would impose an undue economic burden on cable systems." The bulk of Title VI sets forth what franchisors (*i.e.*, state or local governments granting franchises) are permitted to do in enforcing and renewing franchises and in regulating rates and services. Passage of the Cable Act reduced significantly the regulatory authority of franchisors. Title VI establishes procedures for granting and renewing franchises, specifying that a "franchising authority may award...1 or more franchises within its jurisdiction." Franchise authorities may collect franchise fees of up to five percent of the cable system's gross revenues. Under certain conditions, and subject to limitations, franchisors may regulate basic cable rates.

Franchise authorities may enforce programming requirements in franchise agreements already in effect when the Cable Act became effective, although under specified circumstances the cable system may be able to eliminate a required service (*e.g.*, if it is no longer available to the operator). Operators also have broad freedom to move channels from one service tier to another. As a condition of franchise renewal, authorities may require the cable operator to provide channels for public, educational, and/ or governmental use, but for other services can only impose requirements "for broad categories of video programming or other services." Title VI also requires cable systems with thirty-six or more channels to set aside a certain percentage of channels for leased access by unaffiliated entities. It also sets out general procedures for renewing a franchise and for the sale of cable system facilities in the event that a franchise is not renewed or is revoked.

Under Title VI, telephone companies are prohibited (with very limited exceptions, *e.g.*, in rural areas) from owning cable television systems within their telephone service area. Television broadcast stations are prohibited from owning a cable system if there would be an overlap between the cable community and the broadcast station's coverage area.

Effective competition and price regulation

Under the Cable Act, franchising authorities can regulate "rates for the provision of basic cable service in circumstances in which a cable system is not subject to effective competition." Basic cable service is defined as "any service tier which includes the retransmission of local television broadcast signals." The Cable Act also permits cable operators to increase basic rates by five percent per year without franchise authority approval. Franchise authorities are expressly permitted to prohibit discrimination among basic cable subscribers. The Cable Act required the commission to adopt regulations defining effective competition and establishing rate regulation standards. The commission concluded in 1985 that a cable system faced effective competition if three unduplicated off-the-air television broadcast signals were available to the cable community (FCC 1985). The commission's implementation of the Cable Act's rate regulation provisions brought about substantial deregulation of basic cable rates. A study by GAO (1989) indicates that, as of October 31, 1988, only three percent of cable systems were regulated. While some jurisdictions had suspended rate regulation on their own initiative, the deregulatory impact of the Cable Act was considerable.

In January 1990, the commission embarked on a comprehensive review of its effective competition and rate regulation rules (FCC 1990a). The commission pointed to the substantial increase in the average number of channels available on the basic tier since deregulation and suggested that the three-signal standard might no longer be adequate. There are now two alternative criteria for effective competition (FCC 1991a). First, "a cable system will be deemed to face effective competition if at least six unduplicated broadcast television signals are available over the entire cable community." (An unduplicated signal is one that does not simultaneously duplicate more than fifty percent of another signal's weekly prime time schedule.) Second, a cable system is subject to effective competition if "an independently owned, competing multichannel video delivery service is available to fifty percent of the homes passed by the incumbent cable system and subscribed to by at least ten percent of the homes passed by the alternative system within the incumbent cable system's service area."

The new standards went into effect on October 25, 1991. The revised effective competition standards will likely increase significantly the number of cable systems and subscribers subject to regulation. The National Telecommunications and Information Administration (NTIA) estimated that fifty-two percent of all cable systems, serving eighteen percent of all subscribers, could be subject to rate regulation with a six signal standard. (Editor's note: Under the six-signal rule, many, if not most, of Maine's cable TV systems could be subject to rate regulation.)

The commission's six signal criterion does not necessarily lead to unregulated basic cable rates that are competitive in the textbook sense. The commission, conscious of its Congressional mandate to "minimize unnecessary regulation that would impose an undue economic burden on cable systems," sought a rule that would "not only protect the public from the exercise of market

power by a cable system in the provision of basic service, but also minimize regulation that would impose an undue economic burden directly on cable systems and indirectly on the public." The multichannel competitor criterion should also be understood as an informed judgment that balanced competing concerns. While the multichannel criterion does not explicitly include retransmission of local broadcast signals, the commission indicated that "it is implicit in our analysis that access to such service (local broadcast signals) is also present and not impeded." In other words, effective competition to basic cable service is either six local signals or a multichannel competitor, plus all available local signals.

In establishing these criteria, the commission was aware of the limitations on regulatory control over the content of basic cable service. The commission noted that, after passage of the Cable Act, when cable operators no longer had to place basic cable services on separate tiers in order to avoid price regulation, they apparently found it desirable to reduce tiering. Under current law, operators retain substantial flexibility to retier even if their basic service is or becomes subject to regulation. Thus, one consequence of increased price regulation, or even the prospect of it, could be retiering. Indeed, many cable operators have already engaged in retiering, apparently spurred by the possibility of cable re-regulation by Congress (*Broadcasting* May 21, 1991, pp. 35-41). Between December 31, 1989 and April 1, 1990, the average number of basic channels in the lowest priced tier declined by 1.4 and the average number of basic channels in the most popular tier increased by 1.7. (See 1991 GAO Cable Survey, p. 15.) The commission considered retiering and other "strategic behavior" by cable operators and concluded that it had no authority to respond to such behavior.

Procedural standards for rate regulation

The commission retained its existing procedural standards for rate regulation and adopted some additional standards. Procedural requirements include requirements for public notice for proposed basic rates and an opportunity for parties to comment, at least in writing, on such proposals. Franchising authorities "shall allow a fair return on investment taking into account appropriate costs," including, capital costs, basic cable programming, customer service, labor, and other costs, as well as "a reasonable profit." The commission amended its procedural rules to provide for a written decision on all rate cases and to require "substantial written evidence" to support any decision not to permit the cable operator to recover documented increases in these costs.

The commission's rules provide that franchising authority decisions must be appealed to the relevant state court rather than to the commission. The commission also suggested that states consider granting state public utility commissions the power to regulate basic cable rates. State public utility commissions have rate-making responsibilities in various other areas already and are likely to have the experienced staff and resources needed to implement the commission's basic cable rate-making standards. Small communities may not have adequate staff and resources for this task.

Signal carriage rules

The commission's effective competition decision also included a *Second Further Notice of Proposed Rulemaking* (FCC 199la), which explores the question of must-carry rules. When Congress passed the 1984 Cable Act, commission rules required cable systems to carry all local broadcast signals. Those rules were declared unconstitutional. The present *Second Further Notice* asks whether must-carry rules "would assist substantially in preserving the system of over-the-air broadcasting established in the Communications Act." In particular, the commission is interested in whether the availability of six television broadcast signals can, in fact, constrain cable rates if those signals are not carried by the relevant cable system. The underlying concern is that, absent cable carriage, cable subscribers will not view those channels. The resulting decline in advertising revenues could lead those stations to provide less news and public affairs programming and generally to provide a program schedule less competitive to cable offerings. Of course, local signals not carried by cable may, in general, be picked up off the air. However, cable subscribers frequently do not have antennas, and few cable subscribers apparently have acquired input selector switches (so-called "A/B switches") to facilitate the shift between cable and off-the-air reception. Fewer than one percent of cable subscribers have an outdoor antenna and an A/B switch, although this does not mean that consumers cannot acquire input selector switches (See U. S. Senate Report 1991, p. 45).

Prospects for competition to cable television systems

While the recent commission decision is likely to increase the importance of price regulation in cable TV, competition from a number of different sources may, in the long run, be an even more effective constraint on cable rates. At least initially, broadcast signals, rather than rival multichannel delivery services will be the primary source of effective competition to cable. But because multichannel delivery systems can compete with cable not only in providing basic service but also in the full range of services that cable offers, the development of multichannel rivals to cable is of particular public policy importance.

In the *Effective Competition Order and Second Further Notice* (FCC 1991a), the commission listed direct broadcast satellite services, home satellite dish systems, multichannel multipoint distribution service (also known as "wireless cable"), competing cable systems, and satellite master antenna television systems as potential multichannel competitors. While there are currently 53 million cable subscribers, there are no direct broadcast satellite subscribers, roughly 307,000 wireless cable subscribers, and approximately 890,000 satellite master antenna TV subscribers (Paul Kagan Associate 1991, p. 6). In fact, satellite master antenna TV subscription is declining and is unlikely to seriously challenge cable. The number of competing cable systems is also quite small. Next to broadcast television, home satellite dish systems currently provide the closest thing to competition for cable, particularly in rural areas. There are over three million home satellite dish systems in place. Thus, roughly 3.6 percent of television households have home satellite dishes (Paul Kagan Associates 1991).

In assessing the future development of video delivery systems, it is necessary to keep in mind an important technological development - digital video signal compression (Setzer and Levy 1991, Chs. V and VII). Compression is a signal processing technique that permits transmission of a

television signal using a substantially smaller slice of radiowave frequency than is currently needed. This technology, which is applicable to all video delivery modes - broadcast, satellite, cable, and wireless cable - will permit a significant increase in channel capacity and, a reduction in the cost of that capacity. It is likely to be implemented first for satellite, then for cable, and later for broadcasting. The remainder of this section considers competing media and potential competitors (*i.e.*, telephone companies).

Broadcast television

In the immediate future, broadcast signal availability is likely to be the primary source of effective competition (Setzer and Levy 1991, Chs. IV and IX). Between 1975 and 1990 the number of commercial broadcast stations increased from 706 to 1093. Virtually the entire increase consisted of UHF stations, which benefitted from the extension of their coverage areas brought about by cable carriage. About seventy-five percent of the increase consisted of independent stations (*i.e.*, stations not affiliated with one of the three major commercial networks). Within the past few years, more than 100 of the roughly 400 "independent" stations have affiliated with the new Fox network.

In recent years, cable has made significant inroads on broadcasting in terms of both audience shares and advertising shares. The most significant impact has been on the networks, although station revenues have also been adversely affected, particularly smaller market stations and marginal stations in the larger markets. The decline in broadcast audiences and revenues is irreversible, so broadcasting is not likely to be a stronger competitor to cable in the future than it is now. To a great extent, this simply reflects market and technological realities that enable cable to offer a wider range of programming, and to obtain a dual revenue stream (advertising and subscription fees). However, there may also be some regulatory constraints on broadcasting that no longer serve the public interest and, in fact, unfairly constrain broadcasters from competing. The commission has recently opened a broad inquiry on this subject (FCC 1991b).

The cable compulsory license for retransmission of TV signals is one statutory component of the imbalance between broadcasting and cable. Several years ago, the commission recommended elimination of the compulsory license (FCC 1989). More recently, the commission recommended phasing it out as the interim must-carry rules that it recommended for adoption would expire (FCC 1990b, para. 14). The commission believes that, at some point, the compulsory license should be replaced by a "retransmission consent" regime.

Retransmission consent means that a cable operator could not retransmit a television broadcast signal without the consent of the station. Stations would be able to bargain with cable operators over signal carriage and, in the case of those with popular programming, receive compensation in cash or in kind (perhaps through favorable channel positioning or additional channels on the cable system) for carriage. This could provide broadcast stations and program producers with a second revenue stream to supplement advertising revenues. Retransmission consent legislation has been introduced in both houses of Congress during the current session. The bills introduced include must-carry provisions of some sort along with retransmission consent, and permit stations to choose every three years between retransmission consent and must-carry rights.

Satellite services

Currently, virtually all direct-to-home satellite service is in a portion of the spectrum known as the C-band, in the fixed satellite service. Fixed satellite service was not initially conceived as a direct-to-home service, but rather as a point-to-multipoint service for the delivery of programming to local distributors (e.g., television broadcast stations and cable systems) for retransmission to households. The C-band home satellite dish retail business piggybacks on this wholesale distribution business. The advantages of this arrangement are programming availability and low incremental cost. On the other hand, C-band home satellite dish systems require relatively large antennas (ten feet or so in diameter) and are relatively expensive ($2000-$4000).

The commission has issued construction permits to eight companies for direct broadcast satellite systems in the Ku-band. The power levels at which direct broadcast satellites will operate and the relatively wide spacing between orbital slots will permit the use of smaller and less expensive home reception equipment (antennas possibly as small as twelve inches in diameter and costs initially in the $500-$700 range).

Satellite services appear certain to flourish in areas without access to cable television service. In cabled areas, where these services might serve as a source of effective competition to cable, the situation is less clear. While the fixed costs of satellite distribution can be spread across subscribers nationwide, if the cost of home reception equipment is too high it will be hard for direct broadcast satellite to compete with cable.

The other key factor is the programming available to satellite broadcasting. Cable programming is clearly very popular, and it is likely that satellite services will need to offer cable networks, many of which are owned by large cable system operators. Some would-be direct broadcast satellite providers have expressed the concern that these large cable operators will withhold their cable program services from rival delivery systems, or will provide them only on disadvantageous terms. The commission has recommended that Congress enact legislation that would mandate program access under certain circumstances (FCC 1990b). Cable re-regulation bills introduced in Congress during the current session contain more stringent program access provisions. Also, satellite technology does not permit retransmission of local television stations (a clear disadvantage relative to cable), although this may change.

It is possible that satellite services could also compete with cable by offering popular new services. The nationwide coverage of satellite could permit aggregation of specialized audiences and provision of specialized programming targeted at market segments other media cannot effectively serve. With the expanded channel capacity provided by video compression, it might also be possible for a satellite provider to offer the same programming, *e.g.*, a pay-per-view movie, several times per evening (perhaps every fifteen minutes or half hour) on different channels with staggered starting times. Because viewers would never need to wait long for the movie to start, this service has been dubbed "near-video-on-demand." While compression technology will also permit capacity expansion and near-video-on-demand by cable and other media, it is likely that compression will be deployed first in the satellite arena. Thus, satellite

services might get a headstart in near-video-on-demand and might use it to establish their position as competitors to cable.

By and large, the success of satellite services will be determined by business and regulatory factors beyond the control of local officials. However, if local officials wish to encourage, or at least not discourage, competition from satellite services, they would do well to ensure that local zoning ordinances do not discriminate unfairly against the installation of satellite dish antennas (*e.g.*, Setzer and Levy 1991, pp. 100- 101). In 1986, the commission preempted certain state and local zoning regulations that discriminate against satellite antennas. However, the commission has not been directly involved in enforcing its preemption and has relied instead on private action in local courts. (Two petitions requesting more vigorous enforcement are before the commission.) To the extent that zoning ordinances have constrained or would constrain consumers' use of satellite technology, liberalization of such ordinances could indirectly enhance the competitiveness of satellite services.

Multichannel multipoint distribution service

Multichannel multipoint distribution service, a microwave service that is sometimes referred to as "wireless cable," suffers from limited channel capacity and, to some extent, from programming availability problems. There are only thirty-two or thirty-three channels available to wireless cable operators. However, wireless cable systems include VHF and UHF antennas for reception of local broadcast signals, so operators do not need to use the microwave channels for retransmission of those signals. The available microwave channels are governed by two separate commission regulatory regimes. Wireless cable operators can obtain licenses for up to twelve or thirteen channels for full-time use. The other twenty channels are allocated to the Instructional Television Fixed Service, an educational service. Wireless cable operators may obtain licenses for unused educational channels, with certain limitations and conditions. They may also lease "excess capacity" from educational licensees (FCC 1991c).

Wireless cable operators have historically had some difficulty gaining access to cable networks. While the problem of access appears to have abated, wireless cable operators continue to complain about onerous and allegedly anti-competitive geographic restrictions on their exhibition rights for cable services (FCC 1990b, para. 112, 130). It is currently uncertain whether wireless cable operators are covered by the cable compulsory license. This threatens their access to superstations and other distant broadcast signals. The United States Copyright Office, which has some administrative responsibilities for the compulsory license, is currently investigating this matter.

Competing cable systems

Competing cable systems, sometimes referred to as "over-builds," are another potential source of effective competition to incumbents. The Cable Act permits a franchisor to award "1 or more franchises within its jurisdiction." A few communities have been served by competing cable systems for many years. In other cases, however, entrants have been purchased by incumbent systems, which leads to suspicion that entry was undertaken for the purpose of being bought out, a kind of "greenmail."

Due to the high fixed cost of constructing a cable system, there is a certain inefficiency in having two parallel cables passing each home. On the other hand, competition pushes prices closer to costs, so it is possible that consumers would be better off with competing systems. Indeed, for a sample of six communities with competing cable systems, average per channel basic cable rates were thirty-four percent lower than the national average (FCC 1990b, appendix H). It is worth noting that entrants do not always offer lower prices than incumbent cable systems. The entrant may compete by offering a higher-priced, higher-quality package of services.

While local franchisors cannot ensure the presence of a competing cable system, they might at least consider removing impediments to entry. The commission has recommended that Congress enact legislation that forbids local authorities from unreasonably denying a franchise to potential entrants and that permits entrants to begin construction without having to meet a "universal service" requirement during some initial period (FCC 1990b, para. 14). The Communications Act currently permits local franchisors to prohibit discrimination among cable customers, so an incumbent that desires to cut its subscription rate to meet competition could be required to offer the lower price even in areas not subject to direct competition. Of course, franchise authorities that wish to encourage competing cable systems may take these measures without benefit of legislation.

Telephone company provision of cable service

While telephone companies have long wanted to move into the cable business, both commission rule and the Communications Act currently prohibit local exchange telephone companies from providing cable service in their telephone service areas. The commission has had an inquiry on "telco-cable" cross-ownership open for four years. Recently, the commission (FCC 1991d) tentatively endorsed an option called "video dial tone," in which telephone companies would offer, on a common carrier basis, video connections to the home, which various programmers could lease. Consumers could then "dial up" whatever services they wished to purchase. Restricting the telephone company to common carrier provision of video dial tone service would reduce or eliminate concerns about anti-competitive effects of telephone company control of video access to the home.

On the other hand, without the opportunity to profit from programming, telephone companies might not find it profitable to invest in the facilities. For that reason, the commission also opened an inquiry on whether local telephone companies should be able to provide video programming themselves, and, if so, what safeguards might be appropriate. Regulatory safeguards may be needed to rule out the possibility that, through cross-subsidy from its regulated common carrier local exchange activities or other measures, a telephone company that provided video programming could achieve monopoly control of the only "wire" to the home.

Conclusion

The Federal Communications Commission's new effective competition rules will significantly increase the number of cable systems that may be subject to basic cable rate regulation (at the option of local franchise authorities). Cable systems will now be considered subject to effective competition if six unduplicated television broadcast signals are available throughout the cable

service area or if fifty percent of the homes passed by the incumbent cable operator have access to an independently owned, rival multichannel delivery service and at least ten percent of home passed by the rival within the incumbent's service area actually subscribe to the rival.

For the near future, broadcast signal availability will be the primary source of effective competition. Other media, such as competing cable systems, wireless cable, satellite services, or telephone companies, may also provide effective competition later on. Over the next several years, the most promising of these appears to be satellite services. If direct broadcast satellite gains access to cable networks at reasonable prices and if home reception equipment is sufficiently low in price, direct broadcast satellite could provide significant competition for cable. If popular new services (e.g., near video on demand) are offered via satellite before becoming available on cable, this could enhance satellite's competitive position.

On the other hand, if cable becomes the single provider of multi-channel video service to the home, and competition does not materialize, then it will be necessary to reconsider the regulatory regime. This applies not just to "basic cable service" in the meaning of the Cable Act, but also to "local distribution of video programming," the larger category of service identified by the commission. While some components of that service, such as movie channels, face significant competition now, good alternatives to some of the special interest basic cable networks may not be available. These services, which cable operators generally have the freedom to keep off the regulated basic cable service tiers, could be a continuing source of cable market power if multichannel delivery alternatives do not develop.

While the future structure of video delivery markets will be determined primarily by technological, market, and regulatory developments beyond the control of local authorities, those authorities can nevertheless take certain actions to encourage, or at least remove impediments to, competition in video delivery. In particular, local authorities could look more favorably on multiple cable franchises and ensure that local zoning and other ordinances do not unduly discriminate against home satellite (or wireless cable) antennas.

(Editor's note: An expanded discussion of this topic by the same author, which includes greater technical detail, is available from the PURE Technical Paper Series of the Margaret Chase Smith Center for Public Policy, University of Maine.)

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Endnote:

1. The opinions and conclusions expressed in this paper are those of the author and do not necessarily reflect the views of the Federal Communications Commission or any of its Commissioners or other staff.

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