TV Carriage Fee Disputes Hurt Consumers the Most

By Jennifer Holt, John Vanderhoef, Kevin Sanson, and Rachel Allen

14-18 minutes

More than 14 million Dish Network subscribers have been without *Breaking Bad*, *Mad Men,* and *The Walking Dead* since June when the satellite provider pulled AMC Networks—AMC, Sundance, IFC, and WE tv—from its lineup in a dispute over carriage fees. The tactic is called a blackout, and it's becoming increasingly common in the television landscape as pay-TV operators and station owners battle over the nearly $5 billion at stake in the next 5 years.

Such disputes are really nothing more than a high stakes (and quite lucrative) game of chicken between mighty media companies—those who own network stations and cable channels, on one side, and those who operate the cable or satellite systems that brings those stations into our homes, on the other. No matter the outcome, the viewers always lose. They miss out on their favorite programming when negotiations turn sour and ultimately end up paying higher subscriptions rates when cable or satellite companies relent to media conglomerates' costly demands.

Unfortunately, with no regulatory solution in sight, blackouts are likely to prove a mainstay, keeping debates about carriage fees, retransmission consent, and “must carry” rules in the headlines.

Here are five things you need to know about carriage disputes:

1. Corporate profits, not public interests, are at stake in carriage disputes as media conglomerates seek additional revenue from retransmission fees.

2. Historically, local station owners argued that over-the-air broadcasting was a public good unfairly threatened by expanding pay-TV services, and the FCC agreed.

3. Cable and satellite operators and public interest groups are pushing for regulatory reform, but no one expects a resolution anytime soon.

4. Emergent platforms and technologies are providing alternatives to the traditional pay-TV business model.

5. Social media and viral marketing have proven popular tools for programmers to curry favor with audiences despite asking fans to pay more for the very programs they’re being encouraged to save.

1. Corporate profits, not public interests, are at stake in carriage disputes as media conglomerates seek additional revenue from retransmission fees.

Carriage fees, retransmission consent, and “must carry” rules have been hotly contested in a growing number of blackouts.

Content providers and pay-TV operators must renegotiate these contractual relationships every three years, and the fall out from failed negotiations betray a shift away from public interests toward corporate bottom lines.

Carriage fees are what cable and satellite systems pay cable networks for the right to include the company's programming on their channel lineup. According to SNL Kagan, for example, pay-TV operators paid Disney-owned ESPN $4.08 per subscriber in 2009. Networks, like ESPN or AMC, consider their programming a revenue-generating asset for pay-TV operators who rely on it to attract advertising sales and subscribers. In return, carriage fees help underwrite a portion of the network's production costs. Disputes emerge when the parties can't agree on the value of the programming, or more specifically, when pay-TV operators accuse cable networks of bundling: a practice that effectively subsidizes lesser watched channels by packaging them with a network's more valuable properties to charge higher carriage fees (e.g., Dish has accused AMC Networks of requiring the satellite company to also pay for its lower-rated channels, like WE tv, in order to access its more valuable programming on AMC).

Since there's little legal recourse for either party in these disputes, the battle is often fought in the court of public opinion (see the note on social media below). By contrast, broadcast stations (e.g., your local ABC, CBS, or NBC affiliate), unlike cable channels, enjoy special leverage in fee negotiations thanks to federal regulations enacted two decades ago to protect locally produced television. The 1992 Cable Act established that pay-TV providers "must carry" local broadcast networks, or pay a retransmission fee to the broadcaster for the use of its signal. It's only been more recently that the disputes have spread to cable networks. Higher carriage fees help offset declining revenue from ad sales (a trend that affects cable networks and broadcasters alike). For cable networks, however, higher carriage fees also speak to the growing popularity and, thus, shifting value of cable content in relation to broadcast programming. As showrunner Kurt Sutter recently tweeted in response to *Sons of Anarchy*'s ratings surge over broadcasting, "No more niche, bitches."

While the economics of retransmission fees are slightly obtuse, and the FCC does not provide clear guidelines for what constitutes "good faith" negotiations, there is big money at stake. In 2011, retransmission fees totaled $1.46 billion. Analysts expect fees to continue to increase for the next 12 years with some projections predicting totals of more than $4.9 billion by 2017.

2. Historically, local station owners argued that over-the-air broadcasting was a public good unfairly threatened by expanding pay-TV services, and the FCC agreed.

Originally, FCC regulations sought to preserve the public interest in and economic viability of local broadcast networks as cable and satellite operators encroached on audiences and advertising dollars. By requiring cable operators to pay a fee for the right to carry local broadcast signals, the 1992 Cable Act secured additional revenue for station owners who needed the money to invest in programming and sports deals and remain competitive against cable's wherewithal.

Yet, despite the law's twenty-year history, disputes over programming fees are very much a contemporary phenomenon. In the past, as conglomeration brought broadcast networks and cable channels under the same corporate umbrella, "must carry" rules proved an effective way for media companies to secure carriage of their newer, lesser-known channels in lieu of retransmission consent. However, in the mid-2000s, particularly after the economic crisis in 2008, corporate broadcasters started to value increasingly high retransmission fees as an additional revenue source. A growing number of distribution outlets, like satellite, also gave broadcasters more leverage in their negotiations with cable operators. CBS Corp., for example, recently renewed a retransmission deal with Cablevision that puts CBS on track to quadruple its current fees to over $1 billion by 2016.

Ironically, local network affiliates don't benefit much from retransmission fees as most of the revenue is given directly to the network for access to popular primetime programming. It's a lesser-known front in the battle over retransmission and has serious implications for the production of local news and public affairs programming. Nevertheless, these fees have increased as more viewership and advertising dollars move to cable stations, causing some affiliates to drop network content altogether.

3. Cable and satellite operators and public interest groups are pushing for regulatory reform, but no one expects a

resolution anytime soon.

Both pay-TV operators and public interest groups agree that the current retransmission consent regime is "broken" and requires Congress and the FCC to intervene. Several pay-TV providers argue retransmission regulations no longer make sense in the current marketplace. At the time of the Cable Act in 1992, distribution options for broadcast signals were confined to a single operator. Now, the distribution landscape is littered with options: telephone companies, satellite providers, over-the-top technologies, and streaming platforms like Hulu and Netflix. Consequently, the idea that one provider has a monopoly on television distribution holds little purchase. Since regulation guarantees carriage on cable systems, there's nothing stopping broadcasters from holding the pay-TV market hostage for exorbitant retransmission fees.

Senate Commerce Hearings on Cable Act, June 2012

Back in 2010 amidst several high-profile black-outs, a group of twelve satellite, cable, and telecom providers and two public interest groups joined forces to tell the FCC that the Cable Act was in dire need of revision. One year later, the FCC responded with plans toupdate retransmission rules, inviting interested parties to submit comments. Pay-TV operators were in favor of many of the FCC's proposed changes, including offering clearer standards for good faith negotiations and eliminating the rules that prevent a pay-TV provider from carrying the same syndicated programming on two stations in the same market. However, the FCC's authority to enforce these rules has been called into question. FCC Chairman Genachowski has commented that the FCC has limited authority to "revise the way the system works," but the future of these changes remains uncertain.

While the FCC continues their review process, pay-TV providers and public interest groups have shifted their attention to Congress. Earlier this summer, representatives from Time Warner, CBS, and the NAB debated in the Senate whether the 20-year-old Cable Act is a viable framework for promoting the future of video. Law scholar Susan Crawford claims that the impending deadline for reauthorizing the Satellite Television Extension and Localism Act (STELA), which grants satellite operators license to widely distribute over-the-air signals, could reopen debate on the Cable Act, but this remains to be seen.

4. Emergent platforms and technologies are providing alternatives to the traditional pay-TV business model.

Whereas content companies and pay-TV providers struggle to maintain the status quo, new distribution platforms point to the possibility of “unbundling” television content for a la carte consumption. Such technologies enable consumers to access content when and where they want, and on an array of platforms, for much less than increasingly pricey cable subscription packages (this last point has been debated).

Whereas industry reports suggest the exodus from pay-TV is minimal at best, industry trades are still eager to report on the potential threat cord-cutting poses to content companies and traditional distributors.

Evidence for this concern is drawn from the growing number of alternative platforms and services now available for consumers. Despite piracy offering similar content for free, industry-sanctioned OTT options do exist, and include paid streaming and electronic sell through options like Hulu Plus, iTunes, and Amazon, all available on game consoles and set-top boxes including Roku or Apple TV. These services have been modestly successful by offering convenience, quality, and reliability at an affordable cost, a point supported by findings in our Connected Viewing Initiative.

Yet, the fact that pay-TV operators refuse to give these platforms and services access to their live signals cripples a company like Apple from disrupting television's traditional business model. More controversial are services like Aereo and IVI tv that rebroadcast local television signals over Internet-enabled devices. Broadcast networks claim Aereo is stealing content by avoiding retransmission fees, but Aereo argues it only sells the small digital antennas that facilitate access to free, over-the-air programming, not the programming itself. Aero and IVI have been the targets of lawsuits, but Aereo's recent court victory suggests technological solutions may outpace any regulatory reform.

Ultimately, it doesn't make sense to blame the blackouts on viewers who prefer to consume their television content on non-traditional platforms. Rather, the disputes are more indicative of content companies and pay-TV operators struggling to adapt (or maintain) their traditional, and quitelucrative, business models amidst technological change and competing economic pressures.

5. Social media and viral marketing have proven popular tools for programmers to curry favor with audiences despite asking fans to pay more for the very programs they're being encouraged to save.

The dispute between AMC Networks and Dish Networks—which started in June 2012—is approaching a record length of time (nearly 4 months), leaving many subscribers wondering where they will watch the Season 3 opener of *Walking Dead* on Oct. 14.

Dish dropped AMC, IFC, Sundance, and WE tv from its lineup because it claims AMC Networks overvalues its programming, arguing the channels' ratings, even for a hit like *Breaking Bad*, don't justify an increase in carriage fees. AMC reportedly wants to raise carriage fees over the next five years from 26 cents per subscriber to 75 cents per subscriber. Moreover, Dish accuses AMC of forcing the satellite company to carry its less popular networks for the right to carry its more prestigious namesake network. AMC says it simply wants a greater percentage of the revenue its programming already generates for Dish. (An unrelated lawsuit between the companies adds a level of complexity to this particular case). Dish blacked out the channels when the parties failed to reach an agreement.

Viacom Ad, 2008

Such a blackout poses a serious threat to an independent programmer that lacks the financial cushion of a major media conglomerate. Similarly, AMC lacks the extensive lineup of cable properties, like Viacom or Disney, to leverage in a carriage dispute. According to *The Wall Street Journal*, Dish represented nearly 13 percent of AMC's average subscriber base, and losing that revenue likely will reduce the company's third quarter profit by more than 30 percent.

Really, though, the real losers here are the fans themselves who miss out on their favorite programming or end up paying higher subscription rates when contracts are finally renewed. So, it's not without irony that AMC has launched a social media and viral marketing campaign to leverage viewer support against Dish Network.

Initial efforts included commercials during *Mad Men* to warn subscribers about the pending blackout on Dish. Dish retaliated by moving AMC from channel 130 to 9609. After the blackout, AMC offered free screening party kits for anyone who "adopted" a Dish subscriber for the season premiere of *Breaking Bad*. It also offered Dish subscribers a live stream of the premiere online.

Social media messaging on Facebook and Twitter repeatedly lambasted Dish Network for dropping AMC programming, and the campaign's "snarkiness" extended to full-page advertisements in national newspapers. AMC enlisted the help of viral marketer Thinkmodo to rally support for the network by filming a zombie invasion of New York City. The video's final title card reads: "Zombies don't belong here. Put them back on TV." They also launched a viral video contest called "Hey Dish, Where's My AMC?" in which the network asked viewers to act out their ill feelings toward to the satellite company. In addition to a $4,000 cash prize, the winner received free publicity on AMC social media sites, a Canon camera, and a development meeting with a network executive.

Of course, the cable networks have fought for audience sympathies as well, but they historically have been less successful than the networks when it comes to leveraging viewer support during carriage disputes.