Cracking the Cable Conundrum: Government Regulation of A La Carte Models in the Cable Industry

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INTRODUCTION

Prominent politicians and consumers alike are deeply concerned with the state of cable in America. In fact, some Senators have reported that more of their constituents are concerned with expensive cable than highly politicized issues like gay marriage. Even Senator John McCain has described cable as an unwarranted “tax” on Americans and recited in front of Congress the tragic tale of the 74 year-old widow who was forced to pay nearly $7 a month for ESPN.

The source of such high prices in cable is in large part related to the existence of cable “bundles.” In the United States, every cable television provider offers packages of channels as opposed to individual channels. It is impossible for consumers to purchase the vast majority of channels through anything other than these bundles — rather, the channels are offered only as part of a bundle. If consumers want to purchase only one channel out of a 20-channel bundle, they have to request and pay for all 20 channels before they have access to the single desired channel.

Despite all the possibly hyperbolic comments from politicians regarding the ill effects of cable bundling, their views are generally in line with those of the American people. For example, when presented with a theoretical “a la carte” alternative wherein individual channels are made available for purchase, 92% of consumers would be at least “somewhat likely” to switch to a full a la carte option.

To address the concerns surrounding cable bundling, several solutions have been proposed, including mandating that cable providers offer a la carte pricing to consumers. This Article analyzes whether such a solution would be beneficial. Part I discusses the background of the cable bundling and a la carte models, Part II describes the potential benefits and drawbacks of an a la carte model, and Part III analyzes arguments concerning why government intervention may not be the

3. Id.
best means of addressing the cable bundle problem. Part IV explores the future of
cable given the increase in internet viewship alternatives like Netflix and Hulu.

I. CABLE BUNDLING AND THE A LA CARTE MODEL

Cable bundling refers to the practice of cable companies offering consumers a
package of channels, rather than offering channels on an individual basis.\(^5\) Under
the current bundling system, “cable prices have increased by an average of 4.6
percent per year and in excess of 7% per year for the expanded basic program tier
over the past five years.”\(^6\) This increase in cable prices amounts to about three
times the rate of inflation over the same time period.\(^7\)

While the price of cable has increased, the options for consumers within each
cable package has also increased. Although cable companies provide customers
with the flexibility of offering hundreds of channels, the flexibility in choosing
cable packages as a whole is sparse. For example, consumers may only have the
option of choosing between three packages, but each package has hundreds of
channels. This model provides customers with fewer options in terms of the
number of packages they can buy, but allows them viewing flexibility once they
have settled on a package. However, it is unclear that consumers desire this much
viewing flexibility — today, the average household receives 137 channels, but
watches only 33 of those channels each month.\(^8\)

Politicians and consumers alike propose eliminating the cable bundling model
because they believe offering channels in this manner effectively forces people to
pay for products they do not want.\(^9\) Specifically, consumers believe their cable

5. James Surowiecki, Bundles of Cable, NEW YORKER (Jan. 25, 2010), available at
http://www.
newyorker.com/talk-financial/2010/01/25/100125ta_talk_surowiecki.

6. FCC, REPORT ON AVERAGE RATES FOR CABLE PROGRAMMING SERVICE AND EQUIPMENT
and-equipment-1 (“The average monthly price of expanded basic service . . . for all
communities surveyed increased by 4.8 percent over the 12 months ending January 1,
2012, to $61.63, compared to an annual increase of 2.9 percent in the Consumer Price
Index (CPI).”).

7. See id. (“Expanded basic cable rates increased by . . . a compound average annual rate of
6.1 percent over the 17-year period from 1995-2012”).

8. CREDIT SUISSE, PRESENTATION TO NIELSEN GLOBAL CLIENT COUNCIL (2012), available at
http://nielsen.com/content/dam/corporate/campaigns/gcc/NielsenGlobalClientCouncil_Indu-
stryInsights-SPencerWang.pdf.

9. Alex Sherman, Bundled Cable TV Withstands Consumer Opposition, BLOOMBERG
BUSINESSWEEK (November 14, 2013), http://www.businessweek.com/articles/2013-11-
14/2014-outlook-cable-bundling-and-higher-bills-wont-stop-soon; Bruce Walker,
Consumers Will Lose if Cable Is Unbundled, USNEWS (Sept. 17, 2013),
bill would be lowered if channels were offered on an individual or “a la carte” basis, because consumers would only have to pay for the channels they actually want to watch. In contrast, the bundling business model has been characterized as a type of tax upon Americans because certain households end up subsidizing the more expensive viewing preferences of other households. This is particularly true of those who pay for but do not watch sports programming, which is estimated to cost consumers over $20 per month on their cable bill alone. Encompassed in the typical sports bundle is ESPN, which adds about $6 per month to a consumer’s cable bill, and various Fox Sports channels, which cumulatively add around $7 per month.

The economic appeal for consumers of an a la carte model is as follows: cable would be cheaper if consumers paid per channel, since instead of paying $100 for 100 channels they could possibly pay a prorated amount of $5 a month for 5 shows. Following this logic, consumers believe that by cable companies charging for only channels they want, which in many instances might only amount to 5 or 6 channels, their cable bill would be drastically reduced. This line of reasoning relies upon the assumption that cable companies would not respond to regulations by changing the average price per channel in order to maintain profit.

The evidence of the a la carte model actually reducing consumers’ cable bill is disputed. Many studies show not only that cable prices would be unlikely to decrease under an a la carte system, but that an a la carte system would actually increase prices, especially with respect to the sports channels that already

10. See Sherman, supra note 9.
13. See id.
14. Matthew Yglesias, A La Carte Won’t Fix Cable, SLATE (May 14, 2013), http://www.slate.com/articles/business/moneybox/2013/05/mccain_s_la_carte_cable_bill_is_bad_deal_for_consumers.html (“The problem starts with a fundamental misunderstanding: the delusion that if your basic package contains plenty of channels you never watch, you’re paying for many channels you don’t watch.”).
15. See Rennhoff & Serfes, supra note 1.
comprise a large portion of a consumer’s bill. A 2006 review of a la carte cable found that in fact “costs for both operators and subscribers increase when basic cable tiers are customized.”

Nevertheless, other studies have found that a la carte pricing would lower cable prices. For example, one independent study concluded that the average cable bill would fall by 15 to 20 percent under an a la carte system, but that cable companies’ profits would also fall. The same study found that some programming networks would benefit while others would be harmed. The study used industry data and hypothesized how and content producers and cable providers would react to market conditions an a la carte system.

The dispute over the effects of a la carte pricing exists even within the agency responsible for cable regulations. The FCC published reports on a la carte cable pricing in both 2004 and 2006. The 2004 report concluded there would be little benefit to consumers from a la carte pricing, therefore making an a la carte system undesirable. The 2006 FCC report reached the opposite finding, concluding that consumers would see “substantial benefits” from an a la carte model. In examining the two studies, the Congressional Research Service found that “none of the studies or reports issued” by the FCC were “definitive.”

One specialist in the telecommunications policy field, Charles Goldfarb, attempted to make sense of the conflicting FCC reports. In a Congressional report he mentioned that neither report is based on a model developed by the FCC itself. Instead, each model is based on minor modification performed by the


18. See Rennhoff & Serfes, supra note 1.

19. See id.

20. See id.


24. See id.
National Cable & Telecommunications Association.25 The uncertainty and different results in the FCC reports comes as no surprise considering the large number of potential interactions and responses by the many parties involved.26 The various responses of consumers, program networks, and cable operators all must be accounted for in the model. In addition, the FCC does not have a comprehensive data set, forcing it to rely on assumptions, rather than concrete numbers.27

a. Why Does Cable Bundling Exist?

If consumers do not want cable bundling, and if cable bundling is potentially expensive and inefficient, why does it exist in the first place? Cable bundling and the high prices associated with cable are historically recent issues dating back about 20 years. Before 1992, the big four networks of ABC, CBS, NBC, and FOX were considered to be something of a public good and by law had to be available for free.28 These networks saw that the niche cable channels like ESPN, CNN, and Discovery were getting paid by the cable providers.29 This seemed unfair to the big networks because they were offering shows with higher ratings, yet they were forced to provide programming to the cable providers for free.30

The cable providers’ world turned upside down in 1992, when they lost the upper hand in deciding what channels were delivered to the homes of viewers across the country. This is because Congress in 1992 made it legal for the big four networks to be paid for their content with the Cable Television Consumer Protection and Competition Act (“CTCPCA”).31 This new law allowed the big four networks to demand payment for their content moving forward.32 However, cable providers did not immediately kowtow to the big networks by paying them for their content. After all, the cable companies were understandably reluctant to pay for content that they were used to getting for free.

25. See id.
26. See id.
27. See id.
29. See id.
30. Id.
32. See PLANET MONEY, supra note 28.
The refusal of the cable companies to pay for the big networks’ content created a standoff. Networks were unwilling to shell over broadcast rights to their precious hit shows for free, and the cable company refused to pay the “greedy” networks. Specifically, the compromise allowed the cable providers to receive more channels and content from the network owners in a way where the cable provider technically did not have to pay for the big network shows. This compromise resulted in a new set of channels like FX, which was created by FOX, and MSNBC, which was an offshoot of NBC. As a result, the cable bundle was born, with more content for the viewers at the cost of higher cable bills. The downside in this compromise is that bundling these additional network-owned channels was required in order to carry the major network affiliate in the market.

Negotiations between the networks and cable providers continue to this day, and these negotiations often result in standoffs. At the end of every year, networks must renegotiate their licensing terms to the cable providers, and failure to agree to terms can result in publicized disputes such as the recent refusal of CBS to provide any channels to Time Warner Cable.

Channels that are now considered mainstream and vastly popular like ESPN may have never had a chance under the a la carte system. While ESPN is now one of the most widely viewed television networks, this was not always the case. When ESPN first aired in 1979, it advertised itself as being a form of “sports heaven” and set up its office not in a swanky New York City studio but in Bristol, Connecticut. ESPN also had to pay cable providers to include them in their cable packages as opposed to the cable company paying ESPN for its content license. When ESPN gradually became more popular, they were able to bolster their power with the cable providers, therefore switching the power dynamic. As ESPN succeeded and millions of people began tuning into the startup, ESPN could therefore demand more money from the cable companies.

33. See id.
34. See id.
35. See id.
36. See id.
38. Id.
39. Id.
40. See id.
41. It was so unproven that “in its early days, ESPN actually paid cable providers to get into your living room.” See id.
42. See PLANET MONEY, supra note 28.
Other niche channels like Discovery and CNN, also started in a similar way.\textsuperscript{43} The cable companies then passed this costs onto the consumers.

b. Government Attempts to Regulate the Cable Industry

Government attempts to regulate the cable industry began in the 1960s, when federal regulators enacted rules to block cable television operations in large markets in order to protect broadcast television from upstart competitors.\textsuperscript{44} These rules were later overturned in the 1970s, as cable grew in popularity across America.\textsuperscript{45} More deregulation ensued in the mid-1980s, but slowed following complaints regarding rising rates and the monopoly power of cable companies.\textsuperscript{46} The 1992 Cable Act soon followed, along with the rise in cable prices.

As cable bundling led to ever-increasing cable prices, Senator John McCain (R.- Arizona) attempted to pass the Consumers Having Options in Cable Entertainment (“CHOICE”) Act in 2006 to mandate an à la carte model.\textsuperscript{47} The bill ultimately failed and cable prices continued to soar.

The Television Consumer Freedom Act (“Television Act”) is the latest bill introduced by Senator McCain and later supported by Senator Richard Blumenthal (D- Conn.).\textsuperscript{48} If passed into law, this bill would have the effect of providing significant incentives for cable distributors to offer channels on an à la carte basis.\textsuperscript{49} Senator McCain claims that the Television Act is strictly voluntary and would only provide incentives for cable companies to switch to an à la carte program.\textsuperscript{50} However, many of the provisions of the Television Act would effectively force many cable companies to adopt an à la carte type model. For example, the use of a cable compulsory license, which is key to many cable

\begin{itemize}
  \item \textsuperscript{43} See id.
  \item \textsuperscript{44} Stanley Besen & Robert Crandall, The Deregulation of Cable Television, 44 L. & Contemp. Probs. 77, 78 (1981).
  \item \textsuperscript{45} See Hazlett, supra note 16 at 254. When such rules were swept away in the “deregulation wave” of the mid-to-late 1970s, a cable “gold rush” ensued in which the country was wired for multi-channel video service. See Besen & Crandall, supra note 44.
  \item \textsuperscript{46} See Hazlett, supra note 16.
  \item \textsuperscript{47} Derek Thompson, Can John McCain Break Up the Cable Bundle Forever? (No, Probably Not), THE ATLANTIC (May 9, 2013), http://www.theatlantic.com/business/archive/2013/05/can-john-mccain-break-up-the-cable-bundle-forever-no-probably-not/275735/.
  \item \textsuperscript{48} Id.
  \item \textsuperscript{49} Joe Flint, John McCain Introduces Television Consumer Freedom Act of 2013, LOS ANGELES TIMES May 9, 2013, available at http://www.latimes.com/entertainment/envelope/cotown/la-et-ct-mccain-cable-20130509,0,2224732.story#axzz2m6qrtEjP.
  \item \textsuperscript{50} Id.
\end{itemize}
operations, would be stripped if a cable company refused to provide a la carte services.

c. **International Attempts: India and Canada**

Much of the arguments and research concerning cable bundling is purely theoretical rather than based on empirical data, because a truly unbundled cable system has yet to be seen on a large scale in the United States. The international evidence on switching to an a la carte system is also sparse, with only India and Canada implementing policies that reflect a true a la carte system on a national scale. Canada announced in October 2013 that they will start to implement regulations for cable de-bundling, and India currently requires that all cable companies provide an a la carte selection of channels.

India used to have a market for cable similar to the current U.S. bundled system, where consumers paid a monthly subscription for channels sold as a package. In 2007, India passed the Telecommunication Interconnection Regulation, which made it mandatory for all broadcasters to offer channels on an a la carte basis. After the passage of the act, several broadcasters mounted legal challenges, but the Indian Supreme Court ruled that the Act should be implemented because a la carte policy was in the public interest. By 2011, India had a multitude of private companies with a la carte options. However, in spite of the Regulation’s requirements, the multi-system operators do not offer channels a la carte. Instead, cable operators push add-on channel packages to increase the cost to the consumer. Since many cable companies simply refuse to implement an a la carte program, it is unclear what the ultimate effect of the new Indian Regulation will be for cable prices and consumer choice in India.

Concerns about cable bundling have also come to light in Canada. However, unlike in the United States, Canada’s government has already chosen to

51. The FCC reports and other economic models are based on theory and speculation. The FCC report uses subjective economic modeling, as does the social welfare report.
54. Id.
55. Id.
implement an a la carte system. Fueling this drastic change were Canadian politicians who, like American politicians, believe an a la carte system would allow citizens to only pay for channels watched. One Canadian television executive summed up the issue of government unbundling by stating that although the Canadian “government may be well-meaning, . . . they are badly misinformed about how things work in television.” Not surprisingly, this sentiment echoes American cable executive’s concerns.

Although Canada’s federal government recently told cable companies to unbundle their service packages, cable companies still have the obstacle of contracting around their content licenses. The Chief Marketing Officer of one cable provider claimed that “almost all” of his content licenses prohibited him from unbundling his cable programming. Although the existing content licenses may not be compatible with Canada’s aim to break the cable bundle, it is still possible that future negotiations with the content providers would reflect the new policies. Content providers usually negotiate with cable providers about once a year, and if this is the case, the content providers will likely be forced to comply with the Canadian government’s demands of the cable providers.

While Canada has mandated that cable companies unbundle their services, the free market has already created service providers that offer an a la carte system in Canada. One such company includes Eastlink, which unveiled its a la carte type system in the summer of 2013. The plan is called “Personal Picks,” and offers single digital channel selections beginning at a rate of $2.95 per channel per month. Another interesting feature about Personal Picks is that adding channels to the program can lower the cost per channel. One package includes 12 consumer-selected channels for $1.25 per month, and another package where 20 consumer-selected channels costs $1 a month per channel. Additionally, unlike

59. Id.
61. Id.
62. Id.
64. Id.
65. Id.
66. Id. The Canadian dollar is roughly equal to that of the American dollar. At the time of this publication, one Canadian dollar amounted to approximately 94 American cents.
other cable packages, Eastlink allows customers to bypass buying a theme pack. For example, instead of buying the entire 10-channel sports package, customers can simply buy the channel devoted to NHL programming.\textsuperscript{67}

In order for Eastlink to provide consumers with more flexibility, they negotiated with the content providers for the right to offer single selections of digital channels. Eastlink initially only started with a roster of 70 channels as of August 2013. In order to increase the roster of channels, they will need to negotiate further with the content providers. Rogers, another Canadian media company, previously offered the program in a select area of Canada, and claimed that the pick-and-pay pricing scheme was also popular.\textsuperscript{68} This experiment only lasted a few months, but there are plans to implement the program full time.\textsuperscript{69}

\section*{II. \textbf{Benefits and Negatives of A La Carte}}

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  \item \textbf{a. Possible Benefits of A La Carte}
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      \item \textbf{i. Social Benefits}

      One of the main arguments in favor of an a la carte system is that it allows consumers to receive and pay for programming they truly want. Arguably, the a la carte system would reflect what each household prefers to watch, rather than the current one-size-fits-all cable option. For example, a die-hard sports fan might want to purchase only the sports channels, while a law professor would likely purchase those channels that most frequently air Law & Order and other “realistic” legal programming.

      Some public interest groups suggest the a la carte debate is an issue concerning family values, since a la carte programming would allow parents to shield their children from the wiles of cable.\textsuperscript{70} The Parents Television Council and other consumer protection groups feel that there is “something fundamentally wrong with requiring consumers to pay for a product they don't want, and may

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\textsuperscript{67}. \textit{Id.}
\textsuperscript{68}. \textit{See Pedwell Supra 60.}
\textsuperscript{69}. \textit{Id.}
even find offensive, in order to get something they do want.”

For example, being forced to buy bundles that include shows like South Park, where characters are constantly cursing, doing illegal drugs, and making sexually explicit jokes, is the current reality for many parents. While it is true that current technology allows parents to block this type of programming, they are still in some sense subsidizing this offensive programming by purchasing the cable bundle.

A la carte programming could not only provide the protective parents of young children a tool to combat the low quality of programming, but could also have the market effect of increasing the proportion of quality programming. If the reason why high cable prices exist is because content providers want more money to create more quality content for consumers and to be paid for this content, maybe the best course of action is to have an a la carte system where channels with less viewership disappear. Even if the less popular channels vanish, the quality programming from these channels could still find a home on other channels. For example, during the height of its popularity, Breaking Bad on AMC had 10.3 million viewers. Even if the AMC channel discontinued operation altogether, another channel would almost certainly pick up such a valuable show, thereby increasing the average popularity of shows on the remaining channels.

ii. Potential Economic Benefits

An a la carte system could reduce the monopoly power of the content providers since each channel would have to compete individually, rather than as part of a bundle. Under the current scenario, each cable bundle effectively competes with other bundles. But by allowing channels to compete individually, less successful channels will most likely phase out. No longer will more popular channels like ESPN subsidize less popular channels, since every channel will stand independently. Content providers will face more difficulty in sustaining these less popular channels, and will have either enhance the quality of the programming or eliminate the channel altogether. By eliminating less popular channels that are not profitable, the content providers could invest their time and money into creating more popular shows, thereby spending more of their effort on programming consumers will watch and enjoy at higher rates.


72. Id.

b. Potential Negatives of A La Carte

i. Potential Social Costs

Although one of the main drivers for an a la carte program is parental concerns over raunchy programming on channels in current cable bundles, switching to an a la carte system would not necessarily shield children from inappropriate content. Broadcast television also has its share of raunchy material, from Family Guy often showing characters engaging in sexual activity to the reality show dalliances of The Bachelor. Additionally, one of the biggest snafus in television history — Janet Jackson’s Super Bowl halftime “wardrobe malfunction” — occurred on network television, not on cable.

Another potential social cost involves consumers lacking a complete view on what their preferences truly are, and the difficulty in projecting future preferences. For example, consumers might not realize how often they actually view certain channels. Someone might forgo buying the sports package if they do not generally watch sports often, but once a big game arises later in the season they may miss a game if they did not subscribe to that particular channel. Similarly, cable viewers will almost certainly be less likely to sample new shows on channels to which they do not subscribe, because they will not have access to those shows without paying an additional fee.

ii. Potential Economic Costs

While there are multiple reasons why an a la carte system might cause prices to rise even higher, the primary reason includes cable operators wanting to maximize profitability during decreased consumption. An a la carte pricing system would endanger cable operator’s revenue stream because people would likely purchase fewer channels.74 In order to maximize the profitability of such distribution, the cable companies would likely need to increase their prices per channel, if offered on an a la carte basis.75 For example, a cable provider who used to provide 100 channels for $100 under the cable bundling system would do everything in their power to maximize profits under the a la carte pricing. But under the a la carte system, if the cable providers truly pro-rated the channels by charging only $1 per channel, their revenue would plummet. Instead of pro-rating each channel, it is likely that cable companies would increase the price of each individual channel offered.76

74. See Hazlett, supra note 16.
75. Id.
76. Id.
Switching to an a la carte system also increases transaction costs to both the cable providers and consumers. Cable providers will experience increased transaction costs as a result of potentially having to negotiate with the content providers over each individual channel.\textsuperscript{77} The costs associated with the negotiation and information gathering would be much higher than if the cable provider engaged in only a single negotiation for each content provider. Additionally, cable providers would have to increase operational expenses for equipment and infrastructure, customer service operations, and billing and office support.\textsuperscript{78}

Consumers themselves will also likely experience higher transaction costs because consumers do not necessarily know what channels they might like unless they are already exposed to them. Under the current cable bundle model, cable users can simply flip through channels to see what their preferences are for a particular show. However, under the a la carte model, consumers will have to spend time tailoring their package in order to ensure all of their viewing needs will be met. The process of deciding what cable packages to purchase might currently take 5 to 10 minutes of a consumer’s time, whereas the process of selecting individual channels from a set of more than 100 may take hours.

While the transaction costs on the consumer and the cable company will rise, content providers will most likely experience the highest increase in transaction costs.\textsuperscript{79} This is because marketing costs will rise in order to gain the number of subscriptions necessary to sustain a profit. Currently, networks that are sold on an a la carte basis “spend a significant amount of their revenue marketing themselves to consumers.”\textsuperscript{80} Under an a la carte system, content providers who were under the bundle system would spend more money gaining customers. Some argue that this increase in marketing costs would then be transferred onto the consumer.\textsuperscript{81} However, if companies start charging more per channel under an a la carte system, it is likely that far fewer customers will subscribe to any given channel. Therefore the “the loss of cost savings, combined with the loss in advertising

\begin{footnotesize}
\begin{itemize}
  \item[79.] \textit{Id.} at 6.
  \item[80.] \textit{Id.}
  \item[81.] “We estimate that negotiated input costs rise by 103.0\% in equilibrium under à la carte. These are passed on as higher prices, offsetting consumer surplus benefits from purchasing individual channels.” Crawford and Yurukoglu, \textit{supra} note 77.
\end{itemize}
\end{footnotesize}
revenue and the likely rise in license fees to compensate such losses, may cause many program networks to fail, thus adversely affecting diversity."  

Although the marginal cost to the cable company of providing one additional channel is very low, there are generally fixed costs in providing cable service. For example, they need to hire salespeople, customer service, and then maintenance people who go out and install the cable equipment. The cable company also has to pay for the cable box and DVR, if applicable. All of these costs are high, but when divided by the number of channels provided to consumers nationwide, the costs are fairly low. Thus, this cost may be a relatively small percentage of the total cost of cable to an individual consumer when spread out over a 100-channel bundle, but if a customer only wants 3 channels it will raise the price to the consumer by a much larger percentage.

III. **How and When Should the Government Regulate?**

Government attempts to curb the cable bundle may be a poor solution to the rising cable bill since forcing cable providers to “offer” channels a la carte could cause cable prices to increase at exorbitant rates. In an effort to make prices lower, government regulation may have the unintended effect of increasing prices to consumers.

a. **Letting the Market Naturally Gravitate Toward A La Carte**

The research and background of the cable bundling model is speculative and there does not seem to be one definitively right answer. While the vast majority of studies seem to suggest that mandating an a la carte type program would increase cable bill prices, and cause less consumer choice, other studies (even one by the FCC) suggest otherwise. Considering that experts as a whole are uncertain about what the best model for cable should be, it may be best to simply let the market sort out any potential inefficiencies over time.

In addition to offering a la carte channels, an a la carte model can be extended even further by only offering specific shows, or even episodes. Many online viewing forums already engage in this a la carte model. For example, Amazon allows customers to buy specific shows, and in many instances particular episodes

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83. *Id.* at 7.
84. *Id.*
of shows. This model is frequently used when a customer has already seen the first or second season of a show, but because they missed the current season or latest episode on cable, they would like to purchase a particular season or episode of the show.

Additionally, private companies in Canada like Eastlink are already sprouting, and arguably incorporating an a la carte system more efficiently than if such a system had been regulated by the government.

b. Regulation May Decrease Consumer Choice

In an effort to increase consumer choice, the effect of government intervention may paradoxically to be decrease choice. As stated earlier, one likely effect of unbundling legislation would be the demise of the least popular channels and the consolidation of the most popular programming onto the most popular channels. However, this will necessarily lead to a decrease in programming options available to consumers, because only the more popular programming would likely survive an a la carte system.

Although consolidation of popular programming into a narrower range of popular channels might be seen by some as beneficial, it could have the effect of killing off socially valuable but niche channels and shows that may be relatively unpopular. For example, many viewers may be unwilling to pay for much of the educational programming on History or Discovery channels, but they may nevertheless watch the programming from time to time when included in a cable bundle. These channels, which could be at risk of dying under an a la carte system, may result in a more well-informed public under the current bundling system. Similarly, it is possible that parents may not fully consider their children’s viewing preferences when choosing what individual channels to purchase. However, channels that provide educational and interesting children’s programming may provide large social benefits. A bundling system avoids this problem so long as children’s programming is included as part of the basic cable bundle.

An a la carte regime, therefore, may ultimately decrease cable viewers’ quality viewing choices due to the decisions consumers made at the time they subscribed to individual channels. The extent of this effect is uncertain. It is

85. “Amazon has confirmed that the figure of 17,000 movies and TV shows cited for its Prime Instant Video service refers to individual streaming items, not titles. This means that TV shows have their individual episodes weighted as heavily as single movies, of which there are only 1,745.” Sam Byford, Amazon’s Prime Instant Video 17,000 movies and TV shows’ counts individual episodes, (April 13, 212) http://www.theverge.com/2012/4/13/2945267/amazon-prime-instant-videos-17000-counts-tv-episodes.
86. See Eastlink, supra note 63.
possible that consumers will do their research and purchase exactly the channels airing quality programming that they will want to view in the future. But another possibility is that consumers will be relatively uninformed in their decision making processes, and purchase only the most popular and well-known channels to the exclusion of other channels that may have been highly valuable to the consumers if they had done more research.

c. **Does Consumer Willingness to Pay Demonstrate Value?**

Households subscribe to cable if and only if the value they place on cable exceeds the retail price. Thus, consumers that remain subscribed to cable packages continue to value those packages at higher than the retail price. One economist commenting on this issue stated that, “[e]ffectively, the consumer subscribes to realize their individual preferences, and the cable company tosses in the additional channels for free. The practice is highly efficient. It dramatically reduces transaction costs and it prices marginal viewing choices at zero — exactly their marginal cost.”\(^87\) Other economic writers have expressed similar views.\(^88\)

Under this theory, consumers are not paying for the entire bundle, but only for the channels they want to watch. Despite its counterintuitive nature, this theory is well-reasoned as to the means of distribution of the channels, because as described above, the marginal cost to the cable company of providing an individual cable viewer with an additional cable channel is effectively zero.\(^89\)

d. **Parties Other Than Cable Companies Contribute to High Costs**

Considering that the reason why cable companies have to bundle is to keep content providers happy, it is possible that the problem may lie not with the cable providers, but with the content producers. Viacom owns many popular networks such as Comedy Central, MTV, and Nickelodeon. However, it also owns many less popular channels such as MTV2. Despite MTV2’s low viewership, 81 million U.S. homes receive MTV2 — that’s roughly 71 percent of all American households who purchase cable.\(^90\) The cost of creating content for MTV2 is not

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88. See, e.g., Yglesias, *supra* note 14 (“If you subscribe to basic cable and just four channels represent 95 percent of your viewing, then by definition what you’re paying for is *access to those four channels.*”).
89. One potential criticism of this theory is that it ignores the fixed cost to the content providers of producing content for the additional channels, and the subsequent fixed cost to the cable providers of purchasing the additional channel. Arguably, under an a la carte system, many channels included in cable bundles would cease to exist, which would reduce overall costs.
free. Viacom must offset its cost of programming for MTV2 by increasing its revenue. While this revenue can come from advertising, it also largely comes from the pockets of the cable providers who pay Viacom for its package of channels. Since cable companies must carry all of Viacom’s channels and not just the popular ones, they are must bear at least a portion of the increase in Viacom’s costs.91 This cost is ultimately transferred onto consumers’ cable bills.

In fact, one cable company, Cablevision Systems Corp., filed suit against Viacom in 2013 because Cablevision did not want to pay for channels with low viewership.92 Cablevision attempted to do exactly what consumers are advocating: pay only for the channels actually desired. It is currently estimated that Cablevision pays $38.8 million a year for 14 channels it doesn’t want, and only $76.8 million a year for the channels it does want.93 Cablevision claimed that Viacom wanted nearly $1 billion dollars if the cable company refused to pay for the low-rated channels.94 Instead of paying for channels like MTV2, Cablevision only wanted premium channels like Comedy Central, MTV, and Nickelodeon that drive revenue.95

Previously, Cablevision signed a long-term agreement to carry Viacom’s networks, which were estimated to cost over $115 million a year.96 Cablevision also claimed that these lower-rated shows were siphoning off bandwidth for channels that were more popular and for new, experimental channels.97 For example, Cablevision would like to launch other experimental channels such as Magic Johnson Enterprises’ ASPIRE, Retirement Living TV, and foreign language channels.98 Viacom, on the other hand wanted Cablevision to pay for a plethora of channels in which Cablevision was not interested. Cablevision argued that by broadcasting Viacom’s less popular channels, it was effectively barred

91. Id.
93. “SNL Kagan, which tracks cable fees, has estimated that Cablevision pays $38.8 million a year for the 14 channels it does not want, and $76.8 million a year for the eight it wants.” Jonathan Stempel, Cablevision: Viacom made $1 billion threat over bundling, (Mar. 7 2013), http://www.reuters.com/article/2013/03/08/us-viacom-cablevision-idUSBRE9261DR20130308.
94. “Cablevision Systems Corp is claiming that Viacom Inc sought to extract a nearly $1 billion penalty if it refused to pay for low-rated channels it did not want in order to access more popular channels such as Comedy Central, MTV and Nickelodeon.” Id.
95. Id.
96. Id.
97. Id.
98. Id.
from broadcasting other networks and shows that might ultimately prove to be more popular.

e. **How Should the Government Regulate, If It Must?**

If the government decided to intervene with the goal of reducing inefficiencies in the market, they should aim to regulate the content providers like Viacom rather than cable providers. After all, cable providers in Canada, where the government has already announced a la carte regulations, worry that they will still be held accountable to the content providers.\(^9^9\)

Effectively forcing cable companies to stop bundling may not solve the problem, since the cable companies would still have to find a way to battle the content providers who want to bundle and to get around the predicted increase in cable prices. Simply banning cable bundling would not necessarily make cable prices more affordable due to the economic models previously described. However, it is likely that banning bundling would give the cable companies the upper hand in negotiation with content providers, because content providers would be unable to realistically demand bundling when cable providers are legally prohibited from offering it.

Another alternative may be to discourage content overproduction through the use of tax incentives. For example, the government could add a small charge (say, between $0.10 to $0.50) per channel to the consumer’s cable bill. Such a tax would discourage cable companies from providing massive cable bundles, because consumers would be unlikely to pay the tax on a large number of channels they don’t want to watch. This would be a particularly attractive option if policymakers conclude that a large driver of cable costs is the production of low-quality programming for channels that few people watch, because the per-channel tax would provide a large incentive to consolidate quality programming into a smaller number of channels that would draw higher ratings. Simultaneously, it is likely that less popular channels such as MTV2 would be discontinued.

**IV. Future of Cable: Signs That an A La Carte World Already Exists**

It is also possible that the government will no longer need to regulate cable providers because cable prices will decline in the near future due to viewers

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switching from cable to internet viewing alternatives like Netflix and Hulu.\textsuperscript{100} Statistics such as the television industry reporting its worst 12-month stretch in November 2013 and the rise of Netflix and Hulu subscriptions seems to support this idea.\textsuperscript{101} Despite the decline in cable television subscriptions, 90% of American households continue to pay for a cable package.\textsuperscript{102} But continuing loss of cable customers could then shift the costs onto the remaining customers who are paying higher prices for bundles of television channels and high-speed internet access.\textsuperscript{103} Cable prices would likely decrease once the demand for cable dramatically declines in an attempt to retain viewership.

This decline in cable subscriptions could be another argument as to why the market is working to provide customers what they truly want and getting rid of the inefficiencies in the market. In January 2013 roughly a quarter of United States televisions already had their television connected to the internet, making it easier for consumers to watch shows on internet based content providers like Netflix, Hulu, and HBO Go.\textsuperscript{104} By the end of 2013 this figure is expected to rise to 30%, which represents 35.1 million US households.\textsuperscript{105} It is also expected that at least one person in each household will use the internet on that television on a monthly basis.\textsuperscript{106}

Accordingly, in this world of cable bundling, a growing contingency of consumers are nevertheless living in their own a la carte paradise. This group mainly consists of a younger generation where Netflix and Hulu are increasingly the main source of entertainment. This generation demands and largely receives high quality programming at an affordable price. Major networks like HBO have tried to jump on this a la carte trend by offering HBO Go, which allows customers to watch specific shows on demand. While Nielsen is indeed reporting a decline in television viewership among America’s younger generation, as of September

\textsuperscript{100} Jim Edwards, \textit{TV is Dying, and Here are the Stats to Prove It}, (Nov. 24, 2013) http://www.businessinsider.com/cord-cutters-and-the-death-of-tv-2013-11
\textsuperscript{101} Id.
\textsuperscript{104} eMarketer: \textit{A Quarter of US Households Now Have a TV Connected to the Internet}, (Jan. 3, 2013) http://www.emarketer.com/newsroom/index.php/emarketer-quarter-households-tv-connected-internet/#VxFBKFBSTA1LmL.0.99
\textsuperscript{105} Id.
\textsuperscript{106} Id.
2013 there has not a dramatic decline, and there are still millions of viewers glued to the cable television.¹⁰⁷

V. Conclusion

The best course of action for policymakers to address the cable bundle is likely to do nothing, sit back, and wait and see what happens next in the rapidly-evolving media landscape. Despite the widespread concern over the rampant practice of cable bundling, the evidence that the current market is significantly worse than it would be under proposed a la carte regulations is scarce. Government intervention could just as easily harm efficiency as promote it. If the much-maligned bundle is truly inefficient, new media platforms such as Netflix, Hulu, and HBO Go will likely necessitate a change in the cable market sooner rather than later.

¹⁰⁷ MarketingCharts Staff, Are Young People Watching Less TV? (Sept 10, 2013), http://www.marketingcharts.com/wp/television/are-young-people-watching-less-tv-24817/