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Regulatory Reform: The Telecommunications Act of 1996 and the FCC Media Ownership Rules

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Abstract

The Federal Communications Commission has regulated ownership of mass media outlets since the 1920s. The Telecommunications Act of 1996 abolished some of these regulations, changed others, and required the FCC to review its rules regularly and to repeal those no longer required.

There is little opposition to the idea that media ownership policy should promote economic competition (to increase the economic welfare of consumers) and First Amendment values (to preserve the political freedom of citizens).

This paper examines, from an economic perspective, federal administrative restrictions on ownership of media properties, including both antitrust and First Amendment policy bases for the rules. It concludes that the present rules are duplicative of antitrust law enforcement and should therefore be abolished as wasteful of public resources and a burden on consumer welfare. It argues that First Amendment goals are not threatened by abolition.

Keywords: mass media ownership, FCC media regulation, First Amendment policy, antitrust in media industries, Merger Guidelines, television broadcasting, radio broadcasting, newspaper publishing, cable television, horizontal concentration, vertical restraints, market definition, concentration measures, radio spectrum, scarcity doctrine.

The author is Gordon Cain Senior Fellow in the Stanford Institute for Economic Policy Research and Professor, by courtesy, of Economics, Stanford University.

Media Ownership

Bruce M. Owen[1]

I. Introduction

This Article examines, from an economic perspective, federal administrative restrictions on ownership of media properties. I review both antitrust and First Amendment policy bases for the rules. I conclude that the present rules are duplicative of antitrust law enforcement and should therefore be abolished as wasteful of public resources and a burden on consumer welfare. I argue that First Amendment goals are not threatened by abolition.

The Federal Communications Commission (Commission or FCC) has regulated ownership of mass media outlets since the 1920s. The Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (1996), abolished some of these regulations, changed others, and required the FCC to determine "…as part of its [biennial] regulatory reform review under [47 U.S.C. § 161] … whether any of such rules are necessary in the public interest as the result of competition. The Commission shall repeal or modify any regulation it determines to be no longer in the public interest."[2] The Commission's third biennial review, initiated in 2002, began a comprehensive re-evaluation of the rules affecting broadcast-

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1 Gordon Cain Senior Fellow in the Stanford Institute for Economic Policy Research and Professor, by courtesy, of Economics, Stanford University. This Article originated in invited remarks prepared for an October 2001 FCC Roundtable on Media Ownership (http://www.fcc.gov/ownership/roundtable.html; http://www.fcc.gov/realaudio/tr102901.pdf (Transcript of FCC Roundtable on Media Ownership Policies - 10/29/01)). A refocused version was later submitted in the FCC public record on behalf of several media companies (*Comments of Fox Entertainment Group, Inc. and Fox Television Stations, Inc., National Broadcasting Company, Inc. and Telemundo Communications Group, Inc., and Viacom*, MB Docket No. 02-277, January 2, 2003). The present final version was prepared for, but on account of scheduling conflicts not delivered at, the February 2003 Quello Symposium. I am grateful to Kent Mikkelsen and Michael Baumann for useful suggestions.

2 (47 U.S.C. §202(h)). The statutory language is not a model of clarity, and the meaning of the phrase "whether any of such rules are necessary in the public interest as the result of competition" has been subject to judicial interpretation. See note 4 infra.

ers.[3] This review was predicated, in part, on D.C. Circuit reversals of Commission actions in earlier biennial reviews.[4] While the FCC will likely have acted in its current proceeding by the time this Article is published, probable judicial review and further FCC proceedings will support the continued relevance of the analysis.

There are six rules under review in the third biennial. The first four rules relate to local markets while the last two are national in scope.

> * *The local TV station ownership rule,* 47 C.F.R. § 73.3555(b), provides that no one may own more than two TV stations in any one market and may own two only under certain conditions.
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> * *The local radio ownership cap,* 47 C.F.R. § 73.3555(a), provides that a firm may own up to eight radio stations in one market depending on the number of radio stations in that market.
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> * *The local TV-radio cross-ownership rule,* 47 C.F.R. § 73.3555(b), provides that a firm that owns only one TV station in a local market may own one, four, or seven radio stations in that market depending on not only of the number of radio and TV stations but also the number of cable systems and newspapers.
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> * *The broadcast-newspaper cross ownership ban*, 47 C.F.R. § 73.3555(d), provides that no one may own both a daily newspaper and either a TV or a radio station in the same market.
>
> * *The dual network rule*, 47 C.F.R. § 73.658(g), provides that a merger between firms that are among the top four television broadcast networks is not permitted, but a top-four network may merge with a network not among the top four.
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> * *The national TV station ownership cap,* 47 C.F.R. § 73.3555(e), provides that no company may own a group of television stations that, in the aggregate, can reach more than 35 percent of U.S. households. (There is no corresponding nationwide limit on the number of radio stations that any firm can own. The courts in 2001

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[3] Notice of Proposed Rule Making in the matter of 2002 Biennial Regulatory Review – Review of the Commission's Broadcast Ownership Rules and Other Rules Adopted Pursuant to Section 202 of the Telecommunications Act of 1996, MB Docket No. 02-277, released September 23, 2002.

[4] *Fox Television Stations, Inc. v. FCC,* 280 F.3d 1027, *rehearing granted*, 293 F.3d 537 (D.C. Cir. 2002), addressed the national TV ownership rule. *Sinclair Broadcast Group, Inc. v. FCC,* 284 F.3d 148 (D.C. Cir. 2002), *rehearing denied* Aug. 13, 2002, addressed the local TV ownership rule. These cases held that §202(h) carries a presumption in favor of repealing or modifying the ownership rules.

struck down the FCC rule limiting cable television MSOs to 30 percent of U.S. households.[5])

In reviewing these regulations policy analysis is required at several levels. First, what policy goals are at issue? Second, how should media ownership transactions be analyzed in light of these goals, and what standards should apply? Third, is this analysis best conducted case-by-case or reflected in a rule of general applicability?

It is not difficult to identify two broad social values at issue in media ownership policy. There is little opposition to the idea that ownership policy should promote economic competition (to increase the economic welfare of consumers) and First Amendment values (to preserve the political freedom of citizens). Of course there is room for disagreement on the specifics and on how to balance the goals to the extent they are in conflict. I will argue below that the goals are not in conflict, so that no tradeoff is required. On the meaning of First Amendment values, I accept for purposes of this Article the classical Western liberal position that decentralized, unregulated competition in the marketplace of ideas is a desirable prospect, and I reject the modern liberal position that the public has a right passively "to be informed" by the state, directly or through a state-engineered and regulated media industry.[6]

I believe that the economic aspect of media ownership concentration is best approached using the standard tools of economic analysis intended for such purposes. Analyzing the effects and measuring the extent of economic concentration is a well-developed field of economic policy analysis, especially in the context of antitrust enforcement. Whether

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5 In *Time Warner Entertainment Co. v. Federal Communications Commission*, 240 F.3d 1126 (D.C. Cir. 2001), the U.S. Court of Appeals for the District of Columbia Circuit struck down the Federal Communications Commission's cable ownership rules, 47 C.F.R. §§ 76.503-76.504, promulgated pursuant to §11(c) of the Cable Television Consumer Protection and Competition Act of 1992, 47 U.S.C. § 533(f)(1). The court applied a standard developed in *Time Warner Entertainment Co. v. United States*, 211 F.3d 1313 (D.C. Cir. 2000).

6 A defense of the modern liberal position may be found in Lee Bollinger, Image of a Free Press, Chicago, 1991. Statements of the classical liberal position may be found in John Milton's famous *Areopagitica: A Speech For The Liberty Of Unlicensed Printing To The Parliament Of England* (1664) and more recently in Lucas Powe, American Broadcasting and the First Amendment, Univ. of Calif. Press, Berkeley, 1987, and Matthew L. Spitzer, Seven Dirty Words and Six Other Stories: Controlling the Content of Print and Broadcast, Yale Univ. Press 1986.

ownership concentration poses harm to competition or to consumers is precisely the question upon which the antitrust laws and their enforcers focus.

The modern approach to analysis of ownership concentration is illustrated by the framework set out in the *DOJ/FTC Merger Guidelines* (Merger Guidelines or Guidelines). The Guidelines, while certainly not infallible, are widely respected by courts and commentators alike. The Guidelines describe methods by which the government can assess the impact of a proposed transaction. Also, the Guidelines offer the private sector a rational basis to predict the likely reaction of the authorities to a proposed merger or acquisition, thus reducing uncertainty and unnecessary transaction costs. In close cases, the Guidelines help to focus debate on the key factors affecting consumer welfare rather than on extraneous issues.

Very briefly, the Merger Guidelines require analysts to consider what products consumers view as alternatives for those produced by the merging parties, to define a "relevant market" consisting of such products, to measure concentration among sellers in that market, and to consider the ease with which other sellers could enter. The aim of the analysis is to assess the risk that consumers will be faced with price increases (or quality deterioration) as a result of the proposed transaction. In addition to an analytical framework, the Guidelines establish non-binding administrative standards (in terms of permitted levels of concentration, for example) for the exercise of prosecutorial discretion. In an antitrust context the purpose of the Guidelines is to provide the public with tools to predict the authorities' decision whether or not to bring a law enforcement action to stop any given transaction. As spillover effects, the Guidelines informally restrict the discretion of prosecutors and provide authoritative analytical guidance to courts both in deciding merger cases and in other areas of antitrust law, especially those where market definition is a significant issue.

Mass media compete in many different product and geographic markets. Some of these markets are ordinary commercial markets for the sale of advertising, the purchase of programming, and (in the cases of multichannel video program distributors, certain internet service providers, and print media) the compilation of content packages and the provision of transmission or delivery services for sale to consumers. For ease of reference I will refer to the foregoing as "economic" markets. These markets are addressed in Section II of this Article. The mass media also play an important role in the metaphoric "marketplace of ideas," which I discuss in Section III. I will bring the two types of markets together in Section IV.

A brief summary of my proposed approach to FCC media ownership policy is as follows: The most sensible way to consider the effects of ownership concentration in media economic markets is to use the Merger Guidelines approach. But if the Commission adopts this rational policy it will duplicate the work of the Antitrust Division, which would be a waste of public and private resources. The Commission also has monitored the effects of concentration in the marketplace of ideas. However, as a practical matter, enforcement of the Clayton Act in media economic markets will serve to prevent undue concentration in markets for ideas and information. As a result, there is no longer a rational basis for the Commission to regulate media ownership.

Rules versus case-by-case analysis

Rules (e.g., a ban on newspaper-TV station cross-ownership [ownership of a cross is still permitted) conserve public and private resources, but at the cost of increased Type I and Type II errors.[7] Rules also increase predictability. Case-by-case analysis reduces errors, but is more expensive for regulators and applicants.[8]

The Commission's traditional ownership policies might be justified on the basis of what is called "judicial economy." For example, the nature and definition of local advertising markets might be so well-established through prior experience, and the appropriate standards necessary to prevent mergers or natural concentration from harming consumers or advertisers might be so well-understood, that a general rule would save everyone in-

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7 These errors correspond respectively, here, to incorrectly permitting the harmful and to incorrectly forbidding the beneficial.

8 The common law process can in principle be inexpensive if there is *stare decisis* and a sufficient body of applicable precedent. In the present context, with rapidly changing technology and market arrangements, new fact issues will have to be analyzed.

volved from wasting time and effort on case-by-case analysis, even at the cost of some small errors.

It makes sense to have rules, perhaps with waivers, when the outcome of nearly every case can be readily predicted on the basis of easily ascertainable facts. For example, thirty years ago only 2.7 percent of U.S. cities with a daily newspaper had more than one such newspaper. Similarly, most cities had no more than three significant commercial TV stations. A merger between the newspaper and one of the TV stations in these cities would almost certainly have increased concentration significantly in local advertising markets, however broadly defined. In those circumstances, a rule banning such cross-ownership was likely more efficient than repetitive case-by-case analysis. Today, the relevant facts vary significantly across local markets, and a rule-based approach is no longer appropriate.

When facts differ significantly from one transaction to another, a case-by-case approach is likely to be superior to a rule if it employs analytical tools that are well-defined and easy to understand. If prospective applicants understand these tools, they can model the agency's decision process. This increases predictability and, presumably, reduces the number of applications likely to be rejected. The Merger Guidelines are again a very useful model of such a tool.[9]

[9] In spite of the Guidelines' state-of-the-art analytical framework, there might be pragmatic reasons to reject the use of traditional antitrust enforcement *standards* in media industries. Imagine, for example, that empirical studies by the Commission demonstrated significant adverse effects on the price of advertising in local media markets when HHI levels exceeded 800. That might justify the Commission's use of 800 rather than 1,000 or 1,800 as a safe harbor, or it might justify an ownership cap at 800, depending on the nature of the empirical findings. The Merger Guidelines standards are of general applicability. Their numerical values, frankly, are arbitrary. Certainly they are not necessarily appropriate for every industry. As it happens, there is no evidence that a special standard is required for broadcasting and related industries.

II.

Ownership Issues in Economic Markets

There is nothing in the Constitution about competition. Competition is simply a socially useful process for allocating resources. Experience has shown that competition, even if imperfect, generally produces greater and more reliable benefits for consumers than the alternatives. The alternatives include not only monopoly but regulated monopoly, regulated competition, central planning, and collectivization. Based on this pragmatic approach, free markets are desirable policy objectives when they are burdened neither by monopoly nor by regulation. Free markets are an inferior choice when they are so imperfect that even flawed regulation produces better results.

Every free market produces not just a set of outcomes measured in terms of prices, outputs, productivity, technological progress and so on, but also a "natural" market structure. In some cases the natural market structure is rather concentrated. In the extreme it can even be a so-called "natural monopoly." Traditional antitrust (and especially merger) policy seeks to prevent concentration when it is not "natural." Economically sound antitrust enforcement seeks to stop mergers that will tend to reduce consumer welfare by raising prices and to prevent monopolies from arising for reasons *other* than a superior ability to benefit consumers.

FCC ownership policies such as ownership caps and cross-ownership rules appear to accept the idea that competition is desirable. However, such rules implicitly reject the sufficiency of the antitrust approach I have just described. More specifically, the ownership rules reject certain natural market outcomes, even those that are not the result of mergers. What lies behind this choice?

It would be accurate to say that a principal basis for the Commission's historical media ownership policies has been the assumption that "natural" market outcomes would produce insufficient diversity of content or sources or ease of access to the media. And hiding just beneath the surface of the diversity principle has been the more ancient notion that the radio spectrum, as a nationalized resource, should be shared "fairly" among its various claimants. This tension nicely illustrates the conflict between the modern liberal view that fairness should be a paramount goal of resource allocation and the classic view that the chief goal of allocation should be to maximize overall output and its growth rate.

Lurking deeper still in the political roots of the ownership policies is elected (and appointed) officials' genuine fear of their own vulnerability to the popular media. None of the Commission's historical ownership policies can possibly be regarded as growing out of the economic analytical approach embodied in today's Merger Guidelines methodology. And it is the Merger Guidelines *methodology* (even if not the particular standards) that defines rational policy in this area.

There are indeed economic characteristics of media content that make it difficult to presume that a competitive market outcome is necessarily optimal. Half a century ago Peter Steiner made the point that some listener demand structures would be better served by a radio monopolist than by radio competitors. Later work by Michael Spence and others has generalized this finding. It is fair to say, today, that the public good character of programming is one of many flaws that impair the functioning of competitive media markets.[10] Nevertheless, no one has identified any practical intervention by which the government could reliably improve this situation, certainly not by ownership rules.

Horizontal Ownership Issues

The analytical tools of competition analysis, as used in antitrust enforcement, apply directly to the Commission's concentration concerns in media economic markets such as advertising and programming. The three key questions facing the Commission with respect to each of these markets are: Which sellers offer choices that customers find attractive? Are there enough such sellers to provide effective competition? Are there significant barriers to entry? These are the same issues addressed in the Merger Guidelines. Indeed, the antitrust agencies already routinely apply Guidelines analysis to proposed media transactions involving radio, television, newspapers, magazine and book publishers,

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10 The models developed by Steiner, Spence and others are described in detail in Bruce M. Owen and Steven S. Wildman, Video Economics, Harvard Univ. Press., 1993.

online and other media. A very recent example is the challenge mounted by the Department of Justice to the proposed acquisition by EchoStar of DirecTV.[11]

The analytical approach of the Guidelines begins with a focus on consumers. Whether a proposed merger or acquisition is anticompetitive is determined in part by asking what alternatives are, or would be, available to customers in the event that prices were to increase or service deteriorate. These are fact questions. They must be addressed from the perspective of particular, defined customers who are users of the services of the firms that propose to merge and competing firms. This determination of relevant market(s) cannot be prejudged in today's complex and changing media industries by establishing arbitrary *a priori* boundaries.

Similarly, it makes no sense to define either markets or ownership standards *a priori* in terms of particular technologies, such as radio broadcasting, television broadcasting, cable transmission or newspaper publishing, much less AM versus FM or VHF versus UHF unless such distinctions happen to coincide with accurate depictions of consumer demand characteristics. Neither technology nor the Code of Federal Regulations (C.F.R.) categories are based on or bear any useful relationship to customer behavior in media markets, as the Commission's own evidence amply demonstrates.[12]

The Commission's current (2002) ownership rules are based entirely on implicit "market definitions" reflecting technology and other such *a priori* distinctions. For example, the local radio ownership rules imply a "market definition" consisting solely of local radio stations and a concentration standard measured in numbers of local radio stations. If the Commission were concerned with protecting advertisers from the possible effect of radio ownership changes on ad rates, it would consider what alternatives advertisers have to radio advertising. In setting a concentration standard for this purpose, probably it would

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[11] Both companies deliver multichannel video entertainment and Internet access services to consumers via domestic broadcast satellites. See Complaint, *United States, et al. v. EchoStar Communications*, et al., Case Number 1:02CV02138 DDC *Complaint* filed October 31, 2002. http://www.usdoj.gov/atr/ cases/f200400/200409.htm

[12] http://www.fcc.gov/ownership/studies.html (FCC-sponsored studies in the third decennial proceeding).

use advertising revenues, not the number of stations. The present approach makes little sense. Technology-based distinctions today lack any conceptual or empirical link to consumer harm from ownership concentration. In a business with such rapidly changing strategies and technologies, in which consumers have demonstrated their willingness to adopt new media, it makes no more sense to legislate market definitions in quasi-permanent rules than for King Canute to order away the ocean's waves.

If the Commission adopted sound media ownership policies, i.e., policies based on analytically meaningful distinctions such as those found in the Merger Guidelines, it would necessarily duplicate the work of the Antitrust Division of the Department of Justice and the Federal Trade Commission.[13] As the recent EchoStar matter demonstrates, when the Commission applies sound economic principles to the analysis of proposed acquisitions, it ends up with essentially the same result as the Department of Justice both in terms of analysis and in terms of standards (compare the DOJ complaint with the Commission's Hearing Order in the EchoStar matter.)[14] Clearly, such duplicative regulation is inefficient, a waste of public and private resources.

Efficiencies

Efficiencies are cost savings or other potential sources of increased economic welfare resulting from a merger. A weighing of efficiency gains against potential anticompetitive effects is a part of the Merger Guidelines case-by-case analysis, at least in principle. (In practice the antitrust agencies regard efficiency claims with considerable suspicion, although the Commission need not.). The problem of course is that any "natural" market

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[13] Mergers and like transactions must be reported to and reviewed by the antitrust agencies if they exceed certain size thresholds. A small fraction are challenged; those that are not challenged go forward after the expiration of the review period., but in theory may be challenged later. The antitrust agencies retain jurisdiction to challenge non-reportable transactions. The Commission normally must affirmatively approve any license transfer, no matter the amount of consideration.

[14] Perhaps sensitive to the issue of wasteful duplication of effort, the Commission did attempt to distinguish its method of analysis. *In the Matter of Application of EchoStar Communications Corporation*, (a Nevada Corporation), General Motors Corporation, and Hughes Electronics Corporation (Delaware Corporations) (Transferors) and EchoStar Communications Corporation (a Delaware Corporation) (Transferee) HEARING DESIGNATION ORDER, CS Docket No. 01-348 FCC 02-284 Released: October 18, 2002. http://hraunfoss.fcc.gov/edocs_public/attachmatch/FCC-02-284A1.pdf

concentration reflects a triumph of efficiencies over market power. In the extreme, a so-called natural monopoly is able to deliver goods to consumers at a low price because its economies of scale more than offset its monopoly pricing. Antitrust policy attacks such a firm only if its market power is abused. An ownership rule imposed by the Commission must reflect a judgment that the net (of any market power costs) consumer benefits of the natural level of concentration are worth sacrificing to other policy goals. It might be sensible to insist that any such judgment be based in part on a quantitative assessment of the lost consumer benefits. Even if the other goals cannot be quantified, at least we would know how much we are paying to achieve them.

As it happens a concrete example of the "unnatural" and thus costly outcomes of Commission ownership policy is at hand. Before the 1996 Telecomm Act, the FCC strictly limited the number of radio stations that could be owned by a single entity in any one market as well as the total number of radio stations that a single entity could own in total across the country. The Act eliminated the national cap and the FCC eased the local cap. The result has been a significant consolidation of radio station ownership. (At one point, no person was permitted to own more than seven AM and seven FM radio stations. Today, the largest station group owns some 1,100 stations.) No one would argue that radio stations in different markets compete, so joint ownership of such stations portends no monopolistic profits. The only reason for joint ownership is cost savings. The consolidation that has taken place thus implies that the former FCC rules imposed significant costs on society. Nevertheless, it would have been very difficult to demonstrate the existence of such potential efficiencies convincingly in advance of the consolidation.[15]

Vertical Ownership Issues

The last area I will touch on has to do with ownership policies aimed at vertical markets. The national cable ownership cap, for example, cannot possibly have any economic basis

[15] However, radio mergers have often brought stations in the same market under common ownership. In principle, the motivation for these mergers may have been to increase concentration in local markets. In practice, the Department of Justice has been very active in reviewing such mergers. Consequently, it is reasonable to assume that the acquisition of market power in local advertising markets has not motivated the mergers.

other than to prevent the exercise of market power in purchasing programming or to prevent the preservation of market power by denying programming to rivals.

The theory that monopsony problems might arise if a sufficiently large concentration of media outlets were permitted is a respectable starting point for an argument leading to an ownership cap. After all, this was the basis for the decision at the time of the breakup to have more than one local phone monopoly arise from the dissolution of AT&T. But a necessary first step, as always, is market definition. In this case, we need to ask whether program suppliers or the inputs they employ have other ways to reach the audience served by the outlets in question. Clearly, if the answer is yes, an ownership cap makes no sense. Also, unlike telephone switch gear, programs are public goods.[16] A buyer with market power has no incentive to restrict purchases of a given program in order to reduce the price it pays. The effect of restricting purchases will be to *increase* the unit price for the units the MSO still purchases, holding constant the quality of the programming.

So-called "program access" rules are based on a very similar theory of vertical restraints. The 1992 Cable Act contained a provision, retained in the 1996 revisions of the law, requiring cable television companies with ownership interests in satellite-distributed programming to make the programming available to rivals such as DirecTV and EchoStar. I suppose someone might construct an infant-industry story justifying such a rule, although it would have to be premised on evidence that integrated cable owners *would* engage in discrimination or exclusive dealing, that new satellite broadcasters *lacked* access to attractive programming from other sources, and that consumers *would not* be better off with differentiated programming. But no one has put forth such a theory or gathered such evidence, and anyway satellite broadcasting clearly has passed beyond the infant industry stage.

So long as the program access rules stay in place (the Commission in June 2002 declined to permit them to sunset) they reduce the incentive of cable owners to invest in marginal

[16] A public good is not used up when it is "consumed." For a given quality level, its production costs are fixed, and providing the good to an extra consumer costs the producer nothing. Contrast an automobile tire with a video production. A tire sold to consumer X cannot be sold to consumer Y. Producing a tire for consumer Y requires the producer to incur significant costs. A video production can be sold to both consumers, or all consumers, with no increase in production cost.

new programming sources, exactly the enterprises most likely to widen content diversity. By offering satellite services the opportunity to free ride on the investments of others, the rules also discourage the newer entrants from offering differentiated products to their subscribers, potentially reducing consumer welfare.

II.

The marketplace of ideas and information

> *And though all the winds of doctrine were let loose to play upon the earth, so Truth be in the field, we do injuriously…to misdoubt her strength. Let her and Falsehood grapple; who ever knew Truth put to the worse, in a free and open encounter?* —John Milton, Areopagitica[17] (1664)

The preceding section demonstrated that a rational policy approach to media ownership in economic markets requires the Commission to leave these enforcement issues to the antitrust agencies, or at least to employ the same tools as those used by the antitrust agencies. I now turn to whether the Commission's traditional concern with competition in the marketplace of ideas and information, sometimes expressed as pursuit of "diversity," provides a better basis for the Commission to regulate media ownership.

The Commission does have a stronger basis for attending to the marketplace of ideas than to mass media economic markets. After all, while DOJ has vigorously enforced merger law with respect to media economic markets, it has not, in practice, addressed competition in the marketplace of ideas. Further, it is possible in principle (though as I argue below, unlikely) that a given transaction might raise marketplace of ideas issues despite the absence of threats to competition in the relevant economic markets. Therefore it is useful to develop a rigorous framework that the Commission could use to prevent ownership concentration from restricting competition in the marketplace of ideas.

The place to start is with the slippery concept of "diversity," which has many interpretations, as discussed in the Commission's Notice of Proposed Rulemaking (NPRM) at ¶33ff. I will focus on two of these interpretations: content diversity and outlet diversity.

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[17] John Milton, *Areopagitica: A Speech For The Liberty Of Unlicensed Printing To The Parliament Of England* (1664)) http://www.uoregon.edu/~rbear/areopagitica.html. Whether Milton was right or not is a different question.

Content diversity is not a reasonable goal for the Commission. If the Commission were to target media content that would be an *unnecessary* infringement on the First Amendment rights of broadcasters. It would also be *impractical*.

Mass media content is an impermissible target of government regulation, according to the Supreme Court's current interpretation of the First Amendment, except in certain narrow categories such as obscenity. Broadcasting is the only medium to which this interpretation does not apply. The inferior First Amendment status of broadcasting derives from a legal analysis in a 1943 Supreme Court opinion by Justice Frankfurter (and later confirmed in *Red Lion*).[18] The factual basis of the legal argument is spectrum scarcity.

The "scarcity doctrine" is and always has been a factual and economic absurdity. Economics is the science of scarcity. It teaches that spectrum is no scarcer than anything else used as an input by broadcasters. Spectrum is no scarcer than the land used to grow the trees that are made into newsprint. Anything that has a non-zero free market price is, by definition, scarce—there isn't enough to satisfy everyone's wants. The point simply is that spectrum is not scarce in any peculiar or special way—it is no more or less fixed in supply than land, iron ore or antenna sites. All these things are scarce, but all can be economized upon by using more of complementary inputs to produce any given output. Antenna height is a substitute for site altitude. Font size and leading is a substitute for newsprint, hence for trees and forests. Transmitter/receiver power and data compression are substitutes for bandwidth. For Justice Frankfurter to have focused on spectrum scarcity as a special or unique aspect of broadcasting that justifies denying broadcasters equal protection under the First Amendment was bad economics in 1943 and it is worse economics today.

Broadcast spectrum in particular is exactly as scarce as the Commission, through its own policies, has made it. Over the years the Commission has repeatedly restricted the frequencies available for broadcasting in order to serve other policy interests, thus limiting

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18 *National Broadcasting Co. v. United States*, 319 U.S. 190, 219 (1943) http://caselaw.lp.findlaw.com/cgi-bin/219. *Red Lion Broadcasting Co. v. FCC,* 395 U.S. 367 (1969) http://laws.findlaw.com/us/395/367.html.

the diversity of programming available to viewers and listeners.[19] It is circular logic to hold that the Commission can regulate broadcast content because the Commission has chosen to restrict the spectrum available for broadcasting. Spectrum scarcity has never made sense as a *factual* basis for broadcast regulation. (These arguments are laid out in more detail in my book *The Internet Challenge to Television* (Harvard Univ. Press, 1999) at 57-62 and 79-83.)

Even if there had been spectrum scarcity at the time of *Red Lion*, technological developments have long since eliminated that scarcity. Almost twenty years ago the Supreme Court itself recognized the possibility "that technological developments have advanced so far that some revision of the system of broadcast regulation may be required." *FCC v. League of Women Voters*, 468 U.S. 364 (1984)) at n. 11. The Commission's own Spectrum Task Force Report recently acknowledged that "[a]dvances in technology create the potential for systems to use spectrum more intensively and to be much more tolerant of interference than in the past," and even more significantly that " [i]n many bands, spectrum access is a more significant problem than physical scarcity of spectrum, in large part due to legacy command-and-control regulation that limits the ability of potential spectrum users to obtain such access."[20] The factual underpinning of the scarcity doctrine is no longer able to bear its weight. *Stare decisis* cannot make nonsense into fact. Therefore, for all these reasons, the inferior First Amendment status of broadcasters is an *unnecessary* burden on freedom of the press.

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[19] The Commission restricted diversity, ostensibly to serve the cause of localism, in *Amendment of Section 3.606 of the Commission's Rules and Regulations; Amendment of the Commission's Rules, Regulations and Engineering Standards Concerning the Television Broadcast Service; Utilization of Frequencies in the Band 470 to 890 MCS for Television Broadcasting, Sixth Report and Order,* Docket No. 8736, 41 F.C.C. 148, 1 RR 91:559 (1952). The Commission later declined to "deintermix" VHF and UHF frequency assignments in local TV markets, perpetuating artificial scarcity at the local and national level. Similarly, the Commission delayed the use of digital broadcasting methods, thus denying viewers the benefits of increased competition and diversity through digital compression technology. Through its distant signal importation and anti-siphoning rules, the Commission delayed for years the increased competition and diversity now provided by cable networks.

[20] FCC Spectrum Task Force Report, ET Docket No. 02- 135, November 2002 at 7. http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-228542A1.pdf

Further, content diversity is an *impractical* policy target because it cannot be defined or measured, and because there is no analytical linkage between ownership concentration and even abstract concepts of content diversity. In one theoretical model, for example, a monopolist of three channels is predicted to produce more content diversity than three competing broadcasters (See Bruce M. Owen and Steven S. Wildman, *Video Economics,* (Harvard Univ. Press 1993) at 64-100.) In contrast, even "complete" freedom of expression (defined as the availability of universal communication services at zero cost to all speakers and consumers), need not necessarily result in any particular degree of content diversity. Complete freedom in practice might produce no diversity of content. It is the tastes and demands of audiences, not the wishes of broadcasters, that determine the extent of content diversity in a competitive marketplace. I conclude that content diversity is not a sound policy objective for the Commission.

The Commission's traditional concerns with diversity make sense only if diversity is understood as synonymous with what it terms outlet diversity. The difficulty with establishing sound ownership policies and non-arbitrary rules with respect to outlet diversity has been the absence of a rational analytic framework for doing so. Although the "marketplace of ideas" is but a metaphor, I believe that outlet diversity issues can usefully be approached by taking the competition metaphor quite literally.

The goals of freedom of expression and an informed public are best served by ensuring that the media have incentives to respond to consumers' demand for ideas and by eliminating artificial or unnecessary barriers to the transmission of new ideas. Equivalently, the Commission should seek to minimize the price (and thereby maximize the output) of the communication and compilation services provided by media outlets. This can be achieved by pursuing economic competition and minimizing barriers to entry among communication media.

Just as competition, backstopped by antitrust policy, works to ensure that the interests of consumers are served in economic markets, competition is the best protection for consumer access to ideas and information. Media, competing against each other for audience "eyeballs" and consumer and advertiser dollars, will be led "as if by an invisible hand" to serve the public interest in promoting First Amendment values. None of the economic models of broadcast competition supports the notion that the government can reliably improve on competitive market outcomes.

If the Commission does undertake to promote the free flow of ideas through competition, it cannot do better at present than to utilize the rigorous analytical framework reflected in the Merger Guidelines. That framework is aimed at preserving competition by preventing even incipient threats to consumer welfare from ownership concentration. The Commission itself can apply Guidelines principles to the analysis of competition in the marketplace of ideas. As with economic markets, the keys are to identify the outlets for ideas to which a particular group of consumers can readily turn in the event its current supplier(s) raise price, lower quality or otherwise prove unsatisfactory, and to assess ease of entry by new outlets. Building on these facts, the Commission could determine whether a proposed merger or acquisition would unduly reduce competition. Of course, as with any analysis of competition, it is necessary to take account of the particular facts and circumstances in the market, and to have objective standards.

Market definition is the first step in the competitive analysis. What alternatives do consumers have if they are faced with increased prices or reduced quality in the media used to convey ideas? As with economic markets, which alternative outlets should "count" is largely a fact question derived from analysis of consumer demand and entry conditions. It cannot be prejudged based on the technology or format of a given medium, especially in light of the dynamism of today's media markets and technologies, for the reasons given in the preceding section.

A key distinction between most economic markets and the marketplace of ideas, however, lies in the measurement of market shares. The Commission would commit a serious error if it attributed shares in the marketplace of ideas according to the current revenue or audience shares of individual outlets. The measurement of market shares must always reflect the underlying theory according to which increased concentration may bring harm to consumers. Thus, in economic markets, competing firms' shares of revenues in the relevant market often have great significance in understanding the likely effect of a proposed merger on customers. This is so because revenue market shares influence pricing incentives.

In the marketplace of ideas, however, what matters is the number of alternative information outlets available to consumers, not the current popularity, much less the technology of transmission, of the ideas communicated by each outlet. Each source of ideas available to a given consumer is equally significant from a First Amendment perspective. The rational way to measure the "share" of each source of ideas available to a given set of consumers, therefore, is to give each source equal weight. It is availability and not usage of alternatives that should count, because it makes no sense to view the Commission's role as regulating the popularity, as opposed to the availability to consumers, of ideas and information. It is unpopular new ideas that may be of the greatest importance to the future. Such unpopular ideas are the essence of diversity in the marketplace of ideas. To discount media that are available to all, but that garner small audiences because consumers prefer other content, would understate the level of diversity from the perspective of any coherent public policy theory of the *purpose* of promoting diversity. It would be remarkable indeed for the Commission to adopt an ownership concentration metric that implies, as a social ideal, that all ideas should be equally popular.

Moreover, unlike economic markets, the usage of particular media, technologies or channels has no incentive effect on media owners when it comes to possible suppression of ideas. The Guidelines themselves (at §1.41 and n. 15) specifically contemplate the possibility that, in circumstances where current revenue market shares are misleading indicators of competitive significance in economic markets, equal shares should be imputed to each competitor.

The Framers were of course concerned chiefly with official attempts to suppress dissenting political and religious views. It is difficult to conceive of politically or socially significant ideas that can be expressed only through a particular medium. While the effectiveness of each medium may vary from one idea to another, the key is that ideas, once released to the public, can no longer be suppressed or controlled by government or commercial interests. The truth of this assertion is reinforced by the great importance of

Katz's and Lazarfeld's discovery that interpersonal communication with friends, family and co-workers, and opinion leaders dominates in the diffusion and acceptance of ideas.[21] It makes no sense to say that a particular media outlet that has a large audience controls access to that audience, unless members of that audience are inaccessible to other media. But audiences are accessible to many media and many media are accessible to audiences. In short, the audience of a media outlet is unrelated to that outlet's significance in the marketplace of ideas. Every outlet available to the community has equal potential as a source of ideas.

The preceding important point can be made in a somewhat different way. Imagine that there are fifty independent media outlets serving a given community. Each outlet chooses the ideas and information that it will convey, based on a desire to maximize profit given advertiser and subscriber demands. Some outlets will have larger audiences and revenues than others, based on competitive interactions. The outlets with the largest audiences will not necessarily be the most profitable, because some niche outlets serving up relatively unpopular ideas to minority tastes may face less intense competition than those outlets seeking mass audiences. (By "unpopular" I mean simply that the idea or outlet attracts small audiences.) However the competitive process works itself out, the accessibility of the community to new and therefore by definition initially unpopular ideas clearly is a function of how many outlets there are, not on how many outlets currently have large audiences. Indeed, new ideas are far more likely to be aired at first by the media with *smaller* audiences. Once a new idea is available to the community, either directly through each consumer's access to an unpopular outlet or indirectly through interpersonal communication, its diffusion cannot be prevented whether or not the idea is adopted by more popular media.

A question remains as to whether the effective operation of media markets from a political point of view requires a different, stricter, competition standard than would be applied to advertising markets. For example, while an HHI as high as 1,800 might be regarded as

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21 Lazarsfeld, Berelson and Gaudet's conducted research on the role of media messages in opinion formation during the 1940 Presidential election. *The People's Choice, 1944.* Lazarsfeld later developed the "two-step" model of media messages, a process in which opinion leaders play a vital role. See Katz and Lazarsfeld, *Personal Influence* (1955).

tolerable in a relevant market for advertising, should we regard it as tolerable in a relevant market for the expression of ideas?

An immediate problem with this question is that HHIs based on revenue or audience shares measure outcomes, not ease of access. Even a commodious common carrier medium with trivial transmission prices might display a very high HHI among program suppliers, simply because society's tastes produce that result. Popular culture is, by definition, popular. *Ex post* equilibrium HHIs say nothing useful about *ex ante* freedom of expression. It is hard to make economic sense of a policy objective based on ensuring the economic success of unpopular and hence unprofitable messages.

It is reasonable to ask whether "ideas" may not be too broad a definition of the relevant market. Ideas or information about what? It is clear upon reflection that any taxonomy of ideas and information likely would be arbitrary from a competition perspective.

By *arbitrary* I mean that there is no principled basis for a taxonomy of ideas in this context. Even if there were, there is nothing to prevent a new idea from arising in one category and yet having important or even revolutionary implications for other categories. The Commission wisely does not attempt to define its policies with respect to particular categories of ideas—with one exception. The exception is the Commission's longstanding preoccupation with local content.

In its most basic historical decisions regarding the allocation of broadcast spectrum, the Commission expressly sacrificed consumer breadth of choice in order to promote local ownership and "therefore" local content. It turns out, of course, that local ownership, while it *permits* local content, does not often *result* in local content.[22]

The Commission's preoccupation with localism is difficult to explain or to justify. Why should the government seek to promote local content as opposed to, and especially at the

[22] Given a fixed bandwidth allocated to broadcasting, the number of channels available to the average consumer is maximized if all stations are "national." If local stations are to have the option to include local content, then local stations must be protected from interference by limiting stations in nearby cities to different frequencies. This reduces the number of channels available to the average consumer.

expense of, any other category of ideas? One can readily imagine categories of programming more central than locally-produced programs to the political, social, educational, aesthetic or spiritual lives of Americans. Further, to fasten on any category of ideas readily runs afoul of First Amendment values. For example, dissenting national voices might be discouraged by forcing them to speak through numerous local outlets. In short, a focus on local content or local outlets appears to lack a coherent policy basis.

The same is true, of course, of the Commission's sometime preoccupation with news and public affairs, as distinct from entertainment programming. This makes even less sense than localism. First, broadcast news *is* entertainment—it has to be, at least in part, in order to attract audiences that can be sold to advertisers. One need look no further than this to understand what "stories" are "newsworthy." Second, surely some of the most effective of media vehicles for the communication of ideas are classified as entertainment. One could reasonably argue that a given consumer is more likely to be exposed to a controversial idea by a talk radio show or an Internet newsgroup than by either network or local television news.

I conclude that independently-owned outlets for, or sources of, ideas and information generally should each be counted equally as separate sellers in the marketplace of ideas, with respect to the consumers whom they can reach (or the consumers who can reach them), without regard to the classification or popularity of their current content. If the Commission wishes to continue to emphasize local content (notwithstanding the apparent lack of a rational basis for doing so), then the sellers in the relevant market include all independently-owned outlets for or sources of local ideas and information, again without regard to the classification or popularity of their current content.

III.

Competition in economic markets will protect competition in the marketplace of ideas

As a practical matter competition in "economic" media markets, backed by effective DOJ enforcement of the Clayton Act, likely will be sufficient to ensure competition in the marketplace of ideas. There are three reasons for this. First, markets for ideas are much broader than corresponding economic markets. DOJ, for example, has traditionally focused on extremely narrow advertising markets, stopping threats to economic competition long before consolidation poses a threat to competition in the marketplace of ideas. Second, relevant markets for ideas are less concentrated than narrowly-defined economic markets served by given outlets because of the way that shares are measured. Third, entry in the marketplace of ideas is far easier than in economic markets because ideas (especially unpopular ones!) can be introduced at much smaller scales of operation.

For these reasons it is not correct to view the Commission's responsibility to protect First Amendment values as requiring a lower tolerance for concentration than that required by antitrust principles. Indeed, the analysis suggests that the Commission could safely (from a marketplace of ideas perspective) adopt a more tolerant standard, especially if it was concerned about impeding technological progress or handicapping licensees in their competition with non-licensees, and thereby harming consumers.

Merger enforcement in the media has tended to focus on rather narrow advertising markets. DOJ in recent years has chosen to exclude television and newspaper advertising as alternatives to radio when considering advertising market definition in radio station mergers. It has similarly rejected television and radio advertising as alternatives for newspaper advertisers when considering newspaper mergers. In the EchoStar matter, both DOJ and the Commission identified relevant markets for MVPD services, excluding broadcast television and other media as substitutes for the services provided to consumers by DirecTV and EchoStar. My point is not to endorse these market definitions as being factually accurate, but simply to observe that relevant antitrust markets in the media have traditionally been defined narrowly by the antitrust enforcement agencies, excluding from consideration outlets that surely are important competing sources of ideas and information.

The significance of the preceding point lies in the fact that relevant markets for ideas are likely much broader than corresponding economic markets as defined by the antitrust agencies. The hypothetical monopolist paradigm used to define relevant economic markets based on consumer response to a "small" price increase cannot be applied easily to the marketplace of ideas because it is difficult to identify the relevant prices. Merger Guidelines at _____. Even if the paradigm could be applied, the hypothetical monopolist test is too demanding in the context of ideas. What really matters with ideas from a political perspective is whether they can be suppressed. But given the importance of interpersonal communication, it is extremely difficult to suppress ideas—they can "leak out" even through small or economically minor media outlets. That most consumers form opinions based on information derived from mass media through the intermediation of others, rather than directly, has been a central tenet of mass media research for more than half a century.[23]

A relevant question, therefore, is whether alternative sources are or would be available if the media identified as being "in the market" were to suppress an idea or class of ideas. This test would inevitably produce a broader market than the traditional economic market. While DOJ might exclude, say, newspaper advertising from the relevant economic market in its analysis of a local radio station merger, it would make no sense to say a hypothetical monopolist of all radio stations could succeed in depriving consumers of some idea or information.[24] All outlets, regardless of their technology, would have to be included in the hypothetical monopoly in order to suppress an idea. As noted above, each outlet that can reach a given audience has the capacity to make any given idea available to that audience, regardless of the outlet's previous popularity.

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23 Katz and Lazarsfeld, Personal Influence (1955).

24 I do not mean to suggest that the DOJ staff is correct, as a technical matter, in excluding newspaper advertising from the relevant market for radio mergers. [I think this caveat is needed, but it raises some tension—if DOJ is not correct that markets are so narrow, then a more enlightened DOJ may define markets in a way that is no longer comfortably narrower than the appropriate market for ideas.]

Even if the foregoing argument is rejected, markets for ideas are much less concentrated than corresponding relevant economic markets because of the way that their respective concentration should be measured. When concentration is measured using revenue, a market with firms of unequal size will inevitably have higher concentration than a market with the same number of firms all of equal size. In markets for ideas, each firm is just one more source, and should count equally. The smallest level of concentration that could exist among a given number of firms is, by definition, the level associated with an equal market share for each firm.

Finally, entry into the marketplace of ideas often is easier than into the associated economic markets. In many advertising and other economic media markets the minimum scale at which an outlet is viable is not trivially small. Even the weakest low power TV or AM radio station needs a transmitter and an antenna. But politically, socially or otherwise significant information can enter the marketplace of ideas through a single web site, newsgroup or chat room and be disseminated extremely widely among the community. The classic example is Matt Drudge's web site, which broke the Monica Lewinsky story.

It follows from the preceding argument that antitrust merger enforcement in economic markets for advertising and other media services will tend to stop ownership concentration long before it becomes a threat to competition in the broader marketplace of ideas. Moreover, even if the Commission believed, erroneously, that the popularity of a given medium should be given weight in assessing competition in the marketplace of ideas, antitrust enforcement already accomplishes this. Outlets with large advertising or revenue market shares are very likely to be the most popular media. If the Commission sought to weight media by their popularity, it would once again end up duplicating the work of antitrust enforcers.

IV.
Conclusion

If the Commission sought to adopt ownership rules in order to protect advertisers or program vendors from the market power consequences of excessive media ownership concentration, it could not do better than to adopt the conceptual framework of modern industrial organization economics. This framework is imbedded in the Merger Guidelines, and it is already employed by the antitrust agencies in their scrutiny of media mergers. Thus, if the Commission adopted the most rational available basis for its media ownership rules, it would simply duplicate the work already performed by DOJ. This obviously would be wasteful of public and private resources.

The Commission has a better claim to adopt ownership rules in order to protect consumers from the threat of ideas being suppressed through the exercise of power in the marketplace of ideas. The Guidelines framework also can be applied effectively to this problem. It becomes apparent when that is done that concentration among the sources of or outlets for ideas and information available to a given audience will necessarily be less than concentration in the corresponding markets for advertising or programming. Therefore, merger review of relevant economic markets conducted by the antitrust agencies will ensure even greater competition in the marketplace of ideas. Given this relationship, the Commission lacks a basis to extend or adopt ownership rules on either economic or diversity grounds.