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Jamillia Ferris & Amanda Wait[1]

I. INTRODUCTION

On February 13, 2014, Comcast announced that it had entered into a definitive agreement to acquire Time Warner Cable for more than $45 billion. Concurrent with the announcement of the deal, Comcast executives publicly touted the transaction's efficiencies, including a larger and more efficient national platform that would benefit from economies of scale and scope. Almost as quickly, competitors, consumers, and legislators began expressing concerns about the combination. Since that time, both the Antitrust Division of the Department of Justice ("DOJ") and the Federal Communications Commission ("FCC") have confirmed reviews of the transaction—DOJ under an antitrust/consumer welfare standard and FCC under a "public interest" standard, which also considers competitive effects of the transaction.

Much of the initial reaction to, and criticism of, the proposed transaction has focused on the post-merger size of the combined company in terms of the number of subscribers. However, as Comcast was quick to note, while Comcast and Time Warner both serve pay television and broadband internet customers, they do not compete with each other for customers in any of the same zip codes anywhere in the United States.

Given this absence of a horizontal overlap in the companies' existing distribution footprints, the DOJ and FCC (the "agencies") likely will focus their reviews of potential anticompetitive effects from the proposed merger on how the expansions of the pay television and broadband networks affect Comcast's incentives in dealing with content providers, i.e. a bargaining theory analysis. Since 2011, Comcast has controlled pay television and broadband internet distribution networks, as well as access to NBC Universal content (such as NBC, CNBC, and The Weather Channel, among others), making it both a competitor to—and upstream distributor for—other content providers.

The agencies likely will consider the effect of Comcast's expanded pay television network (after the merger) on Comcast's leverage in future negotiations with downstream content providers. In addition, the agencies likely will investigate whether the expansion of Comcast's broadband network increases its incentive and ability to thwart competition and stymie innovation by competitor Online Video Distributors ("OVDs") such as Netflix and Amazon Prime.

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II. LEVERAGE VIS-À-VIS CONTENT PROVIDERS

Pay television is a two-sided market with content providers on one side, providing content to distributors Time Warner and Comcast, among others, and with consumers purchasing such content from distributors on the other side. In pay television, Comcast's existing regional cable monopolies give it negotiating leverage vis-à-vis content providers. While alternate means of content distribution exist, such as satellite and internet-based options, cable networks remain essential for many consumers. Thus, an analysis of the competitive effects of the Comcast/Time Warner acquisition should include an investigation of whether Comcast's increased pay television network will affect its bargaining with competing content providers, and how that change in bargaining leverage will affect pay television subscribers.

However, leverage is a two-way street, as content providers may also have leverage in negotiating with the networks that carry their content. A content provider's negotiating power is determined by its ability to produce and offer an attractive package consisting of TV channels, television shows, and/or movies. For example, the more attractive the content package to consumers, the more consumers might cancel their Comcast pay television subscriptions if that package does not appear in Comcast's cable line-up, creating more leverage for the content provider in its negotiations with Comcast.

Such a theory is suggested by CBS's pricing dispute with Time Warner in late 2013 in which CBS withheld its content as a means of leveraging its negotiating power against Time Warner. Time Warner reportedly lost over 300,000 subscribers during that period and conceded to CBS's demands. A similar dispute was reported between the AMC Network, whose content includes popular TV shows such as *Mad Men* and *Breaking Bad,* and the satellite distribution provider Dish Network.

For the purpose of the competition review, a bargaining theory analysis would require the agencies to determine whether Comcast/Time Warner and content providers are more likely to come to a mutual agreement after the merger than before. As a broader pay television subscriber network could affect both sides of the bargaining dynamic, the analysis would need to answer two questions: (i) whether the broader distribution network would make it more profitable for Comcast to discriminate in favor of its own content, and (ii) whether Comcast's increased cable or broadband scope makes its distribution network more indispensable to content providers, forcing these providers to accept lower licensing fees.

For example, Comcast may have more to gain from discriminating against competing content providers if the result is its own NBCU content gaining a broader audience; but may also risk losing a larger number of subscribers if it excludes competing provider content from its pay television network. Content providers also may have more to gain (in the form of increased subscriber access to their content) and more to lose (in the form of an increased number of subscribers precluded from their content) when negotiating with the combined Comcast/Time Warner.

Aviv Nevo, DOJ's Deputy Assistant Attorney General for Economics, discussed this general bargaining theory in a recent speech at the Stanford Institute for Economic Policy

Research and the Cornerstone Research Conference on Antitrust in Highly Innovative Industries.[2] He explained that bargaining leverage should be measured by the factors that change the likelihood of agreement relative to disagreement. The important factors are the negotiating parties' bargaining power and leverage. Influencing the analysis are consumer preferences, market structure, the relative value of various content, and the documents and data provided by the parties and by third-parties during the course of the agencies' investigations. A merger will be neutral or pro-competitive if the value of an agreement, relative to the value of a disagreement, either remains steady or increases.

Whether the combined Comcast/Time Warner could exert bargaining leverage over content providers was a topic of discussion during the Senate Judiciary Committee hearings on the proposed merger which took place on April 9. This further underscores the importance of these considerations during antitrust review.

III. DEALING WITH COMPETING OVDS

Also relevant to the agencies' antitrust analysis is whether the combined company's expanded broadband network changes Comcast's incentives in dealing with OVDs. Broadband connections are essential to the emerging OVD industry. OVDs, such as Netflix and Amazon Prime, compete with Comcast and Time Warner's cable networks as well as with Comcast's and Time Warner's own OVD services. At the same time, OVDs rely on Comcast and Time Warner to transmit OVD content to consumers via high-speed, broadband internet.

Thus, whether or not the proposed Comcast/Time Warner merger increases the combined company's incentive and ability to harm the growth of OVD providers is an important consideration as the agencies investigate the proposed transaction. The agencies likely will consider whether Comcast would have an incentive (or an increased incentive) to discriminate against competing content being transmitted over its broadband internet network. Indeed, commentators have expressed concern that Comcast may slow the transmission speed of competing OVDs in order to encourage customers to switch to Comcast's own OVD programming or its pay television network.

Concerns about changing incentives resulting in bottlenecks to customer access to content and diminished OVD innovation were at the core of the conditions Comcast agreed to in order to secure the agencies' approval of its acquisition of control over NBCU content in 2011. That transaction resulted in the vertical integration of NBCU content and Comcast pay television and broadband distribution.

The agencies ultimately cleared the transaction but only after Comcast agreed to certain commitments and restrictions on future conduct. Comcast agreed to license the NBCU content and programs to OVDs in a non-discriminatory manner and at a reasonable price and to relinquish its management rights in the NBCU-controlled OVD services Hulu and Hulu Plus.

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[2] Aviv Nevo, Deputy Assistant Att'y Gen. for Economics, Antitrust Div., Dep't of Justice, Remarks at the Stanford Institute for Economic Policy Research and Cornerstone Research Conference on Antitrust in Highly Innovative Industries: Mergers that Increase Bargaining Leverage (Jan. 22, 2014).

The obligations arising from the DOJ and FCC review of the Comcast/NBCU transaction will remain in effect until 2018 and Comcast has publicly conceded that these existing obligations will apply to Time Warner if the current deal is approved. Whether or not that extension is sufficient to remedy any of the agencies' concerns about the Time Warner transaction and its effect on OVD competition remains to be seen.

IV. CONCLUSION

Although the outcome of the DOJ's and FCC's reviews of the proposed acquisition of Time Warner by Comcast remains uncertain, the antitrust review will require a detailed analysis of market dynamics derived from documents and substantial data produced to the agencies by Comcast, Time Warner, and many third parties. Any change in Comcast's incentives to bargain and deal with its downstream rivals through the expansion of its pay television and broadband internet distribution networks will be important to this analysis. The predicted outcome of those future negotiations based on Comcast's new network positions will include assessments on the effect on consumers—and could be central to the agencies' ultimate conclusion.

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